



30th June, 2020

To,

Mr Yogesh Dayal
Chief General Manager
Reserve Bank of India

Sub: Representation and comments on the Draft Directions on Securitisation of Standard Assets and Sale of Loan Exposures

Sir,

This is with reference to the Press Release dated June 08, 2020¹ issued by the Reserve Bank of India, inviting comments on “Draft Framework for Securitisation of Standard Assets” and “Draft Comprehensive Framework for Sale of Loan Exposures”, seeking comments and responses to the discussion questions provided in the draft frameworks by 30th June, 2020.

We, Indian Securitisation Foundation, on behalf of the securitisation and structured finance industry in India, prepared a draft of recommendations and circulated among the stakeholders. Subsequently, we organised an online panel discussion on 25th June, 2020, to discuss the suggestions collated from the industry and decide on the final set of representations to be made to the RBI.

The said meeting was attended by various stakeholders including lawyers, representatives of bankers, NBFCs, structured finance consultants, accounting firms, credit rating agencies. Based on the discussion and feedback received from various stakeholders, we hereby submit our comments on the each of the above mentioned draft frameworks.

Our comments on the ‘Draft Framework for Securitisation of Standard Assets’ have been annexed as “Annexure A”.

Our comments on the ‘Draft Framework for Sale of Loan Exposures’ have been annexed as “Annexure B”.

About Indian Securitisation Foundation

¹ https://www.rbi.org.in/Scripts/BS_PressReleaseDisplay.aspx?prid=49920

INDIAN SECURITISATION FOUNDATION

(A Not-For-Profit Company Licensed under Section 25 of Companies Act, 1956)

Corporate Identity Number: U65923MH2013NPL242178

Regd. Office: 403 – 406, 175 Shreyas Chambers, D.N. Road, Fort, Mumbai – 400 001, India

Phone: 022 – 22614021 Website: www.indiansecuritisation.com

Email: info@indiansecuritisation.com



ISF is a not-for-profit entity representing the securitisation industry in India. The membership of the Foundation includes banks, NBFCs, microfinance institutions, other issuers and investors and securitisation professionals for promoting interest of securitisation and fixed income securities in India.

Typical investors in securitisation include public sector banks, private sector banks, mutual funds, insurance companies and others. The insurance companies find AAA rated fixed income security with higher spreads particularly attractive and world-over insurance companies are significant investors in securitisation transactions.

As ISF is dedicated to the cause of promoting securitisation in India, we humbly submit our representation herein below on permitting insurance companies to invest in all securitised instruments.

Should there be any comments/ queries in this regard, please reach out to us.

Thanking you,

Yours truly,

For *Indian Securitisation Foundation*

Vinita Nair

Director

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Annexure A: Comments on Draft Framework for Securitisation of Standard Assets

Clause	Content	Our comment/ representation/ clarification sought
	Risk weight of the securitisation exposure having lowest rating or highest degree of risk	<p>At several places, the risk weight assigned to the most risky class of securitisation exposure at 1250%. In India, banks are required to maintain capital at the rate 9% and NBFCs are required to maintain capital at the rate of 15%. For HFCs, the capital requirement has been increased in a phase manner.</p> <p>Therefore, the highest risk weight to the most risky class of securitisation exposure should be computed based on 1/regulatory capital required. Accordingly, the risk weights assigned to other tranches should also be appropriately changed.</p>
4	These directions, will be applicable to securitisation transactions undertaken subsequent to the issue of these directions. The provisions of Chapter VI and VII shall come into immediate effect, even for the existing securitisation exposures.	<p>Clause 4 makes the provisions relating to capital relief and disclosure requirements applicable on existing transactions.</p> <p>The conditions for capital relief are new, and most of the existing transactions will fail to satisfy these. As a result, most of the originators will be denied capital relief, for something, which they were unaware of, at the time of structuring of the transactions.</p> <p>It is represented that for implementation of provisions relating to capital relief on existing transactions a longer timeframe may be granted, otherwise, it can have an adverse impact on the capital.</p>
5(i)	"first loss facility" means the first level of financial support provided by the originator or a third party to	<p>1. The support provided need not be to the SPE, even if the support is at the originator level, it is still a first loss support. Accordingly, the</p>

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	a special purpose entity as part of the process to improve the creditworthiness of the securities issued by the SPE such that the provider of the facility bears the bulk (or all) of the risks associated with the assets held by the SPE.	<p>words “to a special purpose entity” may be removed.</p> <p>2. The definition states that the first loss facility should cover the bulk (or all) of the risks associated. The diversification of risk in a securitisation transaction can be achieved even with multiple layers of tranching. In such a situation, the first loss tranche need not always cover up the bulk (or all) of the risks associated. Ideally, for the first loss tranche, expected losses should be taken as a basis, and any other losses can be absorbed in one or more tranches, superior to the first loss tranche.</p> <p>3. For the purpose of clarification, the term ‘first loss facility’ may be redefined to include ‘first loss tranche’ and ‘first loss position’ to ensure uniformity.</p>
5(n)	“notes” mean securities issued by the special purpose entity as a part of securitisation;	In practice, notes are not securities. Usually promissory notes or short term notes are referred to as notes. The term “certificates”, “units” or “securities” may be used instead.
6	All on-balance sheet standard exposures, except the following, will be eligible for securitisation by the originators: <ul style="list-style-type: none"> a. Revolving credit facilities (e.g. Cash Credit accounts, Credit Card receivables etc.); b. Loans with bullet repayments of both principal and interest; and c. Securitisation exposures 	It can be clarified that whether these transaction are completely prohibited or can be undertaken without any capital relief.

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5(u)	<p>“securitisation” means the set of transactions or scheme wherein credit risk associated with eligible exposures is tranching and where payments in the set of transactions or scheme depend upon the performance of the specified underlying exposures as opposed to being derived from an obligation of the originator, and the subordination of tranches determines the distribution of losses during the life of the set of transactions or scheme;</p> <p>Provided that the pool may contain one or more exposures eligible to be securitised;</p>	<p>The definition when read along with the ‘Salient Features’ provided in the 'Brief Summary note treats only multiple tranche structures as securitisation transactions. However, a majority of the securitisation transactions at present have a single tranche structure. Either the definition needs to be modified to include even single tranche structures or else it has to be clarified on which guidelines to follow for such structures. The rationale for mandatory credit tranching is unclear, and especially so for single loan securitisation structures where all tranches could be exposed to the same risk.</p>
8	<p>If the underlying exposures comprise of bank loans, lenders can securitise the loans only after a minimum holding period counted from the date of full disbursement of loans for an activity/purpose; acquisition of asset (i.e., car, residential house etc.) by the borrower or the date of completion of a project, as the case may be.</p>	<p>We understand that the idea here is to consider loans, however, the clause refers to “bank loans”. This may be amended to “loans” so as to cover loans extended by all types of financial institutions whether or not covered under these Directions.</p> <p>Further, the meaning of the term “acquisition of asset” may be clarified, as the term acquisition have many different meanings. For example, in case of residential mortgage loans, the acquisition of asset could mean taking over physical possession of asset or execution of sale deed or completion of the project etc.</p> <p>As is usually referred to commercially, acquisition of asset refers to full disbursement of credit facilities. The same should be appropriately incorporated in the clause.</p>

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13	Lenders in India, including overseas branches of banks in India, are not permitted to undertake the securitisation activities or assume securitisation exposures such as synthetic securitisation	<p>World over synthetic transactions are making come back. European regulators are also considering to bring back synthetic transactions. In USA, synthetic structures are very common in case of RMBS transactions. The adverse perception about synthetic transactions corresponds to 2007 crisis, most of which have been taken care off by way of regulations issued thereafter.</p> <p>Hence, RBI may consider allowing synthetic transactions in the Indian market.</p>
16	<p>The MRR may be maintained by the lenders in either of the following ways:</p> <p>a. the retention of the first loss tranche and, where such retention does not amount to the MRR, other tranches which are <i>pari passu</i> or subordinate to those transferred or sold to investors and not maturing any earlier than those transferred or sold to investors, including a second loss exposure, if any, so that the total retention equals not less than MRR; or</p> <p>b. the retention of the first loss tranche and, where such retention does not amount to the MRR, the retention of a first loss exposure of not less than MRR of every securitised exposure in the securitisation so that the total</p>	<p>Clause 16(a) is broad enough, there is no need 16(b).</p> <p>In any case there is no practical concept of first loss exposure other than first loss tranches.</p> <p>Additionally, other support in the form of cash collateral or overcollateralization may be included in the definition of first loss exposure.</p> <p>Therefore, clause 16(b) may be removed.</p> <p>Further, there is a clear contradiction between clause 16 and clause 79(a)(ii), which states:</p> <p><i>In cases where there are no mezzanine securitisation positions, the originator does not hold more than 20% of the exposure values of securitisation positions that are first loss positions.</i></p> <p>On one hand, clause 16 indicates that the first loss tranche should be retained as MRR, on the other hand, clause 79(a)(ii) states that in order to</p>

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	retention equals not less than MRR.	achieve capital relief, the originator should not hold more than 20% of the first loss tranche. A clarification in this regard may be provided.
28	If the value of the exposures underlying a residential mortgage backed securitisation is Rs.500 crore or above, the securities issued must be mandatorily listed. For securities issued in residential mortgage backed securitisations where the value of the exposures underlying is less than Rs.500 crore, and securities issued in other securitisation transactions, listing of the securities or notes is optional.	Please clarify if the amount of Rs. 500 crores will include loans offered as over-collateralisation as well. There were different views on this and some stakeholders did not vote in favour of the listing to be mandatory. They contended that listing should be made optional, and should be driven by the demand from the investors. For instance, if the investors are mutual funds, the securities will have to be listed mandatorily, as they are prohibited to invest in unlisted debt securities. Whereas, if the investor is a bank, then there is really no merit for getting transaction listed.
29 (e)	If the SPE is set up as a trust, then: iv. The trustee, if any , should only perform trusteeship functions in relation to the SPE and should not undertake any other business with the SPE.	Clause 29(e) deals with cases where SPEs are set up as trust. However, in sub-clause (iv), the words "if any" are redundant, since, a trust cannot function without trustee. Therefore, the aforesaid words may be removed.
30	In cases where the originator has purchased loans from another lender for the purpose of securitisation, the provisions of clause 29 shall apply to the lender from whom the originator has purchased the exposures, as well	Usually, origination or acquisition of loans for the sole purpose of securitisation is discouraged. However, if the intention of this clause is create an exemption for government promoted platform(s) created for promoting securitisation in the country, then the same may be expressly said so in the clause. For example, the Dr. Harsh Vardhan Committee report contemplates NHB to set up platform

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		exclusively for securitisation; there must be a clear exception for such a platform.
33	Any loss, profit or premium arising because of the sale, which is realised, should be accounted accordingly and reflected in the Profit & Loss account for the accounting period during which the sale is completed. However, profits / premium, if any, arising out of such sales, shall be deducted from CET 1 capital or net owned funds for meeting regulatory capital adequacy requirements till the maturity of such assets	The conditions prescribed here conflicts with the provisions laid down in Ind AS 109. Therefore, there is a need for a specific carve out from these conditions where the seller is required to prepare financial statements as per Ind AS. Further, it must be clarified that the gain to be deducted from the capital should be after considering the impact of taxation on the gain.
34	Banks should not recognise the unrealised gains in Profit and Loss account; instead they should hold the unrealised profit under an accounting head styled as “Unrealised Gain on Loan Transfer Transactions”.	Same as above.
39	Only traditional securitisations that additionally satisfy all the criteria laid out in Annex 1 of these directions fall within the scope of the STC framework. The above criteria are based on the prescriptions of the Basel Committee on Banking Supervision. Exposures to securitisations that are STC-compliant can be subject to the alternative capital treatment as determined by clauses 112 to 114 or clauses 127 to 128.	The draft framework does not permit synthetic securitisations, hence, the use of words “only traditional securitisations” seems unnecessary. Hence, the same may be removed.

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48(c)	The amount of credit enhancement extended at the initiation of the securitisation transaction should be available to the SPE during the entire life of the securities issued by the SPE.	There is no reason to compel the credit enhancement to be available for the entire tenure of 'all' the securities issued by the SPV. For example, a guarantee or a cash collateral provided specifically for a senior tranche and not for mezzanine and junior is perfectly fine. Therefore, credit enhancement extended to a particular class of security should be maintained only till the life of that particular security.
78	All securitisation exposures, which are not covered by these directions, or which do not satisfy the conditions prescribed in these directions, or which has exposures originated by an entity which is not a lender as referred to in clause 3, shall be risk weighted at 1250%.	The provision of 1250% risk weight for securitisation exposure not covered by this guideline will precludes Bank/NBFCs to invest into PTCs issued by non-financial sector entities. For example, there has been several recent issuances of PTCs backed by mobile phone lease receivables or service contracts, listed as per the SEBI guidelines. The RBI should prescribe rating based capital requirement for those transactions. Moreover, this clause should specifically be applicable on such transaction that are falling within the guidelines but have not complied with the requirements laid therein.
79(b)	The nominal value of the total first loss positions available to a securitisation is not less than the product of the following: (i) exposure value of the underlying exposures; (ii) weighted average life of the underlying exposures; and (iii) weighted average asset-class slippage ratio of the	Usually, banks and financial institutions in India compute life time expected losses for the pool of loans assigned or securitised. Therefore, it will be appropriate of the thickness of the first loss position is pegged with lifetime expected losses of the asset(s) instead of the slippage ratio.



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	underlying exposures in the past one year. The originator does not maintain direct or indirect control over the transferred exposures. Specifically, the originator should not be able to repurchase the transferred exposures unless it is done through invocation of a clean-up call option. Also, there should not be any obligation on the originator to retain the risk of the transferred exposures.	
	Rating Requirement	The existing guidelines specify that the securities issued by the SPV shall compulsorily be rated by a rating agency, which is not explicitly covered in the proposed guidelines and could be added.

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Annexure B: Comments on Draft Framework for Sale of Loan Exposures

Clause	Content	Our comment/ representation/ clarification sought
4	These directions will be applicable to all loan sales, including sale of loans to special purpose entities for the purpose of securitisation , undertaken subsequent to the issue of these directions.	The guidelines should not be applicable for sale of loans to special purpose entities for the purpose of securitisation as there are separate guidelines being prescribed for the same. Requisite provisions may be inserted to the draft Framework on Securitisation, to make it complete.
5(j)	“stressed assets” mean assets that are classified as NPA or as special mention account, and generally includes accounts which are in default as well as where lenders have given concessions for economic or legal reasons relating to the borrower's financial difficulty	<p>The definition of stressed assets includes NPAs as well as special mention accounts. Further, clause 28 specifically excludes sale of stressed assets from the purview of the provisions relating to standard assets.</p> <p>Technically, special mention accounts are also standard, and becomes sub-standard only when account becomes NPA.</p> <p>Of the different types of SMAs, SMA-0 captures such assets where the default in payment is for a period of 0-30 days. The definition of SMA was changed lately to include default in payment for a period of 0-30 days, however, before the change, the regulations required classification of an account as SMA-0 only when the account showed signs of incipient stress.</p> <p>We understand the change in definition of the SMA-0 was mostly for reporting purposes, however, using the same meaning for the purpose of sell of such assets and treating them at par with SMA-1, SMA-2 and NPA cases is not appropriate.</p> <p>Therefore, accounts becoming SMA-0, only by virtue of delay in payment for a period of 0-30</p>

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		days, without showing signs of incipient stress, may be excluded from the definition of “stressed assets” and be treated at par with “standard” assets.
5(l)	“transferee” means the entity to which the economic interest in a loan exposure is transferred under these directions, and wherever appropriate, may include grantors under a loan participation transaction;	The term “transferee” includes “grantor”. Grantor is defined to mean: <i>“grantor” means the entity in whose books the loan exposure transferred through a loan participation agreement resides;</i> It should refer to “participant” instead of “grantor”.
5(m)	“transferor” means the entity which transfers the economic interest in a loan exposure under these directions, and wherever appropriate, may include participants under a loan participation transaction.	The term “transferee” includes “participant”. Participant is defined to mean: <i>“participant” means the entity to which the grantor transfers its interest in a loan exposure, fully or partly, through a loan participation transaction;</i> It should refer to “grantor” instead of “participant”.
9	A loan sale should result in immediate legal separation of the transferor from the assets which are sold to the extent that the interest has been transferred . The transferred interest should stand completely isolated from the transferor, after its transfer to the buyer, i.e., put beyond the transferor’s as well as its creditors’ reach, even in the event of bankruptcy of the transferor. In case of any retained interest in the	This highlighted text in clause 9 contradicts the definition of “transfer” in clause 5(k) – <i>“transfer” means a transfer of economic interest in loan exposures in the manner prescribed in these directions, and includes loan participations and transactions in which the loan exposure remains on the books of the transferor even after the said transaction.</i> The definition of transfer is wide enough to cover transfer of economic interests, with or without legal transfer of the receivables.

Clause	Content	Our comment/ representation/ clarification sought
	exposure by the transferor, the loan sale contract should clearly specify the distribution of the interest income from the transferred asset among the transferor and the transferee.	<p>However, clause 9 provides for immediate legal separation of assets which are sold.</p> <p>Further, at several places, the term “loan sales” has been used. In this regard, it should be clarified at the provisions relating to loan sales shall apply only in case of legal sale of assets, and not in case of economic transfer of risks by any other means.</p>
13	The transferee shall, wherever applicable, ensure that the security interest, if any, underlying the loans purchased are properly registered, with the transferee as the beneficiary, directly or indirectly, and a mechanism for timely invocation of such interest, if the need arises, is properly documented and put in place.	<p>Usually, in case of direct assignment or securitisation transactions, the underlying security interests in loans transferred are retained by the originator itself, however, it holds it in trust for the transferee. This is done in order to avoid logistical inconvenience, with respect to, modification of charge documents etc.</p> <p>If implemented, this will create large scale logistical inconvenience with respect to modification charge documents, change of registration certificates (in case of motor vehicles loans), registration of mortgage etc.</p> <p>Further, these structures are also used on account of complicated stamp duty and registration laws which are different from state to state and that, unless those laws are made uniform for loan sale transactions / securitisations, there does not appear to be any merit in requiring the transfer of security interest upfront.</p> <p>Therefore, this condition may be reconsidered.</p>
17	Lenders can purchase external commercial borrowings lent by eligible ECB lenders provided that	Clarification is sought on whether this clause will apply only when there is a transfer of loan between eligible lenders.

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	the losses / haircuts, if any, occurring to the transferors on account of the loan sale should not be passed on to the transferees, and instead should be booked in the accounts of the transferors.	
28	The provisions of this Chapter do not apply to: a. ** b. ** c. trading in bonds;	At several places, the term bond and debentures have been used together. Hence, this may be clarified to include debenture as defined under the Stamp Act or the Companies Act.
35	Transferors can transfer loans only after a minimum holding period counted from the date of first repayment of loans for an activity/purpose; date of acquisition of asset (i.e., car, residential house etc.) by the borrower for which the financing had been extended; or the date of completion of a project financed by the loan, as the case may be, whichever is later . The minimum holding period that would be applicable depending upon the tenor and repayment frequency is given in the following table: XX Provided that where the repayment is at more than quarterly intervals, loans can be transferred after repayment of at-least two instalments.	i. The earlier provisions counted the MHP from the date of disbursal. The proposition for considering the date of first repayment of loan or acquisition or completion date, whichever is later may extend the MHP requirement in real terms. Therefore, this should be realigned to be in line the MHP requirements in the draft framework for Securitisation of Standard Assets. ii. The clause on minimum holding period with respect to sale of loans other than to SPEs for securitisation does not allow the relaxation granted to residential loans in case of securitisation transactions. Unless the intention is to disincentivise sale of residential mortgage loans and incentivise securitisation of mortgage loans, the same relaxation may be extended here as well.

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	Provided that in case of loans purchased from other entities by a transferor, such loans cannot be sold before completion of twelve months from the date on which the loan was taken to the books of the transferor.	
38	Any loss, profit or premium arising because of a sale, which is realised, should be accounted accordingly and reflected in the Profit & Loss account for the accounting period during which the sale is completed. However, profits / premium, if any, arising out of such sales, shall be deducted from CET 1 capital or net owned funds for meeting regulatory capital adequacy requirements till the maturity of such assets.	The conditions prescribed here conflicts with the provisions laid down in Ind AS 109. Therefore, there is a need for a specific carve out from these conditions where the seller is required to prepare financial statements as per Ind AS.
50	The transferors shall sell stressed assets to any regulated entity that is permitted to take on loan exposures by its statutory or regulatory framework . The transferee in the case of stressed assets need not be a financial entity.	The draft regulations considers a non-financial entity as an eligible borrower. However, there is no clarity in terms of who can be a regulated non-financial entity. A clarification in this regard is sought.
68	Lenders are free to receive cash or bonds or debentures or security receipts (SRs) or pass-through certificates (PTCs) as sale consideration for the financial assets sold to ARC. Bonds/debentures/SRs/PTCs	In case of sale to ARC, the sale consideration should not include PTCs issued by an SPV. Trusts created by ARCs do not issue PTCs, instead they issue SRs.



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	received by lenders as sale consideration towards sale of financial assets to ARC shall be classified as investments in the books of the lenders.	

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