

Clients & Friends Memo

The European Banking Authority has Published its Final Guidelines on WAM

12 May 2020

On 4 May 2020, the European Banking Authority (“**EBA**”) published a final report containing guidelines ([EBA/GL/2020/04](#)) (the “**Guidelines**”) on the use of the weighted average maturity approach (“**WAM**”) instead of the final legal maturity approach when calculating contractual payments due under the tranche of a securitisation transaction. This is relevant for institutions using the internal or the external rating-based approach for the calculation of their capital requirements under the EU Capital Requirements Regulation ((EU) 575/2013), as amended by the CRR Amending Regulation ((EU) 2017/2401) (“**CRR**”). CRR currently provides for tranche maturity as an additional parameter to calculate the capital requirement in respect of securitisation positions. The Guidelines highlight that institutions have the full discretion to choose between the two alternative approaches to determine the maturity of the tranche: (i) the WAM approach of the contractual payments due under the tranche, or (ii) the final legal maturity of the tranche. The intention of the Guidelines is to harmonise this process and to ensure that this process is simple, reliable and usable.

Market Practice

Many institutions already use WAM for various specific purposes such as for pricing and trading, return calculation, funding and risk analysis and hedging in respect of traditional securitisations. This WAM approach is more risk-sensitive (and therefore usually the preferred approach), whereas the final legal maturity approach is seen to be more conservative.

Traditional and Synthetic Securitisation

Traditional and synthetic securitisations generate different sources of cash flows, therefore, for the purpose of calculating WAM, the Guidelines provide for two methodologies:

Traditional Securitisations – the contractual payments due under the tranche are a combination of the (i) contractual payments of the underlying exposures payable to the securitisation special purpose entity (“**SSPE**”); and (ii) the contractual payments payable by the SSPE to the tranche holders.

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Synthetic Securitisations – for the originator and protection provider calculating the WAM, contractual payments due under the tranche should be understood as (i) contractual payments received by the originator from the borrowers of the underlying exposures allocated to the reduction of the outstanding amount of the tranche; and (ii) contractual payments of the premia payable by the originator to the protection provider.

Prepayments

In relation to prepayments, the Guidelines provide that this should also be calculated in the maturity of the tranche, as these are contractual features commonly taken into account in the market. Prepayment behaviour may vary depending on the asset type of the underlying assets and the jurisdictions. This is taken into account when calculating for traditional securitisations, where the Guidelines account for prepayments under strict conditions, in order not to discriminate against assets that show higher prepayment rates.

In contrast, in the case of synthetic securitisations, prepayments are not taken into consideration.

The Guidelines also show that market participants generally favour including prepayments in the calculation of the WAM to create an even playing field between EU jurisdictions and asset classes showing different level of prepayments.

The Guidelines will apply from 1 September 2020.

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If you have any questions, please feel free to contact any of the following Cadwalader attorneys.

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