Prudential Standard APS 120

Securitisation

Objectives and key requirements of this Prudential Standard

This Prudential Standard aims to ensure that an authorised deposit-taking institution adopts prudent practices to manage the risks associated with securitisation and to ensure sufficient regulatory capital is held against the associated credit risk.

The key requirements of this Prudential Standard are that an authorised deposit-taking institution must:

- have a risk management framework covering its involvement in a securitisation;
- ensure there is clear and prominent disclosure of the nature and limitations of its obligations arising from its involvement in a securitisation;
- not provide implicit support to a securitisation; and
- calculate regulatory capital for credit risk against its securitisation exposures.

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Authority

1. This Prudential Standard is made under section 11AF of the *Banking Act 1959* (the **Banking Act**).

Application

2. Subject to paragraphs 3 and 5, this Prudential Standard applies to an **authorised deposit-taking institution** (**ADI**) and an **authorised non-operating holding company** (**authorised NOHC**).

3. This Prudential Standard does not apply to a **purchased payment facility provider**. A **foreign ADI** need only comply with the provisions of this Prudential Standard relating to separation and disclosure (paragraphs 13 to 18), risk management framework (paragraph 72) and self-assessment (paragraph 73 only).

4. A reference to an ADI in this Prudential Standard, unless otherwise indicated, is a reference to:

   (a) an ADI on a **Level 1** basis; and

   (b) a **group** of which an ADI is a member on a **Level 2** basis.

5. If an ADI to which this Prudential Standard applies is:

   (a) the holding company for a group, the ADI must ensure that the requirements in this Prudential Standard are met on a Level 2 basis, where applicable; or

   (b) a **subsidiary** of an authorised NOHC, the authorised NOHC must ensure that the requirements in this Prudential Standard are met on a Level 2 basis, where applicable.

Interpretation

6. In this Prudential Standard:

   (a) terms that are defined in *Prudential Standard ~~A~~CPS 001 Defined~~itions~~ terms* appear in bold the first time they are used; and

   (b) unless the contrary intention appears, a reference to an Act, Regulations, Prudential Standard, Australian Accounting or Auditing Standard is a reference to the instrument as in force from time to time.

7. Where this Prudential Standard provides for APRA to exercise a power or discretion, this power or discretion is to be exercised in writing.

Scope

8. Except where otherwise provided, this Prudential Standard applies to all roles undertaken by, and investments of, an ADI in a **securitisation**. This Prudential Standard applies whether the exposures in the pool have been:

(a) on an ADI's balance sheet;

(b) originated by an ADI into the pool without being first on the ADI's balance sheet; or

(c) originated by any other entity.

9. An ADI must apply the capital adequacy requirements set out in this Prudential Standard to securitisation exposures held in its banking book. Securitisation exposures held in an ADI's trading book are subject to *Prudential Standard APS 116 Capital Adequacy: Market Risk*, except that securitisation exposures held in the trading book must be deducted from **Common Equity Tier 1 Capital** if they are required by this Prudential Standard to be deducted if held in the banking book.

10. This Prudential Standard applies to securitisations, whether traditional, synthetic or containing features common to both. APRA may determine that this Prudential Standard applies to a particular arrangement, as if it were a securitisation, if APRA considers that it has features similar to a securitisation and gives rise to similar prudential risks.

11. For the purpose of calculating the Level 2 Regulatory Capital requirement, for the underlying exposures in the pool or the securitisation exposures, of an overseas banking subsidiary that is prudentially regulated by a prescribed New Zealand authority, an ADI must calculate risk-weighted assets using the prescribed New Zealand authority's equivalent prudential rules as in force from time to time.[1] An ADI must still make deductions from Common Equity Tier 1 Capital that are required to be deducted under this Prudential Standard.

Definitions

12. The following definitions are used in this Prudential Standard:

(a) asset-backed commercial paper (ABCP) securitisation — a securitisation that predominantly issues commercial paper to investors with an original maturity of one year or less;

(b) basis swap — an interest rate swap aimed at limiting basis risk in a securitisation. For the purposes of this Prudential Standard, a basis swap includes a payment stream on one leg of the swap based on an observable market rate or index, and a payment stream on the other leg based on rates set by a party to the swap, typically the originating ADI;

(c) clean-up call — an option that permits the securitisation exposures to be called by the originating ADI or the special purpose vehicle (SPV) before all of the underlying exposures in the pool or securitisation exposures have been repaid or have matured. In the case of a traditional securitisation, this is generally accomplished by the purchase of the remaining securitisation exposures once the pool balance or outstanding securities issued by an SPV have fallen below some specified level. In the case of a synthetic

[1] *prescribed New Zealand authority* has the meaning given in subsection 5(1) of the Banking Act.

securitisation, a clean-up call may take the form of a clause that extinguishes the credit protection provided by the securitisation;

(d) credit enhancement — a contractual arrangement in which an ADI or other entity provides some degree of protection against credit losses to other parties holding a securitisation exposure;

(e) date-based call — an option that permits securitisation exposures to be called by the originating ADI or the SPV on a predetermined date before all of the underlying exposures in the pool or securitisation exposures have been repaid or have matured;

(f) early amortisation provision — a mechanism in a securitisation of revolving credit facilities that, once triggered, accelerates the reduction of the investor interest in the underlying exposures and allows investors to be paid out, in full or in part, prior to the originally stated maturity of the securities issued;

(g) excess spread (or future margin income) — finance charge collections and other income received by the SPV net of costs, interest and expenses;

(h) facility — a contractual arrangement between an ADI and an SPV for purposes including, but not limited to, the provision of liquidity or other funding, a servicer cash advance or a derivatives transaction in relation to a securitisation;

(i) gain on sale — an increase in an ADI's equity capital or assets as a result of originating exposures into a securitisation, such as recognition of capitalised expected future margin or servicing income, a profit on the sale of exposures or purchase of a residual income unit;

(j) implicit support — support provided by an ADI to a securitisation in excess of its explicit contractual obligations;

(k) liquidity facility — a facility provided by an ADI to an SPV for the primary purpose of funding any timing mismatches between receipts of funds on underlying exposures and payments on securities issued by the SPV or to cover the inability of the SPV to roll-over securities due to market disruption;

(l) managing ADI — an ADI that manages a securitisation. This includes undertaking responsibility for the day-to-day administration of the SPV, allocation of collections, calculation of payments and preparation of investor reports. A managing ADI may also manage swaps, liquidity and other facilities and events such as the issuance, rollover/refinancing or calling of securities;

(m) non-senior securities — debt securities issued in a securitisation which are non-senior securitisation exposures;

(n) non-senior securitisation exposure — a securitisation exposure that is subordinated to another securitisation exposure;

(o) originating ADI — with respect to a securitisation, an ADI that:

(i) directly or indirectly originates underlying exposures in the pool;

(ii) is the managing ADI for the securitisation; or

(iii) provides a facility (other than a derivatives transaction) or credit enhancement to an ABCP securitisation;

(p) pool — the underlying exposure or exposures that are securitised by way of assignment or the transfer of rights and obligations to, or by way of rights and obligations held directly in its name by, an SPV. The pool may consist of, but need not be limited to, loans, bonds or equities;

(q) resecuritisation exposure — a securitisation exposure in which at least one of the underlying exposures in the pool is a securitisation exposure. An exposure to one or more resecuritisation exposures is a resecuritisation exposure. An exposure resulting from retranching of a securitisation exposure is not a resecuritisation exposure if the ADI is able to demonstrate that the cash flows to and from the ADI replicate in all circumstances and conditions an exposure to a securitisation of a pool of assets that contains no securitisation exposures;

(r) securitisation — a financing structure where the cash flow from a pool is used to make payments on obligations to at least two tranches or classes of creditors (typically holders of debt securities), with each tranche or class entitled to receive payments from the pool before or after another class of creditors, thereby reflecting different levels of credit risk;[2]

(s) securitisation exposure — on-balance sheet and off-balance sheet risk positions held by an ADI arising from a securitisation including, but not limited to, investments in securities issued by an SPV, credit enhancements, liquidity and other funding facilities and derivatives transactions;

(t) securitisation of revolving credit facilities — a securitisation in which one or more underlying exposures represent, directly or indirectly, current or future draws on a revolving credit facility;

(u) self-securitisation — a securitisation which is solely for the purpose of using the securities created as collateral in order to obtain funding via a repurchase agreement with the Reserve Bank of Australia (**RBA**);

(v) seller interest — a senior or *pari passu* with a senior interest held by an originating ADI of a securitisation of revolving credit facilities that is

[2] Payments to investors depend upon the performance of the underlying exposures, as opposed to being derived from an obligation of the entity originating those exposures. The tranched structures that characterise securitisation differ from ordinary senior/subordinated debt in that non-senior securitisation tranches can absorb losses without interrupting contractual payments to senior tranches, whereas subordination in a senior/subordinated debt structure is a matter of priority of rights to the proceeds of liquidation.

collateralised by the revolving pool of underlying exposures, equivalent in size to the total asset pool less the investor interest;

(w) senior securities — debt securities issued in a securitisation which are senior securitisation exposures;

(x) senior securitisation exposure — a securitisation exposure effectively backed or secured by a first claim on the entire amount of the assets in the underlying pool. Securitisation exposures with different maturities that share *pro rata* loss allocation with senior securitisation exposures so that they benefit from the same level of credit enhancement, are themselves senior securitisation exposures;[3,4,5]

(y) SPV — a special purpose vehicle that purchases and holds, or otherwise holds directly in its name, the pool for the purpose of a securitisation. The SPV's acquisition of exposures held in the pool is typically funded by debt issued by the SPV, including through the issue of securities or units by the SPV;

(z) servicing ADI — a service provider that administers a pool for an SPV. This may include calculating account balances in relation to securitised loans as well as preparing borrowers' statements, collecting payments and calculating write-offs in relation to such loans;

(aa) synthetic securitisation — a securitisation whereby the credit risk, or part of the credit risk, of a pool is transferred to a third party which need not be an SPV. The transfer of credit risk can be undertaken through the use of funded (e.g. credit linked notes) or unfunded (e.g. credit default swaps) credit derivatives or guarantees; and

(bb) traditional securitisation — a securitisation where the pool is transferred (or assigned) to, and held by, or otherwise held directly in its name by, an SPV.

Separation and disclosure

Separation

13. There must be clear limitations governing the extent of an ADI's involvement in a securitisation. Any undertakings given by an ADI in a securitisation must be expressed clearly in the legal documentation relating to the securitisation and must be fixed as to time and amount.

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3 If a senior tranche is itself retranched or partially hedged, only the most senior tranche or hedged portion would be treated as senior for regulatory capital purposes.

4 Claims such as a swap claim, servicer cash advance, taxes and similar imposts and fees to service providers may be more senior in the cash flow waterfall and may be disregarded for the purpose of determining which positions are treated as senior.

5 The material effects of differing tranche maturities are captured by maturity adjustments to the risk weights assigned to the securitisation exposures under this Prudential Standard.

14. An ADI must, except in the case of a self-securitisation:[6]

    (a) deal with an SPV and the securitisation's investors on an arm's-length basis and on market terms and conditions; and

    (b) not provide, or knowingly create or encourage a perception that it will provide, implicit support for a securitisation.

Requirements for an SPV

15. In a securitisation, an SPV must satisfy the following criteria:

    (a) the SPV must be a corporation, trust or other entity organised for a specific purpose; and

    (b) the purpose of the SPV must be clearly defined as facilitating securitisation and the activities of the SPV must be limited to those associated with the securitisation.

16. In a securitisation, an originating ADI must not:

    (a) own or hold a material direct, indirect or beneficial interest[7] in any share capital, including ordinary shares or preference shares, of an SPV where the SPV is a corporation;

    (b) own or hold a material direct, indirect or beneficial interest in any share capital in the trustee where the SPV is a trust;

    (c) include, permit or acquiesce to the inclusion of the word 'bank', 'banking', 'building society', 'credit union', 'authorised deposit-taking institution' or 'ADI' in the name of an SPV;

    (d) allow any of the ADI's directors, officers or employees to sit on the Board of an SPV, or on the Board of a trustee of an SPV, unless the Board has at least four members. The ADI, however, may be represented by one director on a Board of four to six directors and by no more than two directors on a Board of seven or more directors;

    (e) act, or allow any of its directors, officers or employees to act, in any circumstances as a trustee of an SPV, or in any similar role. The trustee must not be part of the group, as defined in **Australian Accounting Standards**, to which the ADI belongs; or

    (f) be liable for the obligations and liabilities of the SPV, particularly in the event the SPV incurs losses.

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6 In a self-securitisation, the originating ADI may 'repurchase' securities issued by the SPV under the repurchase agreement with the RBA. In a self-securitisation, the originating ADI may also repurchase (or replace) exposures out of the pool held in the securitisation to meet a security's eligibility for purchase under the repurchase agreement with the RBA.

7 For the purpose of paragraph 16, any shareholding in an SPV over and above an entitlement to a residual interest distribution is considered material.

Disclosure

17. An originating ADI must ensure that there is clear and prominent disclosure to investors in a securitisation of the nature and limitations of the ADI's obligations arising from its involvement in a securitisation. Documentation or marketing of a securitisation must not give the impression that recourse to the ADI would extend beyond any specific undertakings to which the ADI has legally committed itself.

18. It must be clearly disclosed that an investment in the securitisation does not represent a deposit with, or other liability of, the originating ADI.

Exposures transferred in a securitisation

19. An originating ADI must not maintain effective or indirect control[8] over exposures transferred to an SPV. An originating ADI must not, except in the case of a self-securitisation:[9]

    (a) be obliged to retain the credit risk of the exposures; or

    (b) be obliged to repurchase the exposures out of the pool held by the SPV, except where an ADI is required to repurchase (or replace) an exposure as a result of a representation or warranty under paragraph 6(b) of Attachment A and paragraph 5(b) of Attachment B, where relevant.

20. The issued securities must not be obligations of the ADI. Investors in a securitisation may only have a claim on the relevant pool and any applicable facilities of the SPV.[10]

21. The holders of the securities issued by the SPV must have the right to pledge or exchange them without restriction, other than restrictions that are necessary for statutory compliance.

22. An originating ADI must not, except in the case of a self-securitisation:[11]

    (a) alter the underlying exposures such that the pool's credit quality is improved;

    (b) increase a retained first loss position or provide additional credit enhancement after the inception of the transaction;

    (c) increase the yield payable to the investors in a securitisation in response to a deterioration in the credit quality of the pool; or

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8 For the purpose of paragraph 19, an originating ADI's servicing of the exposures may not constitute effective or indirect control of the exposures provided the ADI complies with Attachment D.

9 Refer to footnote 6.

10 In a self-securitisation, the originating ADI may give an undertaking to 'repurchase' the securities under the repurchase agreement with the RBA.

11 Refer to footnote 6.

(d) in the case of a synthetic securitisation, limit the credit protection or credit risk transference[12] or increase the ADI's cost of credit protection in response to deterioration in the credit quality of the pool.

23. Representations and warranties provided by an ADI concerning the exposures transferred in a securitisation must:

(a) be provided at the time the exposures are transferred to the SPV;

(b) be provided by way of a formal written agreement and be in accordance with market practice;

(c) refer to an existing state of facts that is capable of being verified by the ADI, and is within the control of the ADI, at the time the exposures are transferred to the SPV; and

(d) not be open-ended or, in particular, relate to the future creditworthiness of the exposures, the performance of the SPV or the performance of the securities issued in a securitisation.

24. An originating ADI must ensure the document of transfer specifies that, if cash flows relating to an exposure in a pool are rescheduled or renegotiated, the SPV will be subject to the rescheduled or renegotiated terms.

25. An originating ADI must obtain written advice from legal counsel that:

(a) the exposures in the pool are legally isolated from the ADI in such a way that the exposures are put beyond the reach of the ADI and its creditors, including in the case of the appointment of a statutory manager (or its equivalent), or its winding up and receivership; and

(b) all agreements, deeds and other legal documentation relating to the securitisation are enforceable in all relevant jurisdictions.

Legal opinion

26. APRA may, at its discretion, require an ADI to seek a legal opinion on any of the requirements relating to separation and disclosure (paragraphs 13 to 18), exposures transferred in a securitisation (paragraphs 19 to 25) and any other requirement of this Prudential Standard, from an independent legal counsel chosen by APRA, at the expense of the ADI.

[12] For example, the instruments used to transfer credit risk in a synthetic securitisation must not contain clauses that allow for the early termination of the protection due to deterioration in the credit quality of the underlying exposures, significant materiality thresholds below which credit protection is deemed not to be triggered even if a credit event occurs or early amortisation provisions in a securitisation of revolving credit facilities that subordinate the originating ADI's interest.

General capital adequacy requirements

27. The capital treatment of a securitisation must be determined on the basis of its economic substance rather than its legal form.

Securitisation start-up costs

28. Where an ADI contributes to the start-up costs of a securitisation and these costs have been capitalised (rather than written off through the ADI's profit or loss), they must be deducted from the ADI's Common Equity Tier 1 Capital as capitalised expenses.

Spread accounts and similar surplus income arrangements

29. Where an originating ADI has included any gain on sale, including expected future margin or servicing income from a securitisation, on its balance sheet or in its profit, then it must, until such income is irrevocably received, deduct from its Common Equity Tier 1 Capital the amounts involved. Where an originating ADI provides funds to establish a reserve or similar account, those amounts must be deducted from Common Equity Tier 1 Capital until the funds are irrevocably received by the ADI.

30. Where an originating ADI provides a derivatives transaction (e.g. a basis swap or other interest rate swap) to a securitisation, a positive mark-to-market value of the swap represents the present value of certain future excess cash-flows generated by the asset pool. In this case an ADI must deduct from its Common Equity Tier 1 Capital any positive mark-to-market valuation that it has reported as an on-balance sheet asset or profit until such income is irrevocably received.

31. Where an originating ADI becomes, or is likely to become, a net payer over the life of a derivatives transaction (e.g. a basis swap or other interest rate swap), the ADI must deduct from Common Equity Tier 1 Capital the negative mark-to-market value of the swap where it has not reported such swap revaluation (expense) in its profit or loss.

Regulatory capital relief

32. Subject to meeting the operational requirements detailed in Attachment A, an originating ADI of a traditional securitisation may exclude the underlying exposures in the calculation of its **Regulatory Capital** for credit risk under *Prudential Standard APS 112 Capital Adequacy: Standardised Approach to Credit Risk* (APS 112) or *Prudential Standard APS 113 Capital Adequacy: Internal Ratings-based Approach to Credit Risk* (APS 113).

33. An originating ADI must hold regulatory capital in respect of credit risk for facilities or exposures to an SPV held by the originating ADI that relate to the pool (refer to paragraphs 41 to 44).

Funding-only securitisation

34. An originating ADI may treat a securitisation as funding-only, subject to meeting the operational requirements detailed in Attachment B. An originating ADI in a funding-only securitisation must include the underlying exposures in the pool in the calculation of its regulatory capital for credit risk under APS 112 or APS 113.[13]

35. For a funding-only securitisation, an originating ADI is not required to hold regulatory capital in respect of credit risk for facilities or exposures to the SPV held by the originating ADI that relate to the pool.

36. An originating ADI[14] of a securitisation of revolving credit facilities must treat the securitisation as a funding-only securitisation and comply with the operational requirements for funding-only securitisation (refer to Attachment B). APRA will not regard residential mortgages with redraw facilities as revolving exposures, i.e. a securitisation of revolving credit facilities, provided the redraws or further advances are not expected to be material in relation to the size of the pool.

37. An originating ADI[15] of an ABCP securitisation must treat the securitisation as a funding-only securitisation and comply with the operational requirements for funding-only securitisation (refer to Attachment B).

38. An originating ADI of a self-securitisation must treat the securitisation as a funding-only securitisation and comply with the operational requirements for funding-only securitisation (refer to Attachment B) from the time the securities are used as collateral in order to obtain funding via a repurchase agreement with the RBA.

Synthetic securitisation

39. An originating ADI of a synthetic securitisation must include the underlying exposures in the pool in the calculation of its regulatory capital for credit risk under APS 112 or APS 113.

40. For a synthetic securitisation, an originating ADI is not required to hold regulatory capital in respect of credit risk for facilities or exposures to the SPV held by the originating ADI that relate to the pool.

Treatment of securitisation exposures

41. Subject to paragraphs 35 and 40, an ADI must hold regulatory capital for credit risk against its securitisation exposures, including credit risk mitigation (CRM)

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13 For the purpose of paragraph 34, an originating ADI need not have regard to the interposed structure when assigning risk weights to the underlying exposures in the pool under APS 112 or APS 113.

14 For the purpose of paragraph 36, an originating ADI does not include an ADI whose role in a securitisation of revolving credit facilities is limited solely to managing the scheme.

15 For the purpose of paragraph 37, an originating ADI does not include an ADI whose role in an ABCP securitisation is limited solely to managing the scheme.

(i.e. eligible collateral, guarantees and credit derivatives) provided by the ADI to a securitisation exposure or to an underlying pool of exposures.

42. With the exception of those exposures required to be deducted from Common Equity Tier 1 Capital under this Prudential Standard, securitisation exposures must be risk weighted. The risk-weighted asset amount of a securitisation exposure is calculated by multiplying the exposure amount (paragraph 43) by the appropriate risk weight (Attachment C).

43. The exposure amount of a securitisation exposure for regulatory capital purposes is the sum of the on-balance sheet amount of the exposure (including the drawn amount of a facility), net of purchase price discounts and specific provisions, and the off-balance sheet exposure amount (including the undrawn amount of a facility), if any.

44. An ADI must measure the exposure amount of its off-balance sheet securitisation exposures as follows:

    (a) for off-balance sheet exposures subject to CRM, the treatment in paragraphs 45 to 50;

    (b) for derivatives transactions other than credit derivatives, the measurement approach that applies to the ADI under APS 112;

    (c) for undrawn servicer cash advances that meet the requirements of paragraph 3 of Attachment D, by applying a credit conversion factor (CCF) of ~~zero~~10 per cent; and

    (d) for all other exposures, by applying a CCF of 100 per cent.

Treatment of credit risk mitigation for securitisation exposures

45. An ADI must not recognise, for regulatory capital purposes:

    (a) tranched credit protection purchased on a securitisation exposure; or

    (b) credit protection purchased on a resecuritisation exposure or any other securitisation exposure required to be deducted from Common Equity Tier 1 Capital or any non-senior exposure.

46. An ADI may only recognise, for regulatory capital purposes, full (or *pro rata*) credit protection purchased on a senior securitisation exposure that is not required to be deducted from Common Equity Tier 1 Capital, in accordance with:

    (a) for eligible collateral, Attachment G to APS 112;[16]

    (b) for guarantees, Attachment I to APS 112;[17] and

[16] For this purpose, eligible collateral pledged by SPVs is recognised.
[17] For this purpose, SPVs are not recognised as eligible guarantors.

(c) for credit derivatives, Attachment J to APS 112.[18]

47. An ADI must hold regulatory capital for credit risk against an exposure arising from credit protection that it has sold.

48. An ADI that provides full or *pro rata* credit protection to a securitisation exposure must calculate regulatory capital as if it directly holds the securitisation exposure on which it has provided credit protection, in accordance with Attachment C.

49. An ADI that provides tranched credit protection to a securitisation exposure must calculate its regulatory capital requirement as if it is directly exposed to the particular sub-tranche of the securitisation exposure on which it is providing protection, in accordance with Attachment C.[19]

Maturity mismatches

50. A maturity mismatch exists when the residual maturity of a securitisation is less than the residual maturity of the pool. When credit protection is bought on a securitisation exposure(s), for the purpose of determining regulatory capital against a maturity mismatch, the capital requirement must be determined in accordance with:

(a) for eligible collateral, Attachment G to APS 112;

(b) for guarantees, Attachment I to APS 112; and

(c) for credit derivatives, Attachment J to APS 112.

Overlapping exposures

51. For the purpose of calculating regulatory capital, an ADI's exposure to a securitisation overlaps another of its exposures to the securitisation if, in all circumstances, the ADI precludes any loss for the ADI on its other exposure by fulfilling its obligations with respect to the first mentioned exposure. If an ADI can verify that fulfilling its obligations with respect to the exposure will preclude a loss from its other exposure under any circumstance, the ADI is not required to calculate regulatory capital for the other exposure.

52. Overlap may also be recognised between relevant capital charges for exposures in the trading book and capital charges for exposures in the banking book, provided the ADI is able to calculate and compare the regulatory capital charges for the relevant exposures.

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18 For this purpose, SPVs are not recognised as eligible credit protection providers.

19 In the case of tranched credit protection to a securitisation exposure, the original securitisation tranche is decomposed into protected and unprotected sub-tranches. The decomposition is not treated as a new securitisation transaction. The resulting sub-tranches are not considered resecuritisation exposures solely due to the presence of credit protection.

Operational requirements for the use of external credit assessments

53. Where an ADI has exposures to a securitisation, for the purpose of determining the regulatory capital requirement, the ADI may only use an external credit assessment that takes into account all amounts, both principal and interest, and any other amounts, owed to it.

54. For regulatory capital purposes, an ADI may only use external credit assessments of **ECAIs** that are published in a form accessible to Australian wholesale clients[20] and foreign entities and that are included in the ECAI's transition matrix. An eligible credit assessment, procedures, methodologies, assumptions and the key elements underlining the assessments by the ECAIs must be available to Australian wholesale clients and foreign entities, on a non-selective basis and free of charge. Also, loss and cash-flow analysis as well as sensitivity of ratings to changes in the underlying ratings assumptions must be available from ECAIs to Australian wholesale clients and foreign entities.

55. An ADI must apply the external credit assessments of an ECAI consistently across a securitisation. Where ECAIs assess the credit risk of the same securitisation exposure differently, Attachment F to APS 112 applies. An ADI must not use the external credit assessments issued by one ECAI for some tranches and those of another ECAI for other tranches within the same securitisation.

56. Where CRM is used on a securitisation exposure and this protection is reflected in the external credit assessment, an ADI must treat the exposure as if it is an unrated exposure and then apply the relevant CRM treatment detailed in APS 112 to recognise the credit protection for regulatory capital purposes.

57. An ADI must not use any external credit risk assessment for risk-weighting purposes where the assessment is at least partly based on unfunded support (e.g. a liquidity facility or credit enhancement) provided by the ADI.[21] In such cases, the ADI:

    (a) must continue to hold regulatory capital against the other securitisation exposures it provides (e.g. against the liquidity facility or credit enhancement);

    (b) must ensure the capital charge for such exposures held in the trading book is no less than the amount required under the banking book treatment; and

    (c) may recognise any overlap in its exposures consistent with paragraphs 51 and 52.

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20 For the purpose of paragraph 54, 'wholesale clients' has the meaning given by section 761A of the *Corporations Act 2001* (**Corporations Act**).

21 For the purpose of paragraph 57, a liquidity facility that only covers timing mismatches between receipts of funds on underlying exposures and payments on securities issued by the SPV, and is limited and sized as a relatively small proportion of the pool, is not considered 'unfunded support'. Derivatives transactions are not considered unfunded support where they do not provide credit enhancement.

Operational requirements for inferred ratings

58. In accordance with Attachment C, an ADI may infer a rating for an unrated securitisation exposure, provided the following operational requirements are satisfied:

    (a) the reference securitisation exposure (the externally rated securitisation exposure) cannot be senior in any respect to the unrated securitisation exposure. Credit enhancements, if any, must be taken into account when assessing compliance with this requirement. If the reference securitisation exposure benefits from any third-party guarantees or other credit enhancements that are not available to the unrated securitisation exposure, then the latter may not be assigned an inferred rating based on the reference securitisation exposure;

    (b) the maturity of the reference securitisation exposure must be equal to or longer than that of the unrated securitisation exposure;

    (c) any inferred rating must be updated on a regular basis to reflect any subordination of the unrated securitisation exposure or changes in the external rating of the reference securitisation exposure; and

    (d) the external rating of the reference securitisation exposure must satisfy the general requirements for recognition of external credit assessments (paragraphs 53 to 57).

Due diligence requirements

59. An ADI must perform due diligence on its securitisation exposures, including:

    (a) a comprehensive understanding of the risk characteristics of its individual securitisation exposures, whether on-balance sheet or off-balance sheet, as well as the pools underlying its securitisation exposures;

    (b) access to detailed performance information on the underlying pools which it reviews in a timely manner;

    (c) for resecuritisation exposures, access to information on the underlying securitisation tranches and on the risk characteristics and performance of the pools underlying the securitisation tranches which it reviews in a timely manner; and

    (d) a comprehensive understanding of all structural features of a securitisation transaction that may have a material impact on the ADI's exposures to the transaction.

60. An ADI must deduct from Common Equity Tier 1 Capital the value of any securitisation exposure where the requirements of paragraph 59 are not met.

Overcollateralisation arrangement

61. Where an originating ADI transfers exposures to an SPV below their book value (e.g. pursuant to an overcollateralisation agreement or by sale at a discounted price), the difference between the book value and the amount received by the ADI must be deducted from its Common Equity Tier 1 Capital unless it is written off through the ADI's profit or loss.[22]

Capital charge cap

62. An originating ADI that complies with the operational requirements for regulatory capital relief (refer to Attachment A) may apply a cap on the capital charge for securitisation exposures it holds equal to the capital requirement under APS 112 or APS 113, as appropriate, that would apply to the underlying exposures in the pool had they not been securitised.

Risk-weight cap for senior securitisation exposures

63. An originating ADI may apply a 'look-through' approach to senior securitisation exposures (other than those relating to resecuritisation exposures or other exposures that are required to be deducted from Common Equity Tier 1 Capital) so that they are subject to a risk-weight cap equal to the average risk weight that would apply to the underlying exposures in the pool, under either APS 112 or APS 113, had the underlying exposures not been securitised. Where an ADI is not an originating ADI, it may apply a risk-weight cap for senior exposures (other than those relating to resecuritisation exposures or other exposures that are required to be deducted from Common Equity Tier 1 Capital) so that they are subject to a risk-weight cap equal to the average risk weight that would apply to the underlying exposures in the pool under APS 112.

64. In order to apply the risk-weight cap under paragraph 63, an ADI must have a comprehensive understanding of the risk characteristics of the pool underlying the securitisation exposures.

65. Where the risk-weight cap results in a lower risk weight than the risk-weight floor of 15 per cent (refer to Attachment C), the 15 per cent risk-weight floor must be applied.

Cash collateral arrangements

66. Where cash collateral provided by an ADI to collateralise facilities and services provided by the ADI to an SPV is lodged in the name of the SPV, the ADI's exposure to the SPV must be treated as a securitisation exposure. Where treated as a securitisation exposure, the repayment of cash collateral must not be subordinated to any investor in the securitisation or subject to deferral or waiver. For the purpose of calculating regulatory capital, cash collateral, together with

[22] The deduction does not apply to an originating ADI where the originating ADI includes the underlying exposures in the pool in the calculation of its regulatory capital for credit risk under APS 112 or APS 113.

the relevant facility may be treated as overlapping securitisation exposures (paragraphs 51 and 52).[23,24]

Redraws and further advances to customers

67. An ADI that retains a contractual commitment to advance further funds to a customer under a redraw arrangement on a loan is required to hold regulatory capital against that commitment as an exposure to the customer according to the requirements of APS 112 or APS 113, as appropriate. Where:

    (a) the loan has been assigned to an SPV under a securitisation arrangement;

    (b) the ADI has provided a facility to the SPV to fund a contractual commitment of the SPV to acquire any further advances by the ADI on the underlying loan; and

    (c) the facility provided by the ADI complies with Attachment D of this Prudential Standard,

    the ADI is not required to include the undrawn commitment in its risk-weighted assets as an exposure to the customer. Instead, the ADI that provides the facility to an SPV must treat the facility as a securitisation exposure in accordance with this Prudential Standard.[25]

Shared collateral

68. Where an ADI retains an interest in collateral assigned to an SPV as a result of additional exposures secured against that collateral, such as an interest relating to arrangements to provide additional advances to customers, these additional exposures will not be eligible for a risk weight of less than 100 per cent unless a formal second mortgage arrangement is in place that meets the requirements of Attachment A of APS 112.

Implicit support and other risks

69. If APRA considers that an ADI is providing implicit support to a securitisation, or otherwise does not comply with this Prudential Standard, APRA may require the ADI to hold additional regulatory capital considered by APRA to be commensurate with the risk to the ADI arising from the support or other non-compliance.

70. If APRA considers that an ADI is providing implicit support to a securitisation, APRA may require the ADI to publicly disclose the implicit support.

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23 Services do not overlap as the cash collateral required to collateralise services provided by an ADI does not relate to any particular facility or other exposure.

24 An originating ADI is not required to hold regulatory capital for cash collateral where treated as a securitisation exposure, where the originating ADI includes the underlying exposures in the pool in the calculation of its regulatory capital for credit risk under APS 112 or APS 113.

25 An originating ADI is not required to hold regulatory capital for a redraw funding facility to the SPV, where the originating ADI includes the underlying exposures in the pool in the calculation of its regulatory capital for credit risk under APS 112 or APS 113.

71. If APRA considers that the risks arising out of securitisation are not adequately managed by the ADI holding additional regulatory capital, APRA may impose limits (both quantitative and qualitative) on the extent to which additional exposures may be securitised by the ADI, the extent to which additional securitisation exposures are acquired by the ADI or the extent to which additional services are provided by the ADI.

Risk management framework

72. An ADI must have, as part of its risk management framework (refer to *Prudential Standard CPS 220 Risk Management*), policies and procedures relating to its securitisation business. These policies and procedures must:

    (a) address the effects of an ADI's involvement in securitisation on its risk profile, including credit risk, liquidity risk and, where relevant, capital adequacy; and

    (b) address any reputational risk and how the ADI will ensure that it is not providing implicit support to a securitisation.

Self-assessment

73. An ADI must assess, in writing, each securitisation in which it participates. The assessment must demonstrate compliance with this Prudential Standard including, where relevant, the applicable regulatory capital treatment. An ADI must provide to APRA, upon request, copies of an assessment and any documentation (e.g. transaction and disclosure documentation) as well as any legal or accounting advice associated with its participation in the securitisation.

74. An originating ADI must designate a securitisation at inception as eligible for regulatory capital relief or as funding-only. An originating ADI must meet all requirements for either regulatory capital relief (including significant credit risk transfer) or for funding-only, from the inception of the securitisation upon such designation. An originating ADI must not switch treatment after designation, unless it switches from a funding-only securitisation to a securitisation for regulatory capital relief where it meets all the requirements for regulatory capital relief, including significant credit risk transfer.

Transitional provisions

75. For the purposes of these transitional provisions, 'the previous APS 120' means *Prudential Standard APS 120 Securitisation* made on 3 December 2014 by Banking (prudential standard) determination No. 7 of 2014.

76. An originating ADI may continue to exclude the underlying pool of exposures in the calculation of its regulatory capital for credit risk under APS 112 or APS 113 where the securitisation was in existence immediately prior to 1 January 2018 and in relation to which the originating ADI complied with the operational

requirements for regulatory capital relief of the previous APS 120. It may do so only until the first date at which a clean-up call may be exercised.[26]

77. For any services or facilities agreements which were in existence immediately prior to 1 January 2018 and in relation to which the ADI complied with the previous APS 120, the ADI may treat the services or facilities agreement as if the provisions of Attachment D of this Prudential Standard that are applicable to facilities and services agreements are met. It may do so only until either:

    (a) the termination of the agreement; or

    (b) the first date upon which the agreement may be renewed or cancelled, at the option of the parties to the agreement.

78. For the avoidance of doubt, an ADI eligible for transition under paragraphs 76 and 77 must hold regulatory capital in respect of credit risk for any facilities or exposures to an SPV in accordance with Attachment C.

Prior notification

79. Prior to entering into a funding arrangement involving an ADI providing another party an interest in the ADI's assets, the ADI must notify APRA of the proposed arrangement, except in relation to:

    (a) a covered bond issued consistent with Division 3A of Part II of the Banking Act;

    (b) a covered bond issued or originated by an overseas Level 2 banking subsidiary in accordance with the requirements of its regulator;

    (c) a securitisation that complies with the operational requirements for regulatory capital relief (refer to Attachment A);

    (d) a securitisation that complies with the operational requirements for funding-only (refer to Attachment B);

    (e) a synthetic securitisation that complies with the requirements in this Prudential Standard;

    (f) repurchase agreements over marketable (publicly rated, tradeable) securities;

    (g) securities lending agreements; or

    (h) agreements which provide for collateral as a part of over-the-counter or centrally-cleared derivatives transactions.

80. As part of its notification to APRA, an ADI must establish to APRA's satisfaction that the arrangement does not entail any other party to the arrangement achieving,

[26] In the absence of a clean-up call, an originating ADI must apply and APRA agree to a fixed period for transition.

even in limited or unlikely circumstances, an effective recourse to any pool of assets covered by the arrangement in preference to claims on assets of the ADI established under subsections 13A(3)(a) to (e) of the Banking Act.

81. In the event that an ADI cannot satisfy APRA as to the ADI's compliance with paragraph 80, the ADI must, for the purposes of calculating its capital adequacy (on both a Level 1 and Level 2 basis) under *Prudential Standard APS 110 Capital Adequacy*, deduct those assets in the pool from the ADI's Common Equity Tier 1 Capital, and not include those assets in the ADI's assets for the purposes of subsection 13A(4)(a) of the Banking Act.

82. For those arrangements where APRA is satisfied with an ADI's compliance with paragraph 80, APRA will notify the ADI how the ADI's exposures, if any, associated with the arrangement must be treated for the purposes of *Prudential Standard APS 111 Capital Adequacy: Measurement of Capital*, APS 112 or APS 113 or any other Prudential Standard, as relevant. APRA may determine that such exposures must also be deducted from the ADI's Common Equity Tier 1 Capital (on a Level 1 and Level 2 basis).

Adjustments and exclusions

83. APRA may adjust or exclude a specific requirement in this Prudential Standard in relation to an ADI.[27]

Previous exercise of discretion

84. An exercise of APRA's discretion (such as an approval, waiver or direction) under a previous version of this Prudential Standard continues to have effect as though exercised pursuant to a corresponding power (if any) exercisable by APRA under this Prudential Standard.

[27] Refer to subsection 11AF(2) of the Banking Act.

Attachment A — Operational requirements for regulatory capital relief

Significant credit risk transfer

1. In order to obtain regulatory capital relief, an originating ADI must ensure that significant credit risk associated with the underlying pool of exposures has been transferred to third parties. For this purpose, an originating ADI and any member of a group to which an ADI belongs[28] must not, in aggregate and at any time:

   (a) hold or fund the acquisition of more than 20 per cent of the non-senior securities issued in the securitisation, or more than 20 per cent of any tranche of non-senior securities issued in the securitisation; and

   (b) hold or fund the acquisition of non-senior securities and hold, fund or provide other loss positions or credit enhancements, which represent more than 20 per cent of the loss cover provided in the securitisation to support senior securitisation exposures.[29]

2. Where there are two or more originators of the underlying pool in a securitisation, an originating ADI must apply the tests in paragraphs 1(a) and 1(b) of this Attachment according to the proportion of assets originated by the ADI to the total amount of assets in the pool.[30]

3. Subject to paragraphs 1 and 2 of this Attachment, an originating ADI must sell non-senior securities issued in the securitisation to third parties. An originating ADI must not repurchase non-senior securities once sold except to give effect to a clean-up call that complies with paragraph 6(c) of this Attachment. An ADI must not recognise, for regulatory capital purposes, the use of CRM or any other hedge as constituting a sale of the non-senior securities.

Purchase of securities issued in a securitisation

4. Subject to paragraphs 1, 2 and 3 of this Attachment, an originating ADI may purchase securities issued in a securitisation, provided:

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28 This does not include a member of a group that acts independently on behalf of third parties e.g. statutory funds of life insurance companies, responsible entities, trustees or custodians acting on behalf of beneficiaries or members.

29 For the purpose of determining the amount of loss cover held, funded or provided by an originating ADI, an originating ADI may disregard any increase in loss cover arising from its entitlement to residual income.

30 In these circumstances, the maximum holding or funding of non-senior securities or holding, funding or provision of other loss positions or credit enhancements specified in paragraphs 1(a) and 1(b) of this Attachment are multiplied by the proportion of assets originated in the pool to the total amount of assets in the pool. The maximum holding or funding of non-senior securities or holding, funding or provision of other loss positions or credit enhancements for a managing ADI is based on the lowest proportion of assets originated into the pool by any originator, except in the case of a third party managing ADI (an ADI that does not contribute any assets into the pool), where the third party managing ADI must apply the tests in paragraphs 1(a) and 1(b) of this Attachment as if the ADI had originated all the assets in the pool.

(a) the purchase is conducted on an arm's-length basis and on market terms and conditions;

(b) the ADI has no pre-existing obligation to undertake the purchase; and

(c) the purchase does not give effect to a call option other than a clean-up call that complies with paragraph 6(c) of this Attachment.

5. If APRA considers that the pattern or the amount of an originating ADI's purchase of securities, or its stated willingness to do so, suggests that the ADI is providing implicit support to a securitisation, the provisions in paragraphs 69 to 71 of this Prudential Standard will apply.

Repurchase of exposures out of the pool in a securitisation

6. An originating ADI may only repurchase exposures out of the pool in a securitisation (or repurchase securities to give effect to a clean-up call) under the following circumstances:

(a) where an ADI grants a request for a further advance by a borrower or similar purpose:

(i) the purchase (or replacement) is conducted on an arm's-length basis and on market terms and conditions; and

(ii) the purchased exposures (or replaced exposures) are not in default;

(b) where an ADI is required to repurchase (or replace) an exposure as a result of a representation or warranty. In such a case the repurchase (or replacement) must be:

(i) completed in all respects within 120 days of the transfer of exposures in a securitisation; and

(ii) conducted on the same terms and conditions as the original transfer;

(c) for securitisation transactions that include a clean-up call:

(i) the exercise of the call must be at the full discretion of the originating ADI;

(ii) the call must not be structured to avoid allocating losses to the SPV or its investors, or positions held by investors or otherwise structured to provide credit enhancement; and

(iii) the call must only be exercisable when 10 per cent or less of the original underlying portfolio or securities issued remain outstanding.

7. In the case of paragraph 6(b) of this Attachment, after the expiry of the 120-day period an ADI must notify APRA of any instance where it has agreed to pay damages arising out of representations and warranties or where it has agreed to reassume the credit risk of any exposures. If APRA considers that the basis for or

the amount of damages paid, or assumption of credit risk by the ADI constitutes implicit support, then the provisions of paragraphs 69 to 71 of this Prudential Standard will apply.

8. In the case of paragraph 6(c) of this Attachment, an originating ADI must have regard to *Prudential Standard APS 210 Liquidity* (APS 210). An ADI must address the liquidity risk associated with clean-up call options through its liquidity risk management framework to measure, monitor and manage the relevant liquidity risk.

Permanency of funding

9. In order for an originating ADI[31] to achieve regulatory capital relief, the securitisation must have funding in place for the life of the underlying pool such that securities issued by the SPV will be sufficient to fund the exposures in the pool up to their longest contractual maturity date.

Securitisation of revolving credit facilities

10. Where an ADI's role in a securitisation of revolving credit facilities is limited solely to managing the scheme, in addition to paragraphs 1 to 8 of this Attachment, the ADI must ensure that scheduled amortisation, early amortisation or similar provisions, if triggered, do not:

    (a) subordinate, defer or waiver the receipt of contracted fees or other income for its role as manager; or

    (b) under any circumstance result in the ADI having an exposure to losses associated with the underlying pool of exposures, except for contracted fees or other income for its role as manager.

[31] For the purposes of paragraph 9 of this Attachment, an originating ADI does not include an ADI whose role in a securitisation of revolving credit facilities or ABCP securitisation is limited solely to managing the scheme.

Attachment B — Operational requirements for funding-only securitisation

Non-senior securities issued in a securitisation

1. Where a securitisation for funding-only purposes includes a date-based call option, non-senior securities must share *pro rata* loss allocation and must not differ in maturity.

2. An originating ADI must not repurchase previously sold non-senior securities except to give effect to a clean-up call that complies with paragraph 5(c) of this Attachment.[32]

Purchase of securities issued in a securitisation

3. Subject to paragraph 2 of this Attachment, an originating ADI may purchase securities issued in the securitisation, provided:

   (a) the purchase is conducted on an arm's-length basis and on market terms and conditions;[33]

   (b) the ADI has no pre-existing obligation to undertake the purchase;[34] and

   (c) the purchase does not give effect to a call option other than a call that complies with paragraph 5(c) or 5(d) of this Attachment.

4. If APRA considers that the pattern or the amount of an originating ADI's purchase of securities, or its stated willingness to do so, suggests that the ADI is providing implicit support to a securitisation, then the provisions in paragraphs 69 to 71 of this Prudential Standard will apply.

Repurchase of exposures out of the pool held in a securitisation

5. An originating ADI may only repurchase exposures out of the pool held in a securitisation or repurchase securities to give effect to a clean-up or date-based call under the following circumstances:

   (a) where an ADI grants a request for a further advance by a borrower or similar purpose:

      (i) the repurchase or replacement is conducted on an arm's-length basis and on market terms and conditions; and

      (ii) the repurchased exposures or replaced exposures are not in default;

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32 In a self-securitisation, the originating ADI may 'repurchase' securities issued by the SPV under the repurchase agreement with the RBA.

33 Refer to footnote 32.

34 Refer to footnote 32.

(b) where an ADI is required to repurchase (or replace an exposure) as a result of a representation or warranty. In such a case the repurchase or replacement must be:

(i) completed in all respects within 120 days of the transfer of exposures in a securitisation; and

(ii) conducted on the same terms and conditions as the original transfer;

(c) for securitisation transactions that include a clean-up call:

(i) the exercise of the call must be at the full discretion of the originating ADI;

(ii) the call must not be structured to avoid allocating losses to credit enhancements provided to the SPV or its investors, or positions held by investors or otherwise structured to provide credit enhancement; and

(iii) the call must only be exercisable when 10 per cent or less of the original underlying portfolio or securities issued remains outstanding;[35]

(d) for securitisation transactions that include a date-based call:

(i) the call relates to senior securities only;

(ii) the call date is set at the time the securities are issued;

(iii) the exercise of the call is at the full discretion of the originating ADI; and

(iv) the call is not structured to avoid allocating losses to credit enhancements provided to the SPV or its investors, or positions held by investors or otherwise structured to provide credit enhancement;

(e) in a self-securitisation, where the repurchase (or replacement) is to meet a security's eligibility for purchase under the repurchase agreement with the RBA.

6. In the case of paragraph 5(b) of this Attachment, after the expiry of the 120-day period an ADI must notify APRA of any instance where it has agreed to pay damages arising out of representations and warranties or where it has agreed to reassume the credit risk of any exposures. Should APRA consider that the basis for, or the amount of damages paid, or assumption of credit risk by the ADI constitutes implicit support, the provisions of paragraphs 69 to 71 of this Prudential Standard will apply.

[35] In the case of synthetic securitisation, the clean-up call must only be exercisable when 10 per cent or less of the original reference pool value remains.

7. In the case of paragraphs 5(c) and 5(d) of this Attachment, an originating ADI must have regard to APS 210. An ADI must address the liquidity risk associated with clean-up and date-based call options through its liquidity risk management framework to measure, monitor and manage the relevant liquidity risk.

Securitisation of revolving credit facilities

Revolving period of securitisation

8. An originating ADI's seller interest in the underlying exposures may have different principal allocation to other senior securitisation exposures but must not be subordinated with respect to cash flows (e.g. interest payments and expenses) and any losses associated with the underlying exposures.

Scheduled or early amortisation and similar provisions

9. Scheduled amortisation or early amortisation and similar provisions, if triggered, must not:

   (a) subordinate the originating ADI's seller interest in the underlying exposures to the interest of investors;

   (b) further subordinate the originating ADI's subordinated interest; or

   (c) in other ways increase the originating ADI's exposure to losses associated with the underlying exposures.[36]

10. Scheduled amortisation or early amortisation and similar provisions must end the ability of the originating ADI to add new exposures to the pool or fund within the pool further draws in relation to the underlying borrowers in the pool.

11. An originating ADI of a securitisation of revolving credit facilities must have regard to APS 210. The ADI must have in place appropriate liquidity plans that evaluate the probability of an early amortisation or similar provision occurring and address the implications of both scheduled and early amortisation through its liquidity risk management framework to measure, monitor and manage the relevant liquidity risk.

[36] Any pay-out arising from scheduled or early amortisation and similar provisions must be funded from the cash flows emanating from the existing pool of underlying exposures and provide for payments on a *pro rata* basis (principal repayment, interest payments and expenses) to the originating ADI and investors according to their interest in the pool.

Attachment C — Regulatory capital required for credit risk

1. An ADI must calculate regulatory capital for credit risk for its securitisation exposures using either of the following methods:

   (a) an ADI must use the External Ratings-based Approach (paragraphs 4 to 16 of this Attachment) where a securitisation exposure is externally rated (paragraphs 53 to 57 of this Prudential Standard) or for which an inferred rating is available (paragraph 58 of this Prudential Standard); or

   (b) where an ADI cannot use the External Ratings-based Approach, the ADI must use the Supervisory Formula Approach (paragraphs 17 to 34 of this Attachment).

2. The value of securitisation exposures to which none of the approaches in paragraph 1 of this Attachment can be applied must be deducted from Common Equity Tier 1 Capital.

3. An ADI must deduct the value of resecuritisation exposures from Common Equity Tier 1 Capital.

External Ratings-based Approach

4. For a securitisation exposure that is externally rated, or for which an inferred rating is available, the risk-weighted asset amount of a securitisation exposure must be calculated by multiplying the securitisation exposure amount (paragraph 43 of this Prudential Standard) by the appropriate risk weight (paragraphs 5 to 16 of this Attachment).

Short-term ratings

5. For securitisation exposures with short-term ratings, or when an inferred rating based on a short-term rating is available, the risk weights detailed in Table 1 apply.

   Table 1: Short-term credit rating grades and corresponding risk weights

Credit rating grade[37]	**1**	**2**	**3**	**4**
Risk weight	15%	50%	100%	Deduction from Common Equity Tier 1 Capital

[37] Refer to Table 3 of this Attachment.

Long-term ratings

6. For securitisation exposures with long-term ratings, or when an inferred rating based on a long-term rating is available, an ADI must apply:

   (a) the risk weights detailed in Table 2, adjusted for tranche maturity (paragraph 9 of this Attachment) and, where relevant, tranche thickness (paragraph 15 of this Attachment); or

   (b) the risk weights detailed in Table 2, commensurate with a 5 year tranche maturity.

7. The resulting risk weight under paragraph 6 of this Attachment is subject to a risk-weight floor of 15 per cent. The resulting risk weight must not be lower than the risk weight corresponding to a senior tranche of the same securitisation with the same rating and maturity.

Table 2: Long-term credit rating grades and corresponding risk weights

Credit rating grade[38]	**Senior securitisation exposure**		**Non-senior securitisation exposure**	
	Tranche maturity (M_T)		**Tranche maturity (M_T)**	
	1 year	**5 years**	**1 year**	**5 years**
1	15%	20%	15%	70%
2	15%	30%	15%	90%
3	25%	40%	30%	120%
4	30%	45%	40%	140%
5	40%	50%	Deduction from Common Equity Tier 1 Capital	
6	50%	65%		
7	60%	70%		
8	75%	90%		
9	90%	105%		
10	120%	140%		

[38] Refer to Table 4 of this Attachment.

Credit rating grade[38]	Senior securitisation exposure		Non-senior securitisation exposure	
	Tranche maturity (M_T)		Tranche maturity (M_T)	
	1 year	5 years	1 year	5 years
11	Deduction from Common Equity Tier 1 Capital			

8. For tranche maturity (paragraphs 9 to 14 of this Attachment), an ADI must use the linear interpolation between one and five years. For credit rating grade i and tranche maturity (M_T), the risk weight RW_{i,M_T} is calculated as:

$$RW_{i,M_T} = RW_{i,M_1} + \left(RW_{i,M_5} - RW_{i,M_1}\right) \times \left(\frac{M_T - 1}{4}\right)$$

Tranche maturity

9. For credit risk regulatory capital purposes, tranche maturity (M_T) is the tranche's remaining effective maturity in years and can be measured as either:

(a) the weighted-average maturity of the contractual cash flows of the tranche:

$$M_T = \frac{\sum_t t \times CF_t}{\sum_t CF_t}$$

where:

CF_t denotes the cash flows (principal, interest payments and fees) contractually payable by the borrower in period t.

The contractual payments must be unconditional and must not be dependent on the actual performance of the securitised assets;[39] or

(b) on the basis of final legal maturity of the tranche, calculated as:

$$M_T = 1 + (M_L - 1) \times 0.8$$

where:

M_L is the final legal maturity of the tranche.

[39] If such unconditional contractual payment dates are not available, the final legal maturity must be used.

10. When determining the maturity of a securitisation exposure, an ADI must take into account the maximum period of time it is exposed to potential losses from the securitised exposures.

11. Where an ADI provides a commitment, the ADI must calculate the maturity of the securitisation exposure resulting from the commitment as the sum of the contractual maturity of the commitment and the longest maturity of the assets to which the ADI would be exposed after a draw has occurred. If those assets are revolving, the longest contractually possible remaining maturity of the asset that might be added during the revolving period applies, rather than the (longest) maturity of the assets currently in the pool.

12. The treatment in paragraph 11 of this Attachment applies to all other instruments where the risk of the commitment/protection provider is not limited to losses realised until the maturity of that instrument (e.g. total return swaps).

13. For credit protection instruments that are only exposed to losses that occur up to the maturity of that instrument, an ADI may apply the contractual maturity of the instrument and need not look-through to the protected position.

14. In all cases, M_T is subject to a floor of one year and a cap of five years.

Tranche thickness

15. To account for tranche thickness, an ADI must calculate the risk weight for a non-senior securitisation exposure as follows:

*Risk weight = [risk weight from Table 2 after adjusting for tranche maturity] * [1 – min(T; 50%)]*

where:

T equals tranche thickness, and is measured as *D* minus *A*, as defined in paragraphs 27 to 31 of this Attachment.

Tranched credit protection

16. Where an ADI provides tranched credit protection[40] to a securitisation exposure, the relevant risk weights for the different sub-tranches are calculated subject to the following:

    (a) for the sub-tranche of highest priority, the ADI must use the risk weight of the original securitisation exposure; and

    (b) for the sub-tranche of lower priority, the ADI must treat the exposure as a non-senior securitisation exposure even if the original securitisation exposure prior to protection is a senior securitisation exposure.

[40] In the case of tranched credit protection, the original securitisation tranche is decomposed into protected and unprotected sub-tranches.

Supervisory Formula Approach

17. To calculate the regulatory capital requirement for a securitisation exposure using the Supervisory Formula Approach, an ADI must determine the following inputs:

    (a) the capital requirement under APS 112 had the underlying exposures not been securitised (K_{SA});

    (b) the ratio of delinquent underlying exposures to total underlying exposures in the pool (W);

    (c) the tranche attachment point (A); and

    (d) the tranche detachment point (D).

Definition of K_{SA}

18. K_{SA} is expressed in decimal form and is the weighted average capital charge of the entire portfolio of underlying exposures, which is calculated as the ratio of (a) the risk-weighted asset amounts under APS 112 multiplied by 8 per cent to (b) the sum of the exposure amounts of underlying exposures.[41]

19. For structures involving an SPV, all of the SPV's exposures related to the securitisation are to be treated as exposures in the pool. Exposures related to the securitisation that are treated as exposures in the pool include assets in which the SPV may have invested, comprising reserve accounts, cash collateral accounts and claims against counterparties resulting from interest rate or currency swaps.[42] An ADI may exclude the SPV's exposures from the pool for capital calculation purposes if the ADI can demonstrate that the risk of the SPV's exposures is immaterial or that it does not affect the ADI's securitisation exposure.

20. In the case of funded synthetic securitisations, any proceeds of the issuances of credit-linked notes or other funded obligations of the SPV that serve as collateral for the repayment of the securitisation exposure, and for which the ADI cannot demonstrate that they are immaterial, must be included in the calculation of K_{SA} if the default risk of the collateral is subject to the tranched loss allocation.[43]

21. In cases where an ADI has set aside a specific provision or has a non-refundable purchase price discount on an exposure in the pool, K_{SA} must be calculated using the gross amount of the exposure without the specific provision or non-refundable purchase price discount.

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41 K_{SA} is expressed as a decimal between zero and one (e.g. a weighted average risk weight of 100 per cent would result in K_{SA} equal to 0.08).

42 In the case of swaps other than credit derivatives, the numerator of K_{SA} must include the positive current market value multiplied by the risk weight of the swap provider multiplied by 8 per cent. The denominator must not take into account such a swap, as such a swap would not provide a credit enhancement to any tranche.

43 In the case of swaps other than credit derivatives, the numerator of K_{SA} must include the exposure amount of the collateral multiplied by its risk weight multiplied by 8 per cent. The denominator must be calculated without recognition of the collateral.

Definition of delinquent underlying exposures (W)

22. Delinquent underlying exposures are underlying exposures that are 90 days or more past due, subject to bankruptcy or insolvency proceedings, in the process of foreclosure, held as real estate owned or in default, where default is defined within the securitisation transaction documents.

23. The variable (W) represents the ratio of the sum of the nominal amount of delinquent underlying exposures to the nominal amount of underlying exposures.

24. The inputs K_{SA} and W are used as inputs to calculate K_A, as follows:

$$K_A = (1 - W) \times K_{SA} + W \times 0.5$$

25. In case an ADI is not aware of the delinquency status (paragraphs 22 and 23 of this Attachment) for no more than five per cent of underlying exposures in the pool, the ADI may use the supervisory formula approach by adjusting its calculation of K_A as follows:

$$K_A = \frac{Exposure_{Subpool\ \ where\ W\ known}}{Exposure_{Total}} \times K_A^{Subpool\ \ where\ W\ known} + \frac{Exposure_{Subpool\ \ where\ W\ unknown}}{Exposure_{Total}}$$

where:

Exposure is the exposure amount determined under APS 112.

26. If the ADI is not aware of the delinquency status for more than five per cent of the underlying pool, the securitisation exposure must be deducted from Common Equity Tier 1 Capital.

Definition of attachment point (A) and detachment point (D)[44]

27. The attachment point (A) represents the threshold at which losses within the underlying pool would first be allocated to the securitisation exposure. This input, expressed in decimal form, is the greater of:

    (a) zero; and

    (b) the ratio of (i) the outstanding balance of all underlying assets in the securitisation less the outstanding balance of all tranches that rank senior or *pari passu* to the tranche that contains the securitisation exposure of the ADI (including the exposure itself) to (ii) the outstanding balance of all underlying assets in the securitisation.

28. The detachment point (D) represents the threshold at which losses within the underlying pool result in a total loss of principal for the tranche in which a securitisation exposure resides. This input, expressed in decimal form, is the greater of:

    (a) zero; and

[44] Where the only difference between exposures to a transaction is related to maturity, A and D will be the same.

(b) the ratio of (i) the outstanding balance of all underlying assets in the securitisation less the outstanding balance of all tranches that rank senior to the tranche that contains the securitisation exposure of the ADI to (ii) the outstanding balance of all underlying assets in the securitisation.

29. Subject to paragraph 28 of this Attachment, for the calculation of A and D:

(a) overcollateralisation and funded reserve accounts must be recognised as tranches; and

(b) the assets forming these reserve accounts must be recognised as underlying assets.

30. Unfunded reserve accounts, such as those to be funded from future receipts from the underlying exposures (e.g. unrealised excess spread) and assets that do not provide credit enhancement, must not be included in the calculation of A and D.

31. In the case where an ADI provides tranched credit protection to a securitisation exposure, the parameters A and D must be calculated separately for each of the sub-tranches as if they would have been directly issued as separate tranches at the inception of the transaction. The value for K_{SA} is calculated on the underlying pool of exposures of the original transaction. For a sub-tranche of lower-priority, the ADI must treat the exposure as a non-senior securitisation exposure even if the original securitisation exposure prior to protection is a senior securitisation exposure.

Capital requirements as calculated under the Supervisory Formula Approach

32. The capital charge under the supervisory formula is calculated as follows:

$$K_{SSFA(K_A)} = \frac{e^{a \times u} - e^{a \times l}}{a \times (u - l)}$$

where:

$K_{SSFA(KA)}$ is the capital requirement per unit of the securitisation exposure, e is the base of the natural logarithm and the variables a, u, and l are defined as follows:

$$a = \frac{-1}{1 \times K_A}$$

$$u = D - K_A$$

$$l = max[(A - K_A), 0]$$

33. The regulatory capital requirement or risk weight assigned to a securitisation exposure is calculated as follows:

(a) when D for a securitisation exposure is less than or equal to K_A, the exposure must be deducted from Common Equity Tier 1 Capital;

(b) when A for a securitisation exposure is greater than or equal to K_A, the risk weight of the exposure, expressed as a percentage, equals $K_{SSFA(KA)}$ multiplied by 12.5; and

(c) when A is less than K_A and D is greater than K_A, the applicable risk weight is calculated according to the following formula:

$$RW = \left(\frac{K_A - A}{D - A}\right) \times 12.5 + \left(\frac{D - K_A}{D - A}\right) \times 12.5 \times K_{SSFA(K_A)}$$

34. The resulting risk weight is subject to a risk weight floor of 15 per cent.

APRA's discretion where capital requirement is uncertain

35. If the nature of a particular securitisation exposure is such that it is uncertain whether or how much regulatory capital is to be held in relation to the exposure under this Attachment, APRA may agree the amount of regulatory capital, or a method for calculating it, having regard to the nature of the exposure and the general approach taken to similar exposures under this Prudential Standard.

Mapping of rating grades for ~~Standard and Poor's, Moody's and Fitch~~External Credit Assessment Institutions

36. For the purposes of Table 1 of this Attachment, where the ECAI is ~~Standard and Poor's~~S&P Global Ratings, Moody's Ratings, ~~or~~ Fitch Ratings or Morningstar DBRS, the ratings are to be mapped to the relevant credit rating grades as shown in Table 3 below.

Table 3: Recognised short-term ratings and equivalent credit rating grades

Credit rating grade	~~Standard and Poor's~~S&P Global Ratings	Moody's Ratings	Fitch Ratings	Morningstar DBRS
1	A1	P1	F1	R-1
2	A2	P2	F2	R-2
3	A3	P3	F3	R-3
4	All other ratings	All other ratings	All other ratings	All other ratings

37. For the purposes of Table 2 of this Attachment, where the ECAI is Standard and Poor's, Moody's, ~~or~~ Fitch or Morningstar DBRS, the ratings are to be mapped to the relevant credit rating grades as shown in Table 4 below.

Table 4: Recognised long-term ratings and equivalent credit rating grades

Credit rating grade	~~Standard and Poor's~~S&P Global Ratings	Moody's Ratings	Fitch Ratings	Morningstar DBRS
1	AAA	Aaa	AAA	AAA
2	AA+	Aa1	AA+	AA (high)
3	AA	Aa2	AA	AA
4	AA-	Aa3	AA-	AA (low)
5	A+	A1	A+	A (high)
6	A	A2	A	A
7	A-	A3	A-	A (low)
8	BBB+	Baa1	BBB+	BBB (high)
9	BBB	Baa2	BBB	BBB
10	BBB-	Baa3	BBB-	BBB (low)
11	All other ratings	All other ratings	All other ratings	All other ratings

Attachment D — Facilities and services

Facilities and services

1. A facility or service provided by an ADI to a securitisation must comply with the following:

   (a) the facility or service must be expressly stated in a formal written agreement, specify the nature and extent of the ADI's obligations as the provider of the facility or service, and there must be no explicit or implied recourse to the ADI beyond the specified contractual obligations;

   (b) the facility or service must be provided on an arm's-length basis, be subject to the ADI's normal credit approval and review processes and be transacted on market terms and conditions;

   (c) the facility (other than a servicer cash advance facility (paragraph 3 of this Attachment)) or service must be limited to a specified amount and time period. The agreement must end no later than the earlier of the date on which all claims connected with the issue of securities are paid out and the ADI's replacement as party to the agreement. A fixed termination date need not be specified, provided the facility or service extinguishes at the earliest of the scheduled maturity of the securitisation or the date on which the securitisation winds up, and the ADI has the right, at its absolute discretion, to withdraw from the commitment at any time following a reasonable period of notice;

   (d) subject to reasonable qualifications, the SPV and/or investors must have the express right to select an alternative party to provide the facility or service; and

   (e) the facility or service must be documented in a manner that clearly separates it from any other facility or service provided by the ADI. The ADI's obligations under each facility or service must be stand-alone.

Liquidity or other funding facilities

2. In addition to the requirements in paragraph 1 of this Attachment, an ADI that provides a liquidity or other funding facility to a securitisation must ensure that:

   (a) the facility documentation clearly identifies and limits the circumstances under which it may be drawn;

   (b) drawdowns under the facility are limited to the amount that the ADI would consider likely at the time of drawdown and is capable of being fully repaid from the liquidation of the underlying exposures and any other credit enhancements;

   (c) the facility does not cover any losses incurred in the underlying pool of exposures prior to drawdown under the facility;

(d) in the case of a liquidity facility, the facility is not structured such that drawdown is certain as indicated by continuous draws;

(e) the facility must be subject to an asset quality test that precludes it from being drawn to cover credit risk exposures that are non-performing as defined in APS 220;

(f) the facility cannot be drawn after all applicable (e.g. transaction-specific and programme-wide) credit enhancements from which the facility would benefit have been exhausted; and

(g) the repayment of draws on the facility (other than a servicer cash advance facility (paragraph 3 of this Attachment)) must never be subordinated to any interests of any investor in the securitisation and not be subject to deferral or waiver.

Servicer cash advances

3. Servicer cash advances may be provided by a servicing ADI to avoid any short term limited interruption to the flow of payments to investors. In addition to the requirements in paragraphs 1 and 2 of this Attachment, except for the provisions relating to facilities in paragraph 1(c) of this Attachment and those relating to seniority in paragraph 2(g) of this Attachment, a servicing ADI must ensure that:

(a) it is entitled to full reimbursement under the cash advance;

(b) repayments of drawings under the cash advance rank the most senior to all other claims and must not be subject to deferral or waiver;[45] and

(c) the cash advance facility is limited to a specified amount and is unconditionally cancellable without prior notice by the servicing ADI. The cash advance facility must otherwise extinguish no later than the earlier of the scheduled maturity of the securitisation, or the date in which the securitisation winds up.

Derivatives transactions

4. Subject to paragraphs 5 and 6 of this Attachment, derivatives transactions conducted by an ADI in a securitisation must meet the requirements in paragraph 1 of this Attachment.

5. An originating ADI may provide a basis swap to an SPV that does not meet all the requirements of paragraph 1(b) of this Attachment provided the swap is constructed with sufficient margin such that the ADI is not expected to be a net payer over the life of the transaction, including in the event contingencies (e.g. changes in funding costs or changes in funding composition) that may affect the margin received or paid on the swap are triggered.

[45] Claims such as a swap claim, taxes and similar imposts, and fees to service providers may be more senior in the cash flow waterfall and these may be disregarded for the purpose of determining whether servicer cash advance facilities are treated as most senior.

6. Derivatives transactions conducted by an ADI in a securitisation must not be subordinated to any interests of any investor in the securitisation or subject to deferral or waiver.

Services

7. In addition to the requirements in paragraph 1 of this Attachment, an ADI that provides a service to a securitisation must ensure that the formal written agreement specifies the services to be provided and any required standards of performance. These standards must be reasonable and in accordance with normal market practice. The agreement must explicitly state that the ADI has no liability with regard to the performance of the pool.

8. There must not be an obligation for a servicing or managing ADI to remit funds to an SPV and/or investors until the funds are received from the pool, except where this is otherwise provided for in a separate facility (e.g. liquidity or other funding facility).

9. An originating ADI providing a service to a securitisation must not subordinate, defer or waive the receipt of contracted fees or other income for its role as a service provider.

Representations and warranties

10. An ADI that provides facilities or services to a securitisation may make representations and warranties concerning those facilities or services, provided the representations and warranties do not constitute implicit support. In particular, they must:

    (a) be provided by way of a formal written agreement and be in accordance with market practice;

    (b) refer to an existing state of facts that are capable of being verified by the ADI, and is within control of the ADI, at the time the facilities or services are contracted; and

    (c) not be open-ended and, in particular, not relate to the future creditworthiness of the exposures, the performance of the SPV or the securities issued in a securitisation.