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CLIENT BRIEFING

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THE NEW SECURITISATION RULES

On 30 April 2024, both the Financial Conduct Authority (FCA) and the Prudential Regulation Authority (PRA) published policy statements containing the updated rules relating to securitisation. The FCA released PS 24/4: Rules Relating to Securitisation and the PRA released PS 7/24 - Securitisation: General Requirements.

BACKGROUND

The new securitisation rules will apply from 1 November 2024, subject to the government revoking the UK Securitisation Regulations and the related technical standards (UKSR).

Worth noting is that the commencement order that will bring into force the revocation of the UKSR has not yet been made. The government anticipates making this commencement order once The Securitisation (Amendment) Regulations 2024 come into force on 1 November 2024. Consideration will be given to delaying or revoking the FCA's and PRA's rules if the commencement order is not made at the same time.

As part of the Treasury's Smarter Regulatory Framework, some provisions of the UK Securitisation Regulations will be restated in The Securitisation Regulations 2024 and The Securitisation (Amendment) Regulations 2024 whilst the firm facing provisions will be repealed and replaced with the FCA and PRA rules. Therefore, from 1 November 2024, firms will need to comply with the new rules and have modified their training programs and internal systems and procedures accordingly.

The FCA and PRA rules are closely, but not completely aligned, and careful analysis by legal teams is required as to the interplay on transactions.

KEY TAKE-AWAYS FROM THE TWO POLICY STATEMENTS ARE:

- **Geographical Scope**: Both sets of rules apply to sell-side parties (i.e., original lenders, originators, sponsors and securitisation special purpose entities (SSPEs)) "established in the UK", being "an entity which is constituted under UK law with a head office, or, if it has a registered office, that office is in the UK". The term "established in the UK" does not apply to non-UK sell-side parties with branches in the UK and to institutional investors (i.e., buy-side parties who are authorised persons). Effectively, the rules apply to UK securitisations (i.e., with UK sell-side or UK buy-side parties) and in an indirect way, to non-EU securitisations (i.e., with UK buy-side parties).

- **Pre-transfer Securitisations:** Subject to an exception where there is the delegation of responsibility to AIFMs (who are not authorised in the UK), both the FCA and PRA have introduced grandfathering provisions for existing securitisations with the rules at the time the relevant securitisation was issued applying.

- **Due Diligence Delegation:** Clarifying a point of debate in the market, it has been made clear that where an institutional investor instructs another institutional investor (i.e. a managing party in the rules) to fulfil any of its due diligence obligations, responsibility will transfer and the managing party not the delegating party will be responsible for any failure to comply. The only exception to this rule is where the "managing party" is not an institutional investor (e.g., AIFMs): the responsibility will not shift.

- **Due Diligence Timing**: Information (e.g., the legal documentation needed to understand the transaction, the prospectus or where relevant, the STS notification) previously to be made available "before pricing" must now, for primary market investments, be made available, in draft or initial form "before pricing or commitment to invest" and where final, within 15 days of the closing of the transaction. This is a clarificatory change, as unlike a "public" securitisation transaction, there is no clear point of pricing in a "private" securitisation transaction. Further, it has been explained that secondary market investors need only ensure they have been provided with the relevant information, in final form "before the commitment to invest" (rather than pricing, which may have occurred sometime in the past). The market is likely to take the view that the commitment to invest occurs on or around the signing of transaction documents, in the primary market, or the trade date, in the secondary market.

- **Due Diligence Requirements for Investors**: Under the rules, institutional investors are required to verify:

  (a) the sufficiency of the information a manufacturer has made available to them to enable them to independently assess the risk of holding the securitisation position;

  (b) they have received the information listed in the rules; and

  (c) there is a commitment from the manufacturers to make further information continually available.

  This is a significant change from the current rules. Under the existing rules, UK investors must confirm - even when investing in non-UK securitisations - that they have received information that is "substantially the same" as that required to be disclosed by UK securitisations. Given that UK securitisations must disclose on the basis of prescriptive templates derived from those in the EU, the current position enables UK investors to invest in EU securitisations that do not specifically seek to comply with UK disclosure standards. However, UK investors have greater difficulty investing in, for example, US securitisations where such securitisations disclose on a different basis. The new UK due diligence rules should assist UK investors invest in non-UK, non-EU securitisations. However, the requirement for UK securitisations to disclose information on the basis of prescribed templates remains.

- **Holding of Retained Interest**: It is now clear that the hedging of a retained interest is allowed where it is undertaken prior to the securitisation as a legitimate and prudent element of credit granting or risk management and does not create a differentiation (for the retainer's benefit) between the originator's securitised and non-securitised credit risk.

- **Risk Retention and Own Liabilities:** The rules clarify that there is no need for risk retention in relation to the securitisation of own liabilities.

- **Resecuritisations:** There is now no statement of policy in the rules on resecuritisations. Both the FCA and PRA have power under section 138A (Modification or Waiver of Rules) FSMA to modify or waive their rules and accordingly firms may apply for a modification or waiver of the rules restricting resecuritisations under section 138A. It is more likely that this will be exercised on an individual basis rather than on a market wide basis.

- **Exemption from Cash Collateralisation Requirement:** The proposal to extend the scope of the "cash collateral exemption" requirement from only credit institutions to all Capital Requirements Regulation and Solvency II firms was not included in the rules. This exemption set out in the 2014 regulatory technical standards, required retainers fulfilling risk requirements through a synthetic or contingent form to ensure that interest is fully collateralised in cash and held on a segregated basis as client's funds.

- **Use of FCA registered Third Party Verifier (TPV):** The FCA have clarified in their rules that when an originator, sponsor or SSPE uses a TPV to assess whether a securitisation complies with the STS criteria, they must check that such TPV is registered with the FCA.

Consultations on further changes to the rules (e.g., the "public" and "private" securitisation definitions and template reporting) are expected to occur in Q4 2024/Q1 2025 although timings may change. More importantly, detailed feedback given by firms on these topics to the FCA and the PRA, when consultations are open, is paramount in the industry's efforts to avoid regulatory divergence.

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