Clients&FriendsMemo

Next Steps in the Proposed Replacement of the UK Securitisation Regulation

10 August 2023

Background

Following closely behind the consultation paper from the Prudential Regulation Authority ("**PRA**") (for more discussion see our briefing of 1 August), the UK's Financial Conduct Authority ("**FCA**") has published its proposed new rules relating to securitisations in Consultation Paper CP23/17 (the "**FCA CP**"). As with the PRA's consultation, the FCA CP sets out the firm-facing provisions of the UK Securitisation Regulation (Securitisation Regulation (EU) 2017/2402 as onshored) (the "**UK SR**") currently in force as retained EU law and for which the FCA has supervisory responsibility. These provisions will now be FCA rules, and will be set out in a new Securitisation Sourcebook "**SECN**' (see Annex 4 of the FCA CP).

Takeaways

- The proposals in the FCA CP are in line with the proposals in the PRA CP.
- Taken together, (i) this FCA CP, (ii) the PRA consultation paper and (iii) the near-final statutory instrument for the new Securitisation Regulations to repeal the UK SR (including all related SIs and technical standards) while keeping part of it in new legislation, give an overview of the proposed replacement of the UK SR.
- The FCA CP also flags to market participants that another consultation will focus on the adjustment of the disclosure rules, and introduces some possible approaches to distinguish between public and private securitisations**,** with the suggestion that the disclosure templates for private securitisations may be simplified. Market participants have invested in systems designed to comply with the disclosure requirements, therefore those changes, if and when implemented, will have a significant impact.

Scope

Under the Financial Services and Markets Act 2023 ("**FSMA**"), a new Designated Activities Regime or "**DAR**" gives the FCA powers to make rules covering designated activities carried out by authorised and unauthorised firms. The new Securitisation Regulations (currently in the form of a near-final statutory instrument) specify that acting as an originator, sponsor, original lender or securitisation special purpose entity ("**SSPE**") is a designated activity within the scope of the DAR, and the FCA CP therefore proposes rules covering: (i) risk retention requirements; (ii) transparency obligations; (iii) resecuritisation restrictions and (iv) credit granting standards for all

authorised and unauthorised originators, sponsors, original lenders and SSPEs that are not PRA-authorised firms. The FCA is also making rules for:

a. Simple Transparent and Standardised ("**STS**") securitisations for all UK originators and sponsors;

b. Sales of securitisation positions to UK retail customers for all UK sellers;

c. Due diligence requirements for small, registered UK Alternative Investment Fund Managers ("**AIFM**"); and

d. Securitisation repositories ("**SR**") and third party verifiers ("**TPV**").

As with the PRA's consultation exercise, this FCA rule-making exercise intends to 'largely preserve the current requirements' but also proposes to:

a. Clarify due diligence obligations for UK institutional investors;

b. Clarify risk retention requirements, particularly for non-performing exposure ("**NPE**") securitisations;

c. Make a number of other clarificatory changes; and

d. Open a discussion on the definitions of public and private securitisations with a view to consulting later this year on changes to the reporting regime particularly for private securitisations.

Below, we summarise the FCA approach in this FCA CP.

Due Diligence Requirements for Institutional Investors

The FCA proposes that:

a. the information described in what were points (b), (c) and (d) of what was Article 7 (1) of the UK SR must be made available before pricing at least in draft form, with final versions made available within 15 days of the closing of the transaction.

b. due diligence rules preserve the exemption (previously only in recital 14 of the UK SR) under which credit-granting criteria need not be met with respect to trade receivables not originated in the form of a loan.

c. where a delegating party authorises a managing party (that is an institutional investor, but not an occupational pension scheme) to make investment management decisions that might expose it to a securitisation, and the delegating party delegates to the managing party the related regulatory obligation to conduct due diligence, then responsibility passes to the institutional investor which conducts it.

NPE Securitisations and Risk Retention

The FCA CP proposes the use of a non-refundable purchase price discount in the risk retention requirements for NPE securitisations. As a result, risk retention would be calculated on the basis

of the net value of the defaulted portfolio on the date of the securitisation, as opposed to the face value of the underlying assets.

Resecuritisation

The FCA CP proposes to clarify that:

a. in resecuritisations that may be permitted, a retainer shall retain the material net economic interest in relation to each of the respective transaction levels, which is consistent with the purpose of risk retention restrictions;

b. fully supported ABCP programmes that are not considered to be resecuritisations for the purposes of Article 8 of the UK SR would also not be considered as resecuritisations for risk retention purposes; and

c. the retranching of an issued tranche into contiguous tranches by the securitisation's originator does not amount to resecuritisation for purposes of the risk retention.

Geographical Scope

The FCA proposes to limit expressly the application of the FCA rules to entities, including manufacturers, established in the UK (apart from the definition of "institutional investors" because its scope is set out in the SI). "Established" will mean an entity which is constituted under UK law with a head office, or, if it has one, a registered office in the UK.

Public vs Private Securitisations

Disclosure templates are designed to standardise reporting across different asset classes and Article 7 of the UK SR introduces a distinction between private and public securitisations. Public securitisations are described as having a section 85 prospectus under the FSMA 2000. Broadly speaking, this means that public securitisations are those traded on a UK regulated market.

Two potential issues have been identified with the current framework.

a. To be considered as public, the UK SR requires securitisations to be listed on a UK regulated market. However, a number of UK securitisations have sought admission to regulated markets elsewhere (mostly in the EU). Further, some UK securitisations with characteristics akin to public transactions are not captured by the definition because they are listed on non-regulated markets, such as Euronext's Global Exchange Market (GEM), which is a multilateral trading facility (MTF) in Ireland, and continue to be largely listed there.

b. Current reporting requirements for transactions (especially private ones) may not always be proportionate, and the information reported is not always useful to investors. This is partly because the legal definition of a securitisation is broad and includes transactions which go beyond well understood securitisation transactions, such as traditional RMBS.

The FCA is proposing to expand the current description of public securitisations to cover securitisations that are public in substance, i.e. what the market would recognise as a publicly distributed and traded transaction:

a. The public securitisation description would cover securitisations that are subject to primary listings (i.e., listings a manufacturer has requested) on UK regulated markets or appropriate

equivalent non-UK venues. This would only apply to UK securitisations, i.e., where the originator, sponsor or SSPE is located in the UK.

b. The public securitisation description would cover primary admissions to trading on an appropriate UK MTF and similar non-UK venues, where there is at least one UK manufacturer.

c. The public securitisation description would also include securitisations where there is at least one UK manufacturer and where a public announcement or other general communication is made to a wide audience of potential investors, intended to solicit orders or expressions of interest as part of the primary marketing of the securitisation.

Together with the PRA, the FCA is considering whether the disclosure templates for "private" securitisations could be made more proportionate or principles-based, whilst still supporting the provision of sufficient information by manufacturers of securitisations to investors and the FCA will look to consult on proposals to the disclosure templates in a later consultation.

Next Steps

Comments are due by 30 October 2023 and implementation is expected in Q2 2024. As no changes to reporting templates or transparency requirements are being proposed, implementation can take place when final rules are made.

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