New EU Securitisation Regulation – Political Agreement Reached

June 2017

Last week the EU co-legislators reached a political agreement on the new EU Securitisation Regulation, clearing a major hurdle to its implementation. Agreement was also reached on related amendments to the Capital Requirements Regulation. While considerable technical work remains outstanding, it is expected that the new regime will apply from 1 July 2018. The texts of the agreement have not yet been published and the exact detail of the political agreement is continuing to emerge, but it is understood that the key aspects of the agreement are:

Risk retention

The existing risk retention requirement will be kept at 5% for all retention methods. The European Systemic Risk Board will be mandated to report regularly on excessive buildup of market risk and if necessary make recommendations on increasing the risk retention levels, but any increase will remain at the Commission's discretion.

All securitisations – nature of investors

There will be no requirement for investors in securitisations to be EU regulated institutional investors, allowing US investors and (post-Brexit) UK investors to invest in securitisations originated in the EU. Non-EU investors investing in securitisations in which there is at least one EU-established sponsor, originator or SSPE will likely be effectively obliged to comply with the EU due diligence requirements in any event.

All securitisations – nature of securitisation parties

There will be no general requirement for securitisations to have at least one EU regulated entity among the originator, sponsor and SSPE. This means that corporate entities will still be able to establish securitisations, provided they comply with CRR credit underwriting standards.

Private transactions

Private securitisations which are exempt from the requirement to publish a Prospectus Directive-compliant prospectus will not be required to make public disclosure. However, many of the transparency requirements will apply to all securitisations including private securitisations, for example the provision of loan level data to their private investors.

Investor transparency

Contrary to earlier proposals, there will be no requirement for investors to make available to competent authorities information relating to their beneficial ownership, place of establishment, business sector and size and tranche of their investment.

Resecuritisations

Resecuritisations will be prohibited, but there will be some grandfathering for existing resecuritisations and some exemptions for certain technical resecuritisations which are established for risk management purposes, subject to approval by relevant competent authorities.

STS securitisations - third country entities

To qualify as a "simple, transparent and standardised" (STS) transaction, each of the sponsor, originator and "securitisation special purpose entity" (SSPE) will have to be established in the EU. It appears that there will be no equivalence mechanism allowing entities established in third countries with equivalent STS regulation to participate in EU STS securitisations. The impact of Brexit on this will depend on the detail of any grandfathering provisions (and, possible, the terms of any Brexit deal between the UK and the EU27), but it is likely that any STS securitisation with a UK established sponsor, originator or SSPE will cease to qualify as STS subsequent to the Brexit date, thereby no longer benefiting from favourable capital treatment for EU regulated firms.

Third party verification of the STS criteria

Third parties may be used to verify that STS securitisations meet the STS criteria. However, statutory liability for compliance with the STS criteria will remain with the originator, sponsor and SSPE. Third party verifiers will face EU regulation and supervision.

Timing and next steps

It is likely that detailed technical work by the Commission on the Securitisation Regulation and related work by the European Banking Authority and European Securities and Markets Authority on the technical and implementing standards will begin immediately. We understand that the final text of the Securitisation Regulation is likely to be published in the Official Journal by the beginning of 2018, coming into force 20 days thereafter and applying from 1 July 2018. All secondary measures will have to be in place by 1 July 2018 and consultations on these are expected to take place from Q3 2017.

Conclusion

On balance, the political agreement represents a victory for the European securitisation industry, which has succeeded in convincing the co-legislators that many of the Parliament's proposals were unworkable and/or undesirable. However, the jury is still out on whether or not the new regime will succeed in its aim of revitalising the European securitisation markets. The best possible outcome would be one in which revised capital requirements both for securitisers and investors were such that market participants were not unduly disincentivised from entering into securitisations. It is also important that policy makers continue to consult appropriately with industry participants in order to ensure that the technical detail of the Securitisation Regulation and its related secondary measures is workable and that, for example, existing securitisations can be appropriately grandfathered. There is also a risk that some securitisations could become uneconomic if the upcoming review of EMIR results in securitisation issuers being classified as financial counterparties, with no specific provisions addressing their particular characteristics. Any effective restrictions on US and UK entities participating in EU securitisations either on the buy side or the sell side may decrease liquidity and concentrate risk. The political battle on these fronts may be only just beginning.

If you would like to discuss further, please do not hesitate to contact a member of our team.

Richard Jones
T +44 (0)20 7090 4733
E richard.jones@slaughterandmay.com

Guy O'Keefe
T +44 (0)20 7090 3299
E guy.o'keefe@slaughterandmay.com

Oliver Wicker
T +44 (0)20 7090 3995
E oliver.wicker@slaughterandmay.com

Oliver Storey
T +44 (0)20 7090 3987
E oliver.storey@slaughterandmay.com

Eric Phillips
T +44 (0)20 7090 3055
E eric.phillips@slaughterandmay.com

© Slaughter and May 2017
This material is for general information only and is not intended to provide legal advice. For further information, please speak to your usual Slaughter and May contact.