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From:	General Secretariat of the Council
To:	Working Party on Financial Services and the Banking Union (Securitisation) Financial Services Attachés
Subject:	Securitisation Review: Presidency's discussion paper on the recognition of (re)insurance-based unfunded credit protection (UFCP) under the STS framework. Agenda item No. 6 - WP meeting of 22 September 2025

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PCY discussion paper on the recognition of (re)insurance-based unfunded credit protection under the STS framework - Working party 22 September 2025

Date: 15. Sep. 2025

Introduction

This non-paper builds on the Commission services' non paper on the same provision and aims to facilitate discussions on key issues and possible ways forward regarding the recognition of (re)insurance-based unfunded credit protection under the STS securitisation framework.

Should MS be open to exploring the potential for such recognition, the PCY presents in this non-paper different possibilities to adjust/enhance the safeguards.

1. Unfunded credit protection (UFCP)

COM proposal to allow UFCP under the STS-label, under certain specific safeguards, was received with mixed views.

Many MS was open to the concept but wanted more information on the expected scope of actors eligible to use UFCP and asked for the safeguards to be refined to ensure their intended effect.

On the contrary, some MS note that an increased role of UFCP would always increase the risk for banks and that allowing UFCP for STS-transactions might dilute/water down the label.

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Along these lines, the ESRB has raised concerns that the Commission's proposal could lead to an increase in both concentration risk and counterparty risk in its letter to the Chair of the Council Working Party dated 25 July 2025[1].

The concerns raised are addressed in some of the proposed options to adjust the safeguards, in particular section 2.2, which introduces a minimum credit rating to mitigate counterparty risk, and section 2.5, which addresses concentration risk by proposing a cap on the amount of unfunded credit protection that may qualify for STS treatment.

On the basis of the above, invite MS to share their views on whether they support the recognition of UFCP under the STS framework, possibly with adjustments to the safeguards. In the following section 2, the PCY invites MS to indicate how the safeguards should ideally be configured, should the recognition of UFCP for STS transactions be maintained going forward.

Questions on section 1 – UFCP
Option 1: Maintain the recognition of UFCP under the STS-framework (COM proposal).
Option 2: Maintain the recognition of UFCP under the STS-framework, but subject to enhanced safeguards
Option 3: Remove the recognition of UFCP under the STS-framework (status quo)
Q1: MS are invited to provide their views on the presented options and indicate which are preferred.

2. Appropriateness of the safeguards

2.1 Requirement to use an internal model for capital requirements on guarantees

According to the Commission Services' some insurers active in the 'Significant Risk Transfer' (SRT) securitisation market use the standard formula to calculate capital requirements. Insurers argue that obtaining internal model approvals is costly and time-consuming. In addition, internal model approvals are subject to varying levels of restrictiveness across MS, potentially creating barriers to participation and an uneven playing field.

[1] ESRB/2025/0092 – distributed to MS as part of the material for the 22. Sep. WP.

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Conversely, as highlighted in the Commission Services' non-paper, this criterion seeks to ensure that only insurers with robust, tailor-made risk management systems can qualify for STS treatment, thereby safeguarding the soundness and integrity of the label.

One MS has argued in writing that, given the need for specific knowledge and expertise in this market, the criterion should be made more explicit. In its view, the internal model should explicitly capture the specific features of the guarantee, and enhanced governance arrangements should be in place. While such specifications could indeed provide additional safeguards, the PCY notes that they raise potential issues of enforceability. In practice, how could an originating bank be expected to verify whether an insurer's internal model adequately reflects the features of a given guarantee, or whether the governance arrangements are sufficiently robust?

Finally, some industry stakeholders argue that relying on an internal model is not the appropriate way to assess sound risk management.

Questions on section 2.1 – Requirement to use an internal model
Option 1: Keep the criterion as it stands (COM proposal)
Option 2: Strengthen the criterion – please specify how it can be formulated as an objective and verifiable assessment by the originating bank.
Option 3: Keep the criterion as it stands, but add safeguards – which would not need to be assessed ex ante by the originating bank – for insurers providing STS-compliant unfunded credit protection (e.g. on governance); please specify which additional obligations insurers should fulfil.
Option 4: Delete the criterion but introduce instead safeguards – which would not need to be assessed ex ante by the originating bank – for insurers providing STS-compliant unfunded credit protection (e.g. on governance); please specify which additional obligations insurers should fulfil.
Q2: MS are invited to provide their views on the presented options and indicate which they prefer, specifying details where applicable.

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2.2 Requirements to comply with capital requirements and to have at least a BBB rating

Requirement to comply with capital requirements

According to the Commission Services' non-paper, most EU insurers would meet the Solvency Capital Requirement (SCR) and the Minimum Capital Requirement (MCR). While the market may implicitly require capital buffers above regulatory minima, such buffers would not be legally mandated. On the other hand, Solvency II does not trigger automatic supervisory action above the SCR threshold.

Questions on section 2.2 – Requirement to comply with capital requirements
Option 1: Keep the criterion as it stands (COM proposal)
Option 2: Strengthen the criterion or add safeguards – please specify
Q3: MS are invited to provide their views on the presented options and indicate which they prefer, specifying details where applicable.

Requirement to be assigned to credit quality step 3 or better

The Commission Services' non-paper explains that this criterion received some support during the expert group meeting on securitisation of 7 May 2025. A credit quality step 3 corresponds to a BBB rating, though originating banks may prefer a minimum A rating (credit quality step 2) to mitigate cliff effects in case of downgrades.

In addition, one MS has argued that the requirement should be better aligned with Article 249 of Regulation 575/2013 ('CRR'), to enhance consistency with the treatment of other counterparties. This would imply that the criterion would be that the (re-)insurer has been assigned to credit quality step 2 or above at the time the credit protection was first recognised and is currently credit quality step 3 or above.

Finally, the PCY notes that the wording in the COM proposal does not specify who 'assigns' the credit quality step. While it could be argued that the expectation is that the provider of the unfunded credit protection is subject to external credit rating, the proposal does not exclude that the rating can be assigned by the originating bank itself, which would raise issues of conflicts of interest.

Questions on section 2.2 – Requirement to be assigned to credit quality step 3 or better

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Option 1: Keep the criterion as it stands (COM proposal)
Option 2: Strengthen the criterion and require 'at least' credit quality step 2
Option 3: Align the criterion with Article 249 of CRR
Q4: MS are invited to provide their views on the presented options and indicate which they prefer, specifying details where applicable.
Q5: MS are invited to indicate whether the prefer that it is clarified in the legal text that the rating must be assigned by a nominated External Credit Assessment Institution (ECAI).

Addressing procyclicality risks

One MS has argued that the solvency criterion could create procyclical dynamics. The PCY notes that a risk arises under the 'rating' criterion. COM proposal does not foresee any transitional arrangement. As a result, if an insurer ceases to meet the eligibility criteria, i.e. following a deterioration in its credit rating or a breach of the Solvency Capital Requirement (SCR), the STS label would be lost immediately. This would automatically trigger higher risk weights for the bank holding the securitisation position, potentially leading to unintended cliff-edge effects.

Should transitional arrangements be considered to address such transmission channels from (re-)insurers to originating banks, the PCY identified two possible approaches:

- A 'grace period' for persistent non-compliance: The loss of STS status would only occur if the insurer continuously fails to meet the criteria for a specified period (e.g. 6 to 9 months – mirroring the timeframe within which an insurer is required to restore compliance with its SCR under Solvency II)
- Temporary preservation of STS status pending replacement: STS status could be maintained for a limited period (same period as above), but only in order to allow for the replacement of the ineligible insurer by an eligible one, provided such replacement is foreseen in the contractual documentation and subject to the approval of the originator.

Questions on section 2.2 – Addressing procyclicality risks

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Option 1: Do not introduce transitional arrangements (COM proposal)
Option 2: Introduce transitional arrangements – please specify
Q6: MS are invited to provide their views on the presented options and indicate which they prefer.

2.3 Requirement to effectively operate in at least two non-life insurance classes

As explained in the Commission services' non paper, this criterion seeks to ensure a minimum level of business diversification. It aims to exclude undertakings that are technically authorised for two classes but lack substantive activity in one of them.

During the expert group meeting on securitisation of 7 May 2025, concerns have been raised that credit and suretyship insurance – although corresponding to two distinct insurance classes – are part of the same line of business for prudential purposes and are highly correlated. Another MS has argued that the requirement should be to operate in at least three insurance classes, since credit and suretyship insurer also operating in 'miscellaneous financial loss' as an ancillary activity should not be deemed diversified[2]. Another MS suggested that the criterion should not be considered to be met where the two classes are positively correlated[3].

Some stakeholders suggest referring to "lines of business" (LoBs) instead of "classes of insurance", as the former offers more granularity and transparency through disclosures in the solvency and financial condition report (SFCR).[4] Using LoBs could therefore allow for a more objective test of business diversification. For instance, a requirement could be framed such that an undertaking must operate in at least [two] LoBs, each representing a minimum share of total technical provisions. However, this would require additional technical specifications, such as whether to measure provisions on a gross or net (of reinsurance) basis.

2 The PCY notes however that 'credit insurance', 'suretyship insurance' and 'miscellaneous financial loss' are three different insurance classes under Solvency II. Therefore, requiring at least three classes of insurance would not exclude the insurers described by that MS.

3 However, it is not indicated who should specify which asset classes are positively correlated.

4 The nonlife lines of business are not directly set out in the Solvency II Directive. However, they are listed in Annex I of Delegated Regulation (EU) 2015/35, pursuant to the empowerment in Article 86 of the Directive.

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Finally, the PCY notes that the diversification requirement focuses on non-life insurance classes. This means that pure reinsurers which only have a reinsurance license would not fulfil the criterion. As LoBs include both insurance and reinsurance activities, they may offer a more 'inclusive' yet meaningful test of diversification.

Questions on section 2.3 – qualitative nature of the criterion:
Option 1: Keep reference to classes of insurance and make no additional change (COM proposal)
Option 2: Keep reference to classes of insurance and adjust the criterion so that 'pure' reinsurers are not automatically excluded – please specify.
Option 3: replace reference to classes of insurance with reference to 'lines of business'[5] and make no additional change.
Option 4: replace reference to classes of insurance with reference to 'lines of business' and make the criterion quantitative by specifying that there are at least two lines of business[6] each representing no less than a certain percentage of total technical provisions.
Q7: MS are invited to provide their views on the presented options and indicate which they prefer, providing details where applicable.
Questions on section 2.3 – 'correlated' business areas:
Option 1: Keep COM proposal
Option 2: Increase the threshold from 2 classes of insurance to 3 or 4
Option 3: Explicitly specify that operating only in credit, suretyship and miscellaneous financial loss is not sufficient to meet the criterion.

[5] Would facilitate the eligibility of reinsurers and treat credit and suretyship as one single activity.

[6] Or, depending on the answer to Topic 1, three or four

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Q8: MS are invited to provide their views on the presented options and indicate which they prefer.

2.4 Minimum size requirement

This size threshold has raised some reactions from stakeholders:

1. The term "assets under management" is deemed ambiguous by some MS. The PCY notes that EIOPA used 'total assets' for its impact assessment.
2. Clarity is needed on whether the reference is to the prudential or accounting balance sheet. Accounting references are globally applicable but inconsistent in valuation rules. Prudential references ensure harmonisation but may exclude third-country firms. Note that scope and methods of consolidation may also differ between accounting and prudential frameworks.
3. Some argue the EUR 20 billion threshold is too high and suggest using a consolidated level. However, this could widen the scope excessively and blur distinctions between life and non-life activities[7].

Questions on section 2.4 – denomination:
Option 1: no change – continue using 'assets under management' (COM proposal)
Option 2: replace with the term 'total assets'
Option 3: replace with the term 'total assets' and specify that the quantification is under Solvency II framework.
Q9: MS are invited to provide their views on the presented options and indicate which they prefer.
Questions on section 2.4 – quantitative threshold:

[7] The size of the life business could help facilitate fulfilling the criterion, although there seems to be quite some consensus that the STS label should not be possible when the unfunded credit protection is provided by a life company.

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Q10: MS are invited to provide their views on the threshold of the minimum size requirement.

2.5 Possible other criteria

One MS has argued that in order to limit exposure to the risks stemming from unduly concentrated unfunded credit protection insurance, the criteria should limit credit protection insurance activity as a percentage of technical provisions, sums insured and/or written premiums of the undertaking in order for the exposures it covers to be considered STS-compliant. That MS also suggested that additional criteria based on the relative share of unfunded credit protection among the other guarantees issued by the insurer could also be considered.

Questions on section 2.5 – Possible other criteria
Option 1: no further change (COM proposal)
Option 2: add a limitation or cap to the amount of unfunded credit protection provided by (re-)insurers for such credit protection that can be STS-eligible
Option 3: other safeguards – please specify
Q11: MS are invited to provide their views on the presented options and indicate which they prefer, specifying details where applicable.

3. Applicability of the criteria to third-country (re)insurers

Several proposed criteria refer to Solvency II concepts:

- The use of an internal model pursuant to Articles 112 and 113 of Directive 2009/138/EC;
- Compliance with the SCR and MCR referred to in Articles 100 and 128 of Directive 2009/138/EC, respectively.

Depending on the answers to the questions in Section 1, other criteria may become even more Solvency II-centred.

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These criteria, if strictly applied, would *de facto* exclude non-EU (re)insurers. The Commission Services' non-paper notes that the majority of insurers active in the SRT market are headquartered outside the EU. Therefore, with COM proposal, to qualify, they would have to establish a subsidiary in the EU in order to be eligible for the STS label.

Should MS wish to ensure that the criteria do not exclude third-country participants, the following issues would have to be considered:

- As explained in the Commission services' non-paper, the requirement to use an internal model ensures robust risk modelling. However, certain large non-EU jurisdictions do not allow the use of an internal model, or apply lower standards to them;
- Similarly, while certain jurisdictions have obtained full or provisional equivalence in relation to solo supervision[8], this is not the case for others in which (re)insurers that are active in the synthetic securitisation market are headquartered. On the other hand, a simple requirement that insurers comply with their local requirements – even in non-equivalent jurisdictions – may be deemed as setting too low a standard.

Expanding the eligible pool to include third country (re)insurers could facilitate credit risk transfer from EU banks, offering additional flexibility to the market. However, it may also shift prudential risk outside the EU regulatory perimeter. While this could avoid cross-sectoral exposures between EU banks and EU insurers, it may underestimate the counterparty risk borne by EU banks vis-à-vis non-EU entities, especially in the absence of equivalent supervisory safeguards.

By contrast, limiting eligibility to EU-based (re)insurers would reinforce legal certainty, ensure regulatory oversight under Solvency II, and preserve the credibility of the STS label by avoiding dilution of prudential standards. However, it would restrict third-country insurers' ability to participate to the synthetic unfunded STS market.

Questions on section 3 – Applicability of the criteria to third-country (re)insurers
Option 1: third-country (re)insurers should not be eligible.
Option 2: third-country (re)insurers should be eligible, but only for (provisionally/temporarily) equivalent third countries within the meaning of Solvency II.

[8] Equivalence within the meaning of Article 227 of Directive 2009/138/EC

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Option 3: third-country (re)insurers should be eligible.
Q12: MS are invited to provide their views on the presented options and indicate which they prefer, specifying details where applicable.
Q13: Assuming we move forward with Option 2 or Option 3, MS are asked to indicate their views on: **- how the internal model requirement be adapted for jurisdictions with different rules or standards.** **- Whether the solvency requirements should include a buffer to address non-equivalence.** **- Whether further adjustments are needed for other criteria.**