

DEBT CAPITAL MARKETS

Securitisation Regulation: Disclosure, Synthetic Securitisations and Non-Performing Exposures – What you need to know

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Disclosure templates, securitisation repositories, STS notifications, synthetic securitisations and non-performing exposures – these are the key focus areas at the moment under the Securitisation Regulation, following the publication of seven sets of technical standards in the Official Journal, and the launch by the European Commission of its [Capital Markets Recovery Package](#).

In this Briefing, we briefly examine the new technical standards dealing with disclosure templates and securitisation repositories.

We then look at the recent proposal from the European Commission (the **Commission**) to extend the simple, transparent and standardised (**STS**) securitisation framework to on-balance sheet synthetic securitisations, and to remove regulatory obstacles to securitisations of non-performing exposures (**NPEs**).

The Technical Standards: Disclosures; Securitisation Repositories

Seven sets of technical standards under the Securitisation Regulation came into force on 23 September 2020. These deal with:

- the application procedures for authorisation as a securitisation repository;
- operational procedures for securitisation repositories;
- disclosure requirements and reporting templates under Article 7 of the Securitisation Regulation; and
- the STS notification requirements and reporting templates.

From 23 September 2020, the new reporting templates must be used when

complying with the Article 7 disclosure requirements. The CRA3 templates that were used as a transitional disclosure method (see our previous briefing: [Securitisation Regulation Update: Addressing Challenges](#)) should no longer be used for Article 7 disclosures.

The disclosure requirements provide that any Article 7 information for public securitisations must be made available via either a securitisation repository or a website that meets certain requirements set out in the Securitisation Regulation.

From 23 September 2020, entities are also able to apply to register as securitisation repositories with ESMA. It is anticipated that the first securitisation repository could be authorised by ESMA as early as Q1 2021¹. As such, entities that have been designated as the responsible entity to fulfil the information requirements under Article 7 should monitor any authorisation applications that are expected to be successful so that they are ready to transition their reporting procedures once the first securitisation repository is authorised.

Capital Markets Recovery Package: Synthetic Securitisations and NPEs

On 24 July 2020, the Commission adopted a [Capital Markets Recovery Package](#) as part of its overall coronavirus recovery strategy. As part of that package, it made

two key proposals that are designed to facilitate the use of securitisation as a tool in Europe's economic recovery by enabling banks to improve their balance sheets and expand their lending capabilities, in particular to SMEs.

The two securitisation proposals set out in the Capital Markets Recovery Package are as follows:

• Synthetic Securitisations

To extend the STS framework to on-balance-sheet synthetic securitisations (securitisations where the originator continues to own the underlying exposures) (**STS Synthetic Transactions**) which are seen as a key risk management tool for banks. These securitisations would benefit from improved capital treatment as a result, and this proposal would also assist in moving risk off banks' balance sheets, freeing-up bank capital for further lending to businesses and households and ultimately spreading risk across market participants, and allowing a broader range of investors to fund the economic recovery.

• NPE Securitisations

Removing existing regulatory obstacles to the securitisation of NPEs to facilitate banks in moving NPEs off-balance sheet, improving their regulatory capital positions and continuing to lend.

¹ ESMA [announced](#) on 23 September 2020 that it has received its first application for authorisation as a securitisation repository.

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The proposed amendments are set out in two draft regulations, one amending the Securitisation Regulation and the other amending the Capital Requirements Regulation (CRR).

Proposed Amendments to the Securitisation Regulation: STS Synthetic Transactions

The Commission proposes to amend the Securitisation Regulation by inserting a new section into Article 26 which will:

- clarify that an “*STS on-balance-sheet securitisation*” is a synthetic securitisation² which meets the STS criteria set out in the proposed new Articles 26b to 26e
- set out the STS criteria that an on-balance-sheet securitisation must meet in order to obtain an STS designation. The STS criteria are based on the existing STS criteria, with some amendments and additions to take into account the particular nature of STS Synthetic Transactions. The main additions relate to:
 - the structuring of credit protection agreements;
 - the appointment of a third party verification agent to review the operation of the credit protection agreement on the occurrence of a credit event;
 - early termination events in relation to STS Synthetic Transactions; and
 - the operation of synthetic excess spread.

There are also various originator-specific requirements, including that the originator:

- must be authorised or licenced in the EU;
- must hold the underlying exposures on its balance sheet or on the balance sheet of an entity in the same group;
- must originate the exposures as part of its core business activity;
- cannot double-hedge the risk;
- must maintain a reference register which identifies the underlying exposures; and

- must provide additional, tailored representations and warranties in respect of the STS Synthetic Transaction.

Proposed Amendments to the Securitisation Regulation: NPE Securitisations

The Commission's proposed changes to the Securitisation Regulation would create a definition of a “**non-performing exposure (NPE) securitisation**” as follows: “...a securitisation backed by a pool of non-performing exposures that meet the conditions set out in Article 47a(3) of [the CRR] and the value of which makes up at least 90% of the pool's value at the time of origination”.

The Commission aims to facilitate NPE Securitisations by making targeted amendments to the Securitisation Regulation as follows:

• Risk Retention

- The servicer in an NPE Securitisation would be allowed to act as the risk retention holder, recognising that the servicer in an NPE Securitisation often has a more substantive interest in the workout of the assets and value recovery than the originator or original lender.
- The retention of the material net economic interest will be measured at 5% of the net (discounted) value of the securitised exposures that qualify as NPEs, rather than the nominal value, and the Commission's proposed amendments to the Securitisation Regulation set out how this should be calculated.

• Criteria for credit-granting

Where the originator is an entity that purchases a third party's exposures on its own account and then securitises them (known as a **Limb (b) Originator**), the credit-granting criteria set out in Article 9 of the Securitisation Regulation will not apply to any exposures that are NPEs (within the meaning of the proposed amendments to the Securitisation Regulation) at the time the originator purchased them from the relevant third party.

Proposed Amendments to the CRR

The Commission's proposed amendments to the CRR would:

- introduce a more risk-sensitive regulatory treatment for the senior tranches of STS Synthetic Transactions;
- introduce a specific regulatory treatment for NPE Securitisations; and
- limit, to a specific list of eligible providers of unfunded credit protection, the requirement for a qualifying credit assessment.

Comment

It is now for the European Parliament and the EU Council to negotiate and agree the final content of the proposed regulations.

Due to the economic background against which these measures are being proposed, the intention is that the regulations will be reviewed and adopted as soon as possible. This may happen as early as H1 2021. After the regulations are adopted and enter into force, the changes to the Securitisation Regulation and the CRR will apply directly in EU Member States.

The Commission has emphasised that its proposals are designed to enhance transparency, reduce the complexity of the securitisation market, lead to the use of simpler, more standardised and more transparent structures, and contribute to the stability of the financial system. It reiterated that its proposals are not intended to undercut the high levels of investor protection available under the current securitisation framework.

The need for these changes to support banks in the management of their balance sheets and lending capabilities cannot be overstated. The speed at which the legislative process moves will be key to determining whether these tools will be available in time to provide meaningful assistance to Europe's economic recovery from COVID-19.

² Defined in the Securitisation Regulation as a securitisation where the underlying exposures continue to be held by the originator, with the transfer of risk being achieved by the use of credit derivatives or guarantees.

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