CEIOPS Advice for Level 2 Implementing Measures on Solvency II:
Repackaged Loans Investment

(former Consultation Paper 63)
Table of contents

1. Introduction ................................................................................................... 3
   1.1. Background ............................................................................................... 3
   1.2. Scope of this Advice ................................................................................... 4
2. Extract from the Level 1 text .......................................................................... 6
   2.1. Extracts from the Solvency II Level 1 text ................................................ 6
   2.2. Extract from legal provisions applicable to credit institutions ................. 8
       2.2.1. Definitions from the Basel II Accord to the CRD implementation throughout
       the EU – Article 4 ......................................................................................... 8
       2.2.2. Extract from the Capital Requirements Directive (CRD) .................... 9
3. Advice........................................................................................................... 15
   3.1. Purpose ...................................................................................................... 15
   3.1.1. Definitions ............................................................................................ 16
   3.2. Principles .................................................................................................. 16
       3.2.1. Principles relating to Article 135(2a) ............................................... 17
       3.2. Principles relating to Article 135(2b) .................................................... 20
       3.2.3. Breach of requirements .................................................................... 23
   3.3. Grandfathering ........................................................................................ 24
1. Introduction

1.1. Background

1.1. In its letters of 19 July 2007 and 12 June 2009, the European Commission requested CEIOPS to provide final, fully consulted advice on Level 2 implementing measures by February 2010 and recommended CEIOPS to develop Level 3 guidance on certain areas to foster supervisory convergence.

1.2. This Paper aims at providing advice for Level 2 measures with regard to investments in tradable securities and other financial instruments based on repackaged loans as required by Article 135 of the general approach on the Solvency II Directive1 ("Level 1 text"). The aim of the implementing measure is to ensure cross-sectoral consistency in the requirements for financial institutions and remove any potential misalignment of interests between the originators (the companies issuing the financial instrument) and investors in such financial instruments.

1.3. One of the causes of the present instability in the financial markets is the repackaging of debt securities and the distribution of these investments throughout the financial markets2. Whilst the repackaging of debt in itself is not inherently risky the function of passing debt to a third party gives rise to the hazard that the originator can issue loans knowing that their debt will be repackaged and sold as an asset backed security to a third party. This removes the credit risk from the issuing organisation and so the originator often has little interest in writing 'good' risks.

1.4. The misalignment of interest that Article 135(2) is referring to is the situation where originators provide a loan and, because they know they will be able to securitise the debt - removing their credit risk from their balance sheet - the loan is not made in their best business interest. If investors know the quality of the loans being securitised they can make an informed decision whether to invest in them – this has often not happened. Better transparency would make the originators and the investors’ interests more aligned and allow the investors to make a more informed investment decision.

1.5. To reduce the potential moral hazard introduced by the reselling of debt, originators are required to disclose details of the risks they are repackaging. Article 135(2a) of the Level 1 text requires implementing measures to lay down the requirements that need to be met by the originator before an undertaking3 is allowed to invest in the securities it issues. Article 135(2b) also includes the qualitative requirements that

---

3 By "undertaking" CEIOPS is referring to (re)insurance undertakings throughout the Paper.
must be met by an undertaking that invests in these securities or instruments.

1.6. CEIOPS’ advice on setting the requirements for investing in those products should take into account the regulations for credit institutions and certain investment undertakings as part of the amendments to the Capital Requirements Directive (CRD)\(^4\) since it is crucial that the requirements between financial sectors are similar to avoid situations where a certain repackaged loan is an “eligible asset” in one sector but not in another.

1.2. Scope of this Advice

1.7. Article 135(2) of the Level 1 text is only concerned with the repackaging of loans into tradable securities and other financial instruments that effectively transfer credit risk from originators to investors. It is worth noting that, depending upon the economic substance, those tradable securities and other financial instruments whose underlying exposures are liabilities\(^5\) issued by an originator (or originators in the case of multi-seller structures) with the intention of raising funds and which do not transfer credit risk are out of the scope of this advice. CEIOPS intends this definition, and the exemptions, to be consistent with the CRD and proposes to deal with specific exemptions from this advice as they arise on a case-by-case basis.

1.8. This advice does not deal with the effect on the quantitative requirements for undertakings (e.g. SCR) as a result of the purchase of tradable securities and other financial instruments based on repackaged loans as this issue is out of the scope of Article 135(2b) of the Level 1 text.

1.9. It should be noted that the Directive requirements could potentially be very restrictive:

- Article 135(2a) **prohibits** undertakings from investing in tradable securities and other financial instruments based on repackaged loans that do not meet the requirements as defined in the Level 2 implementing measures.

- Article 135(2b) **prohibits** undertakings from investing in tradable securities and other financial instruments based on repackaged loans if the undertaking does not meet the qualitative requirements.

1.10. If the requirements are not met, undertakings will not be permitted to invest in these products at all, rather than simply limiting the credit that can be taken for them or being subject to an adequate capital charge. Therefore it is important that the implementing measures are written in a way which enables undertakings to make sound and sensible investment choices but also ensures an appropriate regulatory regime is in place which maintains cross sectoral consistency with banking regulation.


\(^5\) This would include covered bonds, for example.
1.11. CEIOPS considers that this advice, though potentially very restrictive, is consistent with the prudent person principle. The requirements here are explicit for a specific type of financial product and the principles should apply in a proportionate manner to all investments made. As set out in Article 132, if undertakings consider that they are unable to properly identify, measure, monitor, manage, control and report the risks that they are exposed to through their investment then they should be making the decision not to invest in these products. As there have been significant risks with tradable securities and other financial instruments based on repackaged loans, the Level 1 text explicitly requires specific provisions to address those risks and CEIOPS has been asked by the European Commission to set out what requirements undertakings should need to fulfil for these specific products. Proportionate assessments should be made by undertakings in advance of any investment decision, not just in relation to tradable securities and other financial instruments based on repackaged loans.

1.12. It is also important to note that this advice is different from almost every other Directive implementing measure as the relevant article refers to the criteria that are required to be met by the originator who could potentially be an unregulated third party (e.g. non-financial company issuing securities) before an undertaking is allowed to invest in those securities or instruments issued after 1 January 2011.
2. Extract from the Level 1 text

2.1. Extracts from the Solvency II Level 1 text

2.1. Article 135 (Implementing measures) of the Level 1 text reads:

1. In order to ensure the uniform application of this Directive, the Commission may adopt implementing measures specifying qualitative requirements in the following areas:

(a) the identification, measurement, monitoring, managing and reporting of risks arising from investments in relation to the first subparagraph of Article 132(2);

(b) the identification, measurement monitoring, managing and reporting of specific risks arising from investment in derivative instruments and assets referred to in the second subparagraph of Article 132(4);

2. In order to ensure cross-sectoral consistency and to remove misalignment between the interests of firms that “repackage” loans into tradable securities and other financial instruments (originators) and the interests of insurance or reinsurance undertakings that invest in such securities or instruments, the Commission shall adopt implementing measures laying down:

(a) the requirements that need to be met by the originator in order for an insurance or reinsurance undertaking to be allowed to invest in such securities or instruments issued after 1 January 2011, including requirements that ensure that the originator retains a net economic interest of no less than 5 per cent;

(b) qualitative requirements that must be met by insurance or reinsurance undertakings that invest in such securities or instruments.

3. Those measures, designed to amend non-essential elements of this Directive by supplementing it, shall be adopted in accordance with the regulatory procedure with scrutiny referred to in Article 301(3).

2.2. Article 132 (“Prudent person” principle) of the Level 1 text reads:

1. Member States shall ensure that insurance and reinsurance undertakings invest all their assets in accordance with the prudent person principle, as specified in paragraphs 2, 3 and 4.

2. With respect to the whole portfolio of assets, insurance and reinsurance undertakings shall only invest in assets and instruments whose risks the undertaking concerned can properly identify, measure, monitor, manage, control and report, and appropriately take into account in the assessment of its overall solvency needs in accordance with point (a) of the second subparagraph of Article 45(1).

All assets, in particular those covering the Minimum Capital Requirement and the Solvency Capital Requirement, shall be invested in such a manner as to ensure the security, quality, liquidity and profitability of the portfolio
as a whole. In addition the localisation of those assets shall be such as to ensure their availability.

Assets held to cover the technical provisions shall also be invested in a manner appropriate to the nature and duration of the insurance and reinsurance liabilities. Those assets shall be invested in the best interest of all policy holders and beneficiaries taking into account any disclosed policy objective.

In the case of a conflict of interest, insurance undertakings, or the entity which manages their asset portfolio, shall ensure that the investment is made in the best interest of policy holders and beneficiaries.

3. Without prejudice to paragraph 2, with respect to assets held in respect of life insurance contracts where the investment risk is borne by the policy holders, the second, third and fourth subparagraphs of this paragraph shall apply.

Where the benefits provided by a contract are directly linked to the value of units in an UCITS as defined in Directive 85/611/EEC, or to the value of assets contained in an internal fund held by the insurance undertakings, usually divided into units, the technical provisions in respect of those benefits must be represented as closely as possible by those units or, in the case where units are not established, by those assets.

Where the benefits provided by a contract are directly linked to a share index or some other reference value other than those referred to in the second subparagraph, the technical provisions in respect of those benefits must be represented as closely as possible either by the units deemed to represent the reference value or, in the case where units are not established, by assets of appropriate security and marketability which correspond as closely as possible with those on which the particular reference value is based.

Where the benefits referred to in the second and third subparagraphs include a guarantee of investment performance or some other guaranteed benefit, the assets held to cover the corresponding additional technical provisions shall be subject to paragraph 4.

4. Without prejudice to paragraph 2, with respect to assets other than those covered by paragraph 3, the second to fifth subparagraphs of this paragraph shall apply.

The use of derivative instruments shall be possible insofar as they contribute to a reduction of risks or facilitate efficient portfolio management.

Investment and assets which are not admitted to trading on a regulated financial market shall be kept to prudent levels.

Assets shall be properly diversified in such a way as to avoid excessive reliance on any particular asset, issuer or group of undertakings, or geographical area and excessive accumulation of risk in the portfolio as a whole.
Investments in assets issued by the same issuer, or by issuers belonging to the same group, shall not expose the insurance undertakings to excessive risk concentration.

2.3. Recitals 71 and 72 of the Level 1 text state:

(71) Insurance and reinsurance undertakings should have assets of sufficient quality to cover their overall financial requirements. All investments held by insurance and reinsurance undertakings should be managed in accordance with the "prudent person" principle.

(72) Member States should not require insurance or reinsurance undertakings to invest their assets in particular categories of assets, as such a requirement could be incompatible with the liberalisation of capital movements provided for in Article 56 of the Treaty.

2.2. Extract from legal provisions applicable to credit institutions

2.2.1. Definitions from the Basel II Accord to the CRD implementation throughout the EU – Article 4

2.4. “Securitisation” means a transaction or scheme, whereby the credit risk associated with an exposure or pool of exposures is tranched, having the following characteristics:

(a) payments in the transaction or scheme are dependent upon the performance of the exposure or pool of exposures; and

(b) the subordination of tranches determines the distribution of losses during the ongoing life of the transaction or scheme;

“Tranche” means a contractually established segment of the credit risk associated with an exposure or number of exposures, where a position in the segment entails a risk of credit loss greater than or less than a position of the same amount in each other such segment, without taking account of credit protection provided by third parties directly to the holders of positions in the segment or in other segments;

“Securitisation position” shall mean an exposure to a securitisation;

“Originator” means either of the following:

(a) an entity which, either itself or through related entities, directly or indirectly, was involved in the original agreement which created the obligations or potential obligations of the debtor or potential debtor giving rise to the exposure being securitised; or

(b) an entity which purchases a third party’s exposures onto its balance sheet and then securitisces them;

“Sponsor” means a credit institution other than an originator credit institution that establishes and manages an asset-backed commercial
paper programme or other securitisation scheme that purchases exposures from third party entities.

2.2.2. Extract from the Capital Requirements Directive (CRD)

2.5. Article 122a\(^6\) (Exposures to transferred credit risk)

1. A credit institution, other than when acting as an originator, a sponsor or original lender, shall only be exposed to the credit risk of a securitisation position in its trading book or non-trading book if the originator, sponsor or original lender has explicitly disclosed to the credit institution that it will retain, on an ongoing basis, a material net economic interest which, in any event shall not be less than 5%.

For this purpose, retention of net economic interest shall mean either:

a) retention of not less than 5% of the nominal value of each of the tranches sold or transferred to the investors; or

b) in the case of securitisations of revolving exposures, retention of originator's interest of not less than 5% of the nominal value of the securitised exposures; or

c) retention of randomly selected exposures, equivalent to not less than 5% of the nominal amount of the securitised exposures, where these would otherwise have been securitised in the securitisation provided that the number of potentially securitised exposures is not less than 100 at origination; or

d) retention of the first loss tranche and, if necessary, other tranches having the same or more severe risk profile and not maturing any earlier than those transferred or sold to investors, so that the retention equals in total not less than 5% of the nominal value of the securitised exposures.

Net economic interest is measured at the origination and shall be maintained on an on-going basis. It shall not be subject to any credit risk mitigation or any short positions or any other hedge. The net economic interest shall be determined by the notional value for off-balance sheet items.

For the purpose of this Article, "on-going basis" shall mean that retained positions, interest or exposures shall not be hedged or sold.

There shall be no multiple applications of the retention requirements for any given securitisation.

1a. Where an EU parent credit institution or an EU financial holding company, or one of its subsidiaries, as an originator or a sponsor, securitises exposures from several credit institutions, investment firms or financial institutions which are included in the scope of supervision on a

---

consolidated basis, the requirement referred to in the first subparagraph may be satisfied on the basis of the consolidated situation of the related EU parent credit institution or EU financial holding company. This paragraph shall only apply where credit institutions, investment firms or financial institutions which created the securitised exposures have committed themselves to adhere to the requirements set out in paragraph 5 and deliver, in a timely manner, to the originator or sponsor and to the EU parent credit institution or an EU financial holding company the information needed to satisfy the requirements referred to in paragraph 6.

2. Paragraph 1 shall not apply when the securitised exposures are claims or contingent claims on or wholly, unconditionally and irrevocably guaranteed by:

   a) central governments or central banks;
      (aa) regional governments, local authorities and public sector entities of Member States;

   b) institutions to which a 50% risk weight or less is assigned under Articles 78 to 83; and

   c) multilateral development banks.

Paragraph 1 shall not apply to:

   a) transactions based on a clear, transparent and accessible index, where the underlying reference entities are identical to those that make up an index of entities that is widely traded, or are other tradable securities other than securitisation positions;

   b) syndicated loans, purchased receivables or credit default swaps where these instruments are not used to package and/or hedge a securitisation that is covered by paragraph 1.

4. Before investing, and as appropriate thereafter, credit institutions, shall be able to demonstrate to the competent authorities for each of their individual securitisation positions, that they have a comprehensive and thorough understanding of and have implemented formal policies and procedures appropriate to their trading book and non-trading book and commensurate with the risk profile of their investments in securitised positions for analysing and recording:

   a) information disclosed under paragraph 1, by originators or sponsors to specify the net economic interest that they maintain, on an ongoing basis, in the securitisation;

   b) the risk characteristics of the individual securitisation position;

   c) the risk characteristics of the exposures underlying the securitisation position;

   d) the reputation and loss experience in earlier securitisations of the originators or sponsors in the relevant exposure classes.
underlying the securitisation position;

e) the statements and disclosures made by the originators or sponsors, or their agents or advisors, about their due diligence on the securitised exposures and, where applicable, on the quality of the collateral supporting the securitised exposures;

f) where applicable, the methodologies and concepts on which the valuation of collateral supporting the securitised exposures is based and the policies adopted by the originator or sponsor to ensure the independence of the valuer; and

g) all the structural features of the securitisation that can materially impact the performance of the credit institution’s securitisation position.

Credit institutions shall regularly perform their own stress tests appropriate to their securitisation positions. To this end, credit institutions may rely on financial models developed by an ECAI provided that credit institutions can demonstrate, when requested, that they took due care prior to investing to validate the relevant assumptions in and structuring of the models and to understand methodology, assumptions and results.

5. Credit institutions, other than when acting as originators or sponsors or original lenders shall establish formal procedures appropriate to their trading book and non-trading book and commensurate with the risk profile of their investments in securitised positions to monitor on an ongoing basis and in a timely manner performance information on the exposures underlying their securitisation positions. Where relevant, this shall include the exposure type, the percentage of loans more than 30, 60 and 90 days past due, default rates, prepayment rates, loans in foreclosure, collateral type and occupancy, frequency distribution of credit scores or other measures of credit worthiness across underlying exposures, industry and geographical diversification, frequency distribution of loan to value ratios with band widths that facilitate adequate sensitivity analysis. Where the underlying exposures are themselves securitisation positions, credit institutions shall have the above-listed information not only on the underlying securitisation tranches, such as the issuer name and credit quality, but also on the characteristics and performance of the pools underlying these securitisation tranches.

Credit institutions shall have a thorough understanding of all structural features of a securitisation transaction that would materially impact the performance of their exposures to the transaction such as the contractual waterfall and waterfall related triggers, credit enhancements, liquidity enhancements, market value triggers, and deal-specific definition of default.

Where the requirements in paragraph 4, 7 and in this paragraph are not met in any material respect by reason of the negligence or omission of the credit institution, Member States shall ensure that competent authorities impose a proportionate additional risk weight of not less than 250 % of the risk weight (capped at 1 250 %) which would, but for this paragraph, apply to the relevant securitisation positions under Annex IX, part 4, and
shall progressively increase the risk weight with each subsequent infringement of the due diligence provisions. The competent authority shall take into account the exemptions for certain securitisations provided in paragraph 2 by reducing the risk weight it would otherwise impose under this provision in respect of a securitisation to which paragraph 2 applies.

6. Sponsor and originator credit institutions shall apply the same sound and well-defined criteria for credit-granting in accordance with the requirements of Annex V, point 3 to exposures to be securitised as they apply to exposures to be held on their book. To this end the same processes for approving and, where relevant, amending, renewing and refinancing credits shall be applied by the originator and sponsor credit institutions. Credit institutions shall also apply the same standards of analysis to participations and/or underwritings in securitisation issues purchased from third parties whether such participations and/or underwritings are to be held on their trading or non-trading book.

Where the requirements in paragraph 6 are not met, Article 95(1) shall not be applied by an originator credit institution which will not be allowed to exclude the securitised exposures from the calculation of its capital requirements under this Directive.

7. Sponsor and originator credit institutions shall disclose to investors the level of their commitment under paragraph 1 to maintain a net economic interest in the securitisation. Sponsor and originator credit institutions shall ensure that prospective investors have readily available access to all materially relevant data on the credit quality and performance of the individual underlying exposures, cash flows and collateral supporting a securitisation exposure as well as such information that is necessary to conduct comprehensive and well informed stress tests on the cash flows and collateral values supporting the underlying exposures. For this purpose, 'materially relevant data' shall be determined as at the date of the securitisation and where appropriate due to the nature of the securitisation thereafter.

8. Paragraphs 1 to 7 shall apply to new securitisations issued from 31 December 2010. Paragraphs 1 to 7 shall apply from 31 December 2014 to existing securitisations where new underlying exposures are added or substituted after that date. Competent authorities may decide to temporarily suspend the requirements referred to in paragraphs 1 and 2 during periods of general market liquidity stress.

9. Competent authorities shall disclose the following information:

   a) the general criteria and methodologies adopted to review the compliance with paragraphs 1 to 7 at 31 December 2010;

   c) without prejudice to the provisions laid down in Chapter 1, Section 2, a summary description of the outcome of the supervisory review and description of the measures imposed in cases of non-compliance with paragraphs 1 to 7 identified on an annual basis starting from December 2011.

This requirement is subject to the second subparagraph of Article 144.
10. The Committee of European Banking Supervisors will report annually to the Commission about the compliance by competent authorities with this Article. The Committee of European Banking Supervisors shall elaborate guidelines for the convergence of supervisory practices with regard to this Article, including the measures taken in case of breach of the due diligence and risk management obligations.

2.6. CRD Recital 15 reads:

It is important to remove misalignment between the interest of firms that 're-package' loans into tradable securities and other financial instruments (originators or sponsors) and firms that invest in these securities or instruments (investors). It is also important that the interests of the originator or sponsor and the interests of investors are aligned. To achieve this, the originator or sponsor retains a significant interest in the underlying assets. It is therefore important for the originators or the sponsors to retain exposure to the risk of the loans in question. More generally, securitisation transactions should not be structured in such a way as to avoid the application of the retention requirement, in particular through any fee or premium structure or both. Such retention should be applicable in all situations where the economic substance of a securitisation according to the definition of the Directive is applicable, whatever legal structures or instruments are used to obtain this economic substance. In particular where credit risk is transferred by securitisation, investors should make their decisions only after conducting thorough due diligence, for which they need adequate information about the securitisations. The measures to address the potential misalignment of these structures need to be consistent and coherent in all relevant financial sector regulation. The Commission should put forward appropriate legislative proposals to ensure such consistency and coherence.

There should be no multiple applications of the retention requirement. For any given securitisation it suffices that only one of the originator, the sponsor or the original lender is subject to the requirement. Similarly, where securitisation transactions contain other securitisations as an underlying, the retention requirement should be applied only to the securitisation which is subject to the investment.

Purchased receivables should not be subject to the retention requirement if they arise from corporate activity where they are transferred or sold at a discount to finance such activity.

Competent authorities should apply the risk weight in relation to non-compliance with due diligence and risk management obligations in relation to securitisation for non-trivial breaches of policies and procedures which are relevant to the analysis of the underlying risks.

In the Declaration on Strengthening the Financial System of 2 April 2009, the leaders of the G20 requested the Basel Committee for Banking Supervision and authorities to consider due diligence and quantitative retention requirements for securitisation by 2010. In view of these international developments, and in order to best mitigate systemic risks arising from securitisation markets the Commission will, before end 2009 and after consulting the Committee of European Banking Supervisors,
decide whether an increase of the retention requirement should be proposed, and whether the methods of calculating the retention requirement deliver the objective of better aligning the interests between originators or sponsors and investors."

**Multi-lateral development banks**

Any of the following:

a. African Development Bank;
b. Asian Development Bank;
c. Caribbean Development Bank;
d. Council of Europe Development Bank;
e. European Bank for Reconstruction & Development;
f. European Investment Bank;
g. European Investment Fund;
h. Inter-American Development Bank;
i. International Bank for Reconstruction and Development;
j. International Finance Corporation;
k. International Finance Facility for Immunisation;
l. Islamic Development Bank;
m. Multilateral Investment Guarantee Agency; and

For the purposes of the standardised approach to credit risk the following are considered to be a multilateral development bank:

a. the Inter-American Investment Corporation;
b. the Black Sea Trade and Development Bank; and
c. the Central American Bank for Economic Integration.
3. Advice

3.1. Purpose

3.1. Article 135(2) states that implementing measures for tradable securities and other financial instruments based on repackaged loans are intended to ensure cross-sectoral consistency. Therefore CEIOPS has used the requirements in the CRD\(^7\) that apply to credit institutions and certain investment undertakings as a basis to draft this advice.

3.2. Consistency with the CRD is important although (re)insurance undertakings have not traditionally purchased these products in large quantities\(^8\). The measures set out here can be seen as preventative and mean that undertakings are given an equal opportunity to invest in these products alongside CRD undertakings. The principles may differ because the terminology or the principle does not apply in the same way to undertakings as it would to CRD undertakings.

3.3. The CRD Level 1 text is more detailed than that provided in the Solvency II Framework Directive. Should the Committee of European Banking Supervisors (CEBS) publish further guidance to the CRD once the Solvency II implementing measures have been finalised, this could be considered within Solvency II Level 3 guidance.

3.4. The protection of policyholders and beneficiaries is the main objective of insurance supervision under Solvency II (see Article 27), and therefore robust and effective regulations should be in place for these products. However innovation, which CEIOPS does not wish to discourage, will need to be dealt with appropriately and overly prescriptive implementing measures may be inappropriate for new market developments. Therefore the implementing measures should, on the whole, be high-level and principles-based with any specific details being adopted at Level 3 and amended with any new innovation in the market when required.

3.5. A number of principles are set out that deal with each of the issues in Article 135 but, due to their individual nature, tradable securities and other financial instruments based on repackaged loans will need to be evaluated given their own specific details. The principles to be applied to such securities and instruments should take into consideration the principle of substance over form. This is because it is not possible to anticipate the specific nature that these products may take in future years. That might constrain the investment strategies at the disposal of undertakings but also increase the risk of regulatory arbitrage through the use of new products falling outside the scope of these implementing measures. Establishing high-level principles would facilitate the ongoing development and evolution of financial markets and their proper supervision.

---

\(^7\) The relevant CRD Article 122a is included in Chapter 2.2.2.

3.1.1. Definitions

3.6. CEIOPS intends that the same definitions for key terms should be used in this advice as for the CRD, hence the following apply:

“The repackaging of loans into tradable securities and other financial instruments” means a transaction or scheme, whereby the credit risk associated with an exposure or pool of exposures is tranched, having the following characteristics:

(a) payments in the transaction or scheme are dependent upon the performance of the exposure or pool of exposures; and

(b) the subordination of tranches determines the distribution of losses during the ongoing life of the transaction or scheme.

“Tranche” means a contractually established segment of the credit risk associated with an exposure or number of exposures, where a position in the segment entails a risk of credit loss greater than or less than a position of the same amount in each other such segment, without taking account of credit protection provided by third parties directly to the holders of positions in the segment or in other segments.

“Originator” means either of the following:

(a) an entity which, either itself or through related entities, directly or indirectly, was involved in the original agreement which created the obligations or potential obligations of the debtor or potential debtor giving rise to the exposure being securitised; or

(b) an entity which purchases a third party’s exposures onto its balance sheet and then securitises them.

“Sponsor” means a credit institution other than an originator credit institution that establishes and manages an asset-backed commercial paper programme or other securitisation scheme that purchases exposures from third party entities.

3.2. Principles

3.7. CEIOPS intends that the principle of proportionality should be applied when meeting these requirements. The work involved to meet the requirements should be commensurate to the nature, scale and complexity of the risks inherent in the product in question. For example, CEIOPS would expect more work (monitoring frequency, stress tests etc) to be undertaken to ensure compliance with these principles: if an undertaking intends to invest in or has invested in a material amount of tradable securities and other financial instruments based on repackaged loans; if the underlying exposures prove to be volatile; for instruments with a lower creditworthiness; or if there is (or is likely to be) a material change to the likelihood or scale of default of the underlying exposures.
3.8. Tradable securities and other financial instruments based on repackaged loans should be valued in an undertaking’s balance sheet according to the Solvency II valuation principles.

3.2.1. Principles relating to Article 135(2a)

**Principle 1 – Originators’ retained interest**

3.9. Undertakings should only invest in tradable securities and other financial instruments based on repackaged loans if the originator or sponsor has explicitly disclosed to the undertaking in the documentation governing the investment that it will retain, on an ongoing basis, a net economic interest which in any event should not be less than 5%.

3.10. For this purpose, retention of a net economic interest should mean:

a) retention of not less than 5% of the nominal value of each of the tranches sold or transferred to the investors; or

b) in the case of securitisations of revolving exposures, retention of originators’ interest of not less than 5% of the nominal value of the securitised exposures; or

c) retention of randomly selected exposures, equivalent to not less than 5% of the nominal amount of the securitised exposures, where these would otherwise have been securitised in the securitisation provided that the number of potentially securitised exposures is not less than 100 at origination; or

d) retention of the first loss tranche and, if necessary, other tranches having the same or a more severe risk profile and not maturing any earlier than those transferred or sold to investors, so that the retention equals in total not less than 5% of the nominal value of the securitised exposures.

3.11. The net economic interest is measured at origination and, if later, at the date of investment by the undertaking and should be maintained on an on-going basis. For the purpose of this Article, "on-going basis" means that retained positions, interest or exposures should not be hedged or sold. The net economic interest should not be subject to any credit risk mitigation or any short positions or any other hedge. The net economic interest should be determined by the notional value for off-balance sheet items.

---


10 The CRD article refers to the "the requirements that need to be met...in order for an...undertaking to be allowed to invest, including the requirements that ensure that the originator retains a net economic interest of not less than 5 per cent." This refers to the provisions in article 133(2a) in the Level 1 text. The best way to ensure this is to have it written as a contractual provision.

11 If implementing measures or guidance relating to the CRD were to be introduced requiring that an amount greater than 5% should be maintained by the originator then the provisions relating to (re)insurance undertakings at Level 2 should be updated or future Level 3 guidance should be drafted in a way as to ensure cross-sectoral consistency.
3.12. CEIOPS expects that undertakings should check that the originator or sponsor (as the case may be) maintains a net economic interest of at least 5% in such securities or instruments before investing and as appropriate thereafter. This responsibility does not rest with the supervisory authority responsible for the originator where the originator is a regulated entity.

3.13. There should be no multiple applications of the retention requirements for any given securitisation. This means that the same minimum 5% retained economic interest cannot support multiple tranches of securitisation.

3.14. In order to assist in ensuring that the issuer maintains a net economic interest of at least 5% of the tradable securities and other financial instruments based on repackaged loans throughout the lifetime of the investment, undertakings should make sure that the issuer has declared in a public prospectus that it intends to hold at least 5% throughout the lifetime of the investment. CEIOPS expects that the undertaking should be reasonably sure that the originator would not sell or hedge its 5% interest throughout the lifetime of the investment and CEIOPS would not expect undertakings to invest in the repackaged loans of originators that have sold their interest in a previous offering.

3.15. Securitisation transactions should not be structured in such a way as to avoid the application of the retention requirement, in particular through any fee/commission or premium structure (or both).

3.16. A number of exemptions apply to Principle 1 for investing in tradable securities and other financial instruments based on repackaged loans in the CRD that, in the interests of cross-sectoral consistency, CEIOPS considers should also apply in Solvency 2. Principle 1 should not apply when the securitised exposures are claims or contingent claims on or wholly, unconditionally and irrevocably guaranteed by those institutions listed in CRD Article 122a paragraph 2 (see section 2.2.2 of this advice).

3.17. In addition, supervisory authorities may grant specific exemptions from Principle 1, other than those exemptions referred to in paragraph 3.16, as they arise on a case-by-case basis if the supervisory authority is satisfied that the particular exemption requested by the undertaking is sufficiently similar to the exemptions referred to in paragraph 3.16.

3.18. Exemptions from the requirements for the originator in relation to Principle 1 may also be authorised by supervisory authorities on a case-by-case basis on the request of the undertaking and will only include the following:

a) transactions based on a clear, transparent and accessible index, where the underlying reference entities are identical to those that make up an index of entities that is widely traded, or are other tradable securities other than securitisation positions;

b) syndicated loans, purchased receivables or credit default swaps where these instruments are not used to package and/or hedge a securitisation that is covered by this principle.

3.19. The exemptions are included within the CRD and CEIOPS considers it important, in the interests of cross-sectoral consistency that the same exemptions apply to (re)insurance undertakings. However, supervisory authorities may decide to temporarily the requirements referred to in this
principle during periods of general market liquidity stress. This decision should be consistently applied across financial sectors by the Level 3 Committees.

**Principle 2 – Criteria for sponsor and credit institutions**

3.20. Prior to an undertaking investing in tradable securities and other financial instruments based on repackaged loans the undertaking should ensure that sponsor and originator credit institutions meet the following criteria.

3.21. The sponsor and originator credit institutions should base credit granting (such as the issuance of loans or mortgages) on sound and well-defined criteria and clearly establish the process for approving, amending, renewing, and re-financing loans to the exposures to be securitised as they apply to exposures they hold. To this end the same processes for approving and, where relevant, amending, renewing and re-financing loans should be applied by the originator and sponsor credit institutions. Sponsors and originators should also apply the same standards of analysis to participations and/or underwritings in securitisation issues purchased from third parties if they form part of the exposures to be repackaged.

3.22. In respect of the underlying assets of a specific portfolio, undertakings should ensure that an originator operates effective systems to manage the ongoing administration and monitoring of its various credit risk-bearing portfolios and exposures, including for identifying and managing problem loans and for making adequate value adjustments and provisions.

3.23. The originator has to adequately each credit portfolio given its target market and overall credit strategy.

3.24. Undertakings should ensure that the documentation maintained by the originator includes its policy for credit risk, including its risk appetite and provisioning policy and how it measures, monitors and controls that risk. This includes a description of the systems used to ensure that the policy is correctly implemented. Any contractual securitisation arrangement between the originator and the investor should include contractual terms to allow for the inspection of the necessary documentation to meet regulatory requirements.

**Principle 3 – Transparency and disclosure of the underlying exposures**

3.25. Prior to an undertaking investing in tradable securities and other financial instruments based on repackaged loans the undertaking should ensure that the sponsor and originator credit institutions disclose to the undertaking the level of their commitment, as under Principle 1, to maintain a net economic interest in the securitisation. The originator and sponsor should also disclose any features of the holding that could undermine the concept of its retained interest such as commission payments associated with the transaction.

3.26. Undertakings should ensure that the sponsor and originator credit institutions give readily available access to all material and relevant data on the credit quality and performance of the individual underlying
exposures, cash flows and collateral supporting a securitisation exposure as well as such information that is necessary to conduct comprehensive and well informed stress tests on the cash flows and collateral values supporting the underlying exposures. These stress tests should be carried out in accordance with good asset-liability management as stated in CEIOPS’ Advice for Level 2 Implementing Measures on Solvency II: System of Governance (former CP33)\(^{12}\), Para 3.92. For this purpose, ‘materially relevant data’ should be determined as at the date of the securitisation and where appropriate to the nature of the securitisation thereafter.

3.2. Principles relating to Article 135(2b)

**Principle 4 – Skill, care and diligence**

3.27. Undertakings are required, under Article 132 of the Level 1 text (“prudent person” principle) only to invest in assets whose risks the undertaking concerned can properly identify, measure, monitor, manage, control and report. These prudent person principles should apply equally to all investments made by the undertaking including tradable securities and other financial instruments based on repackaged loans as undertakings need to have a thorough understanding of their investments.

3.28. Given the additional complexity involved in investing in tradable securities and other financial instruments based on repackaged loans, undertakings need to be more aware of the risks embedded in the assets they are buying than for more ‘traditional assets’. CEIOPS considers this particularly important in the case of complex structured instruments.

3.29. CEIOPS’ abovementioned Advice on Governance set out the principle that undertakings need to have an effective risk management system comprising strategies, processes and reporting procedures necessary to identify, measure, monitor, manage, control and report risk to which the undertaking is or could be exposed. Undertakings investing in tradable securities and other financial instruments based on repackaged loans need to comply with these requirements and should pay particular attention to assessing the ALM risk, concentration risk, investment risk etc arising from these products. Undertakings who invest in these products should also have due consideration of these principles within their internal investment policy.

**Principle 5 – Monitoring procedures**

3.30. Undertakings should establish formal monitoring procedures commensurate with the risk profile of their investments in securitised positions to monitor on an ongoing basis and, in a timely manner,

performance information on the exposures underlying their securitisation positions. Undertakings need to have access to relevant information to be able to perform this analysis. This performance information could include:

- the exposure type;
- the percentage of loans more than 30, 60 and 90 days past due;
- default rates, prepayment rates;
- loans in foreclosure;
- collateral type and occupancy;
- frequency distribution of credit scores or other measures of credit worthiness across underlying exposures, industry and geographical diversification; and
- frequency distribution of loan to value ratios with band widths that facilitate adequate sensitivity analysis.

3.31. Where the underlying exposures are themselves securitisation positions, undertakings should have the above-listed information not only on the underlying securitisation tranches, but also on the characteristics and performance of the risks underlying these securitisation tranches.

3.32. Undertakings should have a thorough understanding of all structural features of a securitisation transaction that would materially impact the performance of their exposures to the transaction such as the contractual waterfall and waterfall-related triggers, credit enhancements, liquidity enhancements, market value triggers, and deal-specific definition of default. This is a requirement of the CRD and is also relevant for (re)insurance undertakings.

**Principle 6 – Stress tests (including using financial models)**

3.33. Undertakings, where appropriate, should perform stress tests as part of their Own Risk and Solvency Assessment (ORSA) and wherever else appropriate to ensure the adequate management, monitoring and control of the investments in accordance with Article 132 of the Level 1 text. Where an undertaking holds a material value of tradable securities and other financial instruments based on repackaged loans, CEIOPS will expect these to be subject to their own stress tests simultaneously taking into account the underlying exposures.

---

13 Foreclosure is the legal and professional proceeding in which a mortgagee, usually a lender, obtains a court ordered termination of a mortgagor’s equitable right of redemption i.e. the loan is terminated and repaid early and possibly not in full.

14 Collateral type and occupancy refers to the type of loans that are being securitised into an ABS. For example credit card debt, mortgage, overdraft facilities, car loans, student loans etc.

15 Of mortgage debt there are various types of occupancy, e.g. main residence, second home, buy to let, sub-prime lending or shared ownership schemes.

16 A band width refers to the size of the range of loan to value classifications a credit institution is using.

17 A waterfall in this context is the method by which the various tranches of the CDO are paid interest, whereby the super senior tranches are paid first, followed by the senior, mezzanine and equity tranches.
account the dynamic effect of the stress test scenario on the rest of their business. The results of any stress tests should be documented and mitigating actions taken as appropriate.

3.34. In their own stress tests, undertakings may rely on financial models developed by an External Credit Assessment Institution (ECAI), provided that the undertaking is able to demonstrate, when requested, that it took due skill, care and diligence prior to investing to validate the relevant assumptions in and structuring of these financial models to understand methodology, assumptions and results of their investment decisions and valuation of such products.

3.35. Undertakings should ensure, when investing in tradable securities and other financial instruments based on repackaged loans, that the rating reflects the nature of the underlying risks associated with collateral assets. An undertaking should not rely solely on an ECAI assessment as the purpose of these models may not necessarily be aligned with the need of the undertaking. If a credit rating is used the undertaking should understand how the rating has been derived.

3.36. In addition, undertakings should also always assess the underlying exposures and should not only rely on any hedging instrument, such as a credit default swap, that they have purchased as part of a wrap as protection against adverse performance of the underlying loans.

**Principle 7 – Formal policies, procedures and reporting**

3.37. Before investing in tradable securities and other financial instruments based on repackaged loans, and as appropriate thereafter (e.g. immediately when a breach of the requirements occurs), an undertaking should be able to demonstrate to its supervisory authority that for each of its individual securitisation positions it has a comprehensive and thorough understanding of, and has implemented, formal policies and procedures appropriate to its investment portfolio. These formal policies and procedures should be commensurate with the risk profile of the investments in securitised positions. Analysing and recording tradable securities and other financial instruments based on repackaged loans that the undertaking has invest in should include:

a) information disclosed under Principle 3, by originator or sponsor to specify the net economic interest that it maintains, on an ongoing basis, in the securitisation;

b) the risk characteristics of the individual securitisation position;

c) the risk characteristics of the exposures underlying the securitisation position;

d) the reputation and loss experience in earlier securitisations, if relevant, of the originators or sponsors in the relevant exposure classes underlying the securitisation position;

e) the statements and disclosures made by the originators or sponsors, or their agents or advisors, about their due diligence on the securitised
exposures and, where applicable, on the quality of the collateral supporting the securitised exposures;

f) where applicable, the methodologies and concepts on which the valuation of collateral supporting the securitised exposures is based, e.g. market consistent valuation, and the policies adopted by the originator or sponsor to ensure the independence of the valuer from the originator; and

g) all the structural features of the securitisation that can materially impact the performance of the undertakings securitisation position.

3.38. Undertakings should also ensure that there is an adequate level of internal reporting to the administrative or management body so that they are aware of material investment made in repackaged loans and to ensure that the risks from these products are adequately managed.

3.39. Undertakings should also include appropriate information on their investments in these products, and their risk management procedures in this area, in their supervisory reporting and public disclosure.

3.2.3. Breach of requirements

3.40. CEIOPS believes that there are two possible situations where a breach of the requirements may occur. The first could be a breach by the originator or sponsor in advance of the investment being made identified through the due diligence performed by the undertaking. The second could be a breach by the undertaking not fulfilling its requirements either through inadequate due diligence prior to making the investment or once it has made the investment.

3.41. Firstly, if an undertaking, during its due diligence prior to investing in tradable securities and other financial instruments based on repackaged loans, determines that the requirements imposed on the originator are not being met then it shall not invest in such securities or instruments. For example, if the originator does not hold or intend to retain an interest of more than 5% or if the undertaking determines that the originator does not base credit granting on sound and well defined criteria then the investment cannot be made. CEIOPS considers that this is consistent with Article 135(2a).

3.42. Secondly, a breach could be caused by the undertaking failing to fulfil its requirements after the investment has been made or if the undertaking fails to conduct adequate due diligence prior to making the investment with the result, for example, that it was not aware that the originator or sponsor (as the case may be) did not meet the requirements placed upon it. In this situation, the (re) insurance undertaking shall immediately inform the supervisory authority as soon as they observe that these requirements are no longer complied with. The undertaking should enter into a discussion with the supervisors to assess the consequences of this and the possibilities, in the first instance, for the undertaking to dispose of its holding. Consideration should be given to the ability of the undertaking to dispose of the holding at a reasonable price (given the nominal value) and within an appropriate timeframe. In addition, regard should be given to potential procyclical effects if many undertakings are looking dispose of
their holding simultaneously. If this it is agreed that it is not possible or is not in the best interests of policyholders to dispose of their holding, further actions should be explored such as a capital charge may be levied (e.g. similar to that in CRD\textsuperscript{18}).

3.43. The situation could also arise where, despite the due diligence carried out by the undertaking in Principle 1, if after the investment has been made (with the requirements having been met by the originator or sponsor prior to investing) the originator or sponsor (as the case may be) fails to continue to comply with the requirements. For example, if the originator ceases to maintain at least a 5% nominal value (referred to in Principle 1) through either selling or hedging its exposure having disclosed at the outset of the transaction that they did not intend to do this. Similar to the situation above, CEIOPS would expect the undertaking to discuss with the supervisors the consequences of this and assess the possibilities, in the first instance, for the undertaking to dispose of its holding. Consideration should be given to the ability of the undertaking to dispose of the holding at a reasonable price (given the nominal value) and within an appropriate timeframe. In addition, regard should be given to potential procyclical effects if many undertakings are looking dispose of their holding simultaneously. CEIOPS expects that undertakings seek to take some action in this situation. If it is agreed that it is not possible or is not in the best interests of policyholders to dispose of their holding, further actions should be explored such as a capital charge may be levied (e.g. similar to that in CRD).

3.44. In order to maintain market discipline and discourage originators from reneging on their retained interest, there is a supervisory expectation that undertakings should not enter into future business with originators that have behaved in this way. This aims to provide a disincentive to originators to behave in such a manner as their future business and reputation would be damaged. If, however, it is subsequently determined that the originator has a history of non-compliance that should have been determined by the undertaking prior to investing, this should be dealt with by the supervisory authority (lack of due diligence) under Pillar 2 as we would expect that the undertaking would not invest in such products if the originator had a history of failing to meet its continuing obligations.

3.3. Grandfathering

3.45. The CRD states (re CRD par 122 a, paragraph 8) that the relevant principles for CRD undertakings that invest in tradable securities and other financial instruments based on repackaged loans shall apply from 31 December 2014 to existing securitisations, where new underlying exposures are added or substituted after that date. To maintain cross-sectoral consistency, this requirement should also be applied to (re)insurance undertakings hence only material substitutions made after the grandfathering date that seek to improve the credit quality of the relevant tradable securities and other financial instruments would lead to the relevant tradable securities and other financial instruments based on

\textsuperscript{18} CEIOPS will look to develop this further under its guidance for the SCR to determine how this escalating charge might work.
repackaged loans being subject to the Solvency 2 principles. Any substitutions that do not seek to improve the credit quality of the relevant tradable securities and other financial instruments would lead to the relevant tradable securities and other financial instruments based on repackaged loans being subject to the Solvency 2 principles.

3.46. CEIOPS believes that this proposal creates four different scenarios:

- New tradable securities and other financial instruments based on repackaged loans issued on or after 1 January 2011 would be subject to the Article 135(2) rules from the date on which Solvency 2 is implemented.

- Existing tradable securities and other financial instruments based on repackaged loans that were issued before 1 January 2011 where underlying exposures are never subsequently changed would not be subject to the Article 135(2) rules but would remain subject, for example, to the Prudent Person Principle from the date on which Solvency 2 is implemented.

- Existing tradable securities and other financial instruments based on repackaged loans that were issued before 1 January 2011 where underlying exposures are changed before 31 December 2014 but not after this date would not be subject to the Article 135(2) rules but would remain subject, for example, to the Prudent Person Principle from the date on which Solvency 2 is implemented.

- Existing tradable securities and other financial instruments based on repackaged loans that were issued before 1 January 2011 where underlying exposures are changed after 31 December 2014 would become subject to the Article 135(2) rules from the date of the change.

**CEIOPS’ advice**

**Principles relating to Article 135(2a)**

**Principle 1 – Originators retained interest**

3.47. Undertakings shall only invest in tradable securities and other financial instruments based on repackaged loans if the originator or sponsor has explicitly disclosed to the undertaking in the documentation governing the investment that it will retain, on an ongoing basis, a net economic interest which in any event shall not be less than 5%. The net economic interest shall be measured at the origination and, if later, at the date of investment by the undertaking and shall be maintained on an on-going basis.

3.48. There shall be no multiple applications of the retention requirements for any given securitisation. This means that the same minimum 5% retained economic interest cannot support multiple tranches of securitisation.

3.49. A number of exemptions apply to the requirements for investing in tradable securities and other financial instruments based on repackaged loans in the CRD that, in the interests of cross-sectoral consistency,
CEIOPS considers should also apply in Solvency 2. Principle 1 should not apply when the securitised exposures are claims or contingent claims on or wholly, unconditionally and irrevocably guaranteed by those institutions listed in CRD Article 122a paragraph 2.

3.50. In addition, supervisory authorities may grant specific exemptions from Principle 1, other than those exemptions referred to in paragraph 3.48, as they arise on a case-by-case basis if the supervisory authority is satisfied that the particular exemption requested by the undertaking is sufficiently similar to the exemptions referred to in paragraph 3.49.

3.51. Exemptions from the requirements for the originator in relation to Principle 1 may also be authorised by supervisory authorities on a case-by-case basis on the request of the undertaking and will include the following:

a. transactions based on a clear, transparent and accessible index, where the underlying reference entities are identical to those that make up an index of entities that is widely traded, or are other tradable securities other than securitisation positions; and

b. syndicated loans, purchased receivables or credit default swaps where these instruments are not used to package and/or hedge a securitisation that is covered by this principle.

Principle 2 – Criteria for sponsor and originator credit institutions

3.52. Prior to an undertaking investing in tradable securities and other financial instruments based on repackaged loans, it is required that the undertaking shall ensure that the sponsor and originator credit institutions:

- base credit granting (such as the issuance of loans or mortgages) on sound and well-defined criteria and clearly establish the process for approving, amending, renewing, and re-financing loans to the exposures to be securitised as they apply to exposures they hold;

- ensure that an originator operates effective systems to manage the ongoing administration and monitoring of its various credit risk-bearing portfolios and exposures, including for identifying and managing problem loans and for making adequate value adjustments and provisions;

- diversify adequately each credit portfolio given its target market and overall credit strategy; and

- maintain documentation to include its policy for credit risk, including its risk appetite and provisioning policy and shall describe how it measures, monitors and controls that risk.

Principle 3 – Transparency and disclosure of the underlying

3.53. Prior to an undertaking investing in tradable securities and other financial instruments based on repackaged loans, the undertaking shall ensure that the sponsor and originator credit institutions disclose to the undertaking the level of their commitment as under Principle 1 to maintain a net economic interest in the securitisation. The originator and sponsor shall
also disclose any features of the holding that would undermine the concept of its retained interest, such as commission payments.

**Principles relating to Article 135(2b)**

**Principle 4 – Skill, care and diligence**

3.54. Undertakings investing in tradable securities and other financial instruments based on repackaged loans need to be able to properly identify, measure, monitor, manage, control and report the risks of these products and shall pay particular attention to assessing the ALM risk, concentration risk and investment risk arising from these products. Undertakings who invest in these products shall also have due consideration within their internal investment policy.

**Principle 5 – Monitoring procedures**

3.55. Undertakings shall establish formal monitoring procedures commensurate with the risk profile of their investments in tradable securities and other financial instruments based on repackaged loans to monitor on an ongoing basis and, in a timely manner, performance information on the exposures underlying their securitisation positions. Undertakings need to have access to relevant information to be able to perform this analysis.

**Principle 6 – Stress tests (including using financial models)**

3.56. Where an undertaking holds a material value of tradable securities and other financial instruments based on repackaged loans the undertaking shall regularly perform its own stress tests appropriate to its securitisation positions simultaneously taking into account the dynamic effect of the stress test scenario on the rest of their business.

**Principle 7 – Formal policies, procedures and reporting**

3.57. Before investing in tradable securities and other financial instruments based on repackaged loans, and as appropriate thereafter, an undertaking shall be able to demonstrate to its competent supervisory authorities that for each of its individual securitisation positions it has a comprehensive and thorough understanding of and has implemented formal policies and procedures appropriate to its investment portfolio. These formal policies and procedure shall commensurate with the risk profile of their investments in securitised positions.

3.58. Undertakings shall also ensure that there is an adequate level of internal reporting to administrative or management body so that they are aware of material investment made in repackaged loans and that the risks from these products are adequately managed.

3.59. Undertakings shall also include appropriate information on their
investments in these products, and their risk management procedures in this area, in the supervisory reporting and public disclosure requirements.

**Grandfathering/transitional measures**

3.60. For undertakings that have invested in tradable securities and other financial instruments based on repackaged loans that were issued before 1 January 2011, the above requirements shall apply from 31 December 2014 where new underlying exposures are added or substituted after that date.