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**COMMISSION STAFF WORKING DOCUMENT**  
**EXECUTIVE SUMMARY OF THE IMPACT ASSESSMENT**

*Accompanying the document*

**Proposal for a Regulation of the European Parliament and of the Council**  
**on sovereign bond-backed securities**

{COM(2018) 339 final} - {SEC(2018) 251 final} - {SWD(2018) 252 final}

## Executive Summary Sheet

Impact assessment on a proposal for an enabling regulatory framework for the development of sovereign bond-backed securities (SBBS).

### A. Need for action

#### **Why? What is the problem being addressed?** Maximum 11 lines

Sovereign Bond-Backed Securities (SBBS) are a novel financial instrument that could encourage banks to better geographically diversify their sovereign bond holdings. This would further weaken the bank-sovereign nexus and enhance private sector cross-border risk sharing. At the same time, it would help expand the supply of euro-denominated low-risk assets. In a nutshell, they could enhance the resilience and efficiency of the euro-area financial sector.

Yet their development is hindered by the fact that, currently, prudential regulation does not fully take into account the special nature of SBBS, by treating them as other regular securitisations. In particular, SBBS securitisations would not suffer any of opaqueness and adverse selection risks typical of more traditional securitisations, as they would be issued against a predetermined portfolio (with weights in line with ECB capital key) of such workhorse transparent, liquid and traded financial instruments as euro-area sovereign bonds.

Hence, the capital charges, liquidity discounts and investment limitations imposed on traditional securitisations are not warranted in the case of SBBS. Unless these are removed, SBBS remain too "costly" to hold (and thus uneconomical to produce), especially when compared with direct holdings of euro-area sovereign bonds.

#### **What is this initiative expected to achieve?** Maximum 8 lines

The initiative aims at removing extra costs (in terms of higher capital and liquidity requirements) associated with investing in SBBS compared with investing in euro-area sovereign bonds. It is thus expected to enable the demand-led development of an SBBS market.

#### **What is the value added of action at the EU level?** Maximum 7 lines

The regulatory hindrances currently faced by SBBS are the result of EU Regulations. Thus EU-level action is necessary to remove them. Member States' action is not only legally inadequate to remedy this situation because prudential regulation is an EU competence. It would also be suboptimal, as it could lead to a regulatory race to the bottom, it may fail to establish a unique standard (which is deemed necessary for the novel product to be liquid and thus appeal to potential investors), and could de facto result in obstacles to the Single Market (e.g., high compliance costs for an arranger that would want to operate in multiple jurisdictions).

### B. Solutions

#### **What legislative and non-legislative policy options have been considered? Is there a preferred choice or not? Why?** Maximum 14 lines

The IA proposes an enabling legislation that equates, in terms of regulatory treatment, (the senior tranche of) SBBS to euro-area sovereign bonds. It identifies three key policy choices: (1) the scope of applicability of the enabling framework (only to SBBS, or to any securitisation of euro-area sovereign bonds, regardless of the portfolio weights); (2) whether to "enable" all tranches or only the senior tranche; and (3) how to ensure compliance with the defined eligibility requirements. In addition, the IA consider the conceptually distinct but related option to provide the same treatment of sovereign bonds to a specific basket without tranching of euro-area central government bonds (i.e., one with weights in line with the ECB key), owing to it being a much simpler structure. Combining these options, the IA considers five possible models for the legislative proposal, and assesses them against the baseline scenario which is the status quo (i.e. no legislative intervention).

While solutions ("models") that are unlikely to result in a standardised product are assessed as inferior, the IA retains the other three models, i.e. granting the regulatory treatment of euro-area sovereign bonds to (1) all SBBS tranches, (2) only SBBS senior tranche, and (3) the basket. The IA does not rank these possible solutions, but highlights the main trade-offs involved. In particular, Models 1 and 2, by virtue of tranching, are better at expanding the supply of euro-denominated low-risk assets. Model 3 is, on the other hand, simpler.

#### **Who supports which option?** Maximum 7 lines

Banks (and other investors) would likely prefer Model 1, since this minimises their regulatory costs. The ESRB High Level Task Force (HLTF) on SBBS, which studied the feasibility and merits of SBBS, concluded in favour of Model 2. Debt management officers have expressed general reservations on the SBBS concept, out of concerns

that it might displace/disrupt national debt markets. Among the three Models retained, they are likely to prefer Model 2 (which is less enabling) or Model 3 (which introduces the least changes relative to the status quo).

### **C. Impacts of the preferred option**

#### **What are the benefits of the preferred option (if any, otherwise main ones)?** Maximum 12 lines

Estimating the impact of the preferred solutions in terms of reduced regulatory hurdles is complicated by the fact that none of the relative instruments currently exists, and that the amount of regulatory hurdles in the status quo, i.e. in the absence of any intervention, depends on how much, if at all, these would be held but for these regulatory hurdles (the fact that these products are currently not held is consistent with these regulatory hurdles being prohibitive). Nevertheless some indicative figures are provided in the IA. For example, under the current regulatory framework, if banks included in the EBA 2015 Transparency Exercise switched their sovereign bond holdings into senior SBBS they would face additional capital requirements to the tune of EUR 70 billion. Models 1 and 2 would bring this figure down to zero.

The benefits of enabling these new products would be significant. In particular, SBBS could help banks, insurance companies, pension funds and other investors to better diversify their sovereign exposures, which could further weaken the bank-sovereign nexus. They could also help expand the supply of a euro-denominated low-risk asset, which could elicit the appetite of global investors (thus, indirectly, expanding access to global savings in particular for small Member States) and, more generally, expand the toolkit for private sector risk sharing, including across borders.

The IA has attempted to provide a quantification of some of these effects by considering two scenarios, one in which the new markets only reach a limited size (EUR 100 billion), and a steady state scenario where they reach a macro-economically relevant size (EUR 1500 billion). The analysis shows that the preferred solutions, in particular those involving tranching, can contribute to a greater supply of low-risk assets and greater balance sheet diversification.

None of the options considered has any direct impact on the environment, the social milieu, or SMEs, though indirect positive impacts could result to the extent that the enabled new markets do enhance financial stability.

#### **What are the costs of the preferred option (if any, otherwise main ones)?** Maximum 12 lines

The costs of this legislative intervention are expected to be limited. For the public sector, aside for the one-off cost of drafting new legislation and putting it into force, limited additional costs—difficult to quantify with confidence—would arise since supervision of compliance could be carried out in the course of normal supervisory activities.

For the issuers, costs arising from arranging the product (buying sovereign bonds, warehousing the bonds, issuance of self-attestation, etc.) have been estimated by the HLTF at EUR 3.26 million per year for a EUR 6 billion SBBS programme (with one-off upfront costs in the order of EUR 1.15 million).

Debt Management Offices raised concerns that the introduction of SBBS could lead to higher financing costs for Member States, as liquidity in the underlying bond markets might decrease. A quantitative assessment carried out by the HLTF and summarised in Annex 4 of the IA suggests, also based on the experience with the ECB's Public Sector Purchase Programme, that such effects could be expected to be limited, if any, including because they would be offset by lower overall risk and greater bond demand, including from global investors.

No costs are envisaged for the environment, the social milieu, or SMEs.

#### **How will businesses, SMEs and micro-enterprises be affected?** Maximum 8 lines

No direct effect

#### **Will there be significant impacts on national budgets and administrations?** Maximum 4 lines

Not in the preferred solutions.

#### **Will there be other significant impacts?** Max 6 lines

No

### **D. Follow up**

#### **When will the policy be reviewed?** Maximum 4 lines

Sufficient data has to become available before the initiative can be reviewed. It is proposed to monitor the extent to which the new products are assembled and traded, and to assess the overall impact of the proposal after 5 years from the entry into force of the legislation.