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CAPITAL MARKETS - DEBT

European Commission report on the functionality of the Securitisation Regulation

On 10 October 2022, the European Commission (the **Commission**) published its long-awaited report on the functioning of the Securitisation Regulation (the **Report**).

In this publication, we consider key conclusions of the European Commission including:

- due diligence and transparency obligations
- the treatment of private securitisations
- the jurisdictional scope of the Securitisation Regulation
- sustainable securitisations
- supervisory convergence

5 MIN READ

Background

The Report, which is mandated by Article 46 of the **Regulation (EU) 2017/2402** (the **Securitisation Regulation**), provides an update on the development of the EU securitisation market since the introduction of the Securitisation Regulation and assesses a broad range of non-prudential issues effecting the growth of the market. In assessing the functioning of the legal framework created by the Securitisation Regulation, the Commission draws on the public consultation of market participants launched by it in July 2021, the **recommendations** of the high-level forum on the Capital Markets Union and the **opinion** (the **Joint Committee Opinion**) of the joint committee of the EU Supervisory Authorities (the **Joint Committee**).

The Report also fulfils the Commission's obligations under Article 45a(3) of the Securitisation Regulation to report on the creation of a specific sustainable securitisation framework and confirms the Commission's agreement, to a large extent, with the position of the European Banking Authority (**EBA**) as set out in its March 2022 report on developing a framework for sustainable securitisation (the **EBA Report**).

Whilst the Report concludes that there is room to fine-tune certain aspects of the Securitisation Regulation and confirms the willingness of the Commission to consider some changes, it stops short of making any legislative proposals. A detailed report on prudential matters, as mandated under Article 519(a) of the Capital Requirements Regulation, is expected later this year and, dependent on the outcome of this report, the Commission will reassess whether or not there is a case for other changes to be made.

Summary of the Report

Risk retention – no change

No changes are proposed to the risk retention requirements but the Commission invites the EBA to continue to monitor the application of the requirements, the retention methods adopted by market participants and the effectiveness of each retention method.

Due diligence and transparency – ESMA to review disclosure templates

In response to the feedback provided by market participants regarding the proportionality of the disclosure and due diligence requirements and the usefulness of the disclosure templates published by the ESMA, the Commission has invited EMSA to review the templates to address possible technical difficulties in completing certain fields, remove possibly unnecessary fields and align them more closely with investors' needs. The Commission has also recommended that ESMA consider whether information on a loan-by-loan basis is useful and proportionate to investors' needs for all types of securitisations.

Private securitisations – ESMA to prepare dedicated disclosure templates for private securitisations

Whilst concurring with the views of respondents regarding the usefulness of standardised templates, the Commission acknowledges that, given the bespoke nature of private securitisations, the information needs of investors in and supervisors of private securitisations differ from those of public securitisations. The Commission has therefore invited ESMA to draw up a dedicated disclosure template for private securitisations that is tailored specifically to supervisors' need to gain an overview of the market and the main features of private securitisations. The Commission encourages supervisory authorities to enforce issuers' obligations under Article 7 to make information for private securitisations available to supervisory authorities for use in their work. The Commission suggests that, in the longer term, it may consider amending the Securitisation Regulation to require information in respect of private securitisations to be reported to a securitisation repository.

Despite calls for the definition of a private securitisation to be amended, the Commission does not deem this appropriate or necessary. In its view, stakeholders requested a change to the definition only to ease transparency requirements for private securitisations. The Commission believes stakeholder concerns will be adequately addressed by the simplification of the disclosure templates for private securitisations, as discussed above.

STS equivalence – not at this time

The Commission considers it premature to introduce an STS equivalence scheme. In its view, no third-party jurisdiction's securitisation regime (other than that of the UK) could be considered equivalent to the EU's STS securitisation framework. It will continue to monitor regulatory developments in third-party jurisdictions and may re-consider the need for an STS equivalence regime in the future.

Sustainable securitisations – no need for a dedicated label

The Commission supports the view of the EBA that there is no need, at this stage, to create a dedicated sustainability label for securitisations and invites the European Parliament and the Counsel to take the EBA Report into account in their ongoing negotiations of the EU Green Bond Standard. As regards the disclosure of sustainability-related information and in light of the fact that securitised products fall outside of the scope of the Sustainable Finance Disclosure Regulation, the Commission suggests that the upcoming sustainability regulatory technical standards be widely drafted to capture potential adverse impact disclosures.

Third-party verification of STS criteria – no change

No changes to the third-party verification regime are proposed by the Commission. The regime is seen to function as intended though appropriately frequent dialogue between national competent authorities and the third party verification firms is encouraged to avoid divergence between supervisors and verifiers in their interpretation of the STS criteria.

SSPEs – no need for "limited-licensed banks"

In line with the views of the majority of market participants, the Commission has dropped its proposal for a system of limited-licensed banks to perform the functions of SSPEs.

Jurisdictional scope – no change required

The Report considers the difficulties relating to the jurisdictional scope of the Securitisation Regulation as identified in the Joint Committee Opinion and provides some helpful clarification.

Sell-side obligations – no change required

The Commission rejected the interpretations of the Joint Committee in respect of Articles 6, 7 and 9 of the Securitisation Regulation on the basis that aims of these provisions, namely to ensure that all securitisations with participating EU participants comply with certain structural and quality requirements, are sufficiently met through investor's due diligence obligations under Article 5. The Commission further clarified that:

- a non-EU entity may act as a retainer for the purposes of Article 6 (the Joint Committee suggested that Article 6 be interpreted in a way so that only an EU-based entity should be able to retain risk)
- while a non-EU based originator, sponsor or SSPE (each a **sell-side entity**) may be designated to fulfil disclosure requirements for the purposes of Article 7, the obligations remain joint obligations of the originator, sponsor or SSPE and may be enforced against the EU-based sell-side entity (the Joint Committee suggested that Article 7 be interpreted in a way so that an EU-based entity be chosen as the designated reporting entity)
- EU investors must be satisfied that, for the purposes of Article 9, the credit-granting criteria are "met by the credit-granting entity in the process" regardless of where that entity is located (the Joint Committee suggested that Article 9 be interpreted in a way so that only EU-based entities are responsible).

The Commission did acknowledge the inconsistency between Article 5(1)(b) and Article 9. Currently, Article 9 obliges the sponsor to also ensure sound credit-granting while the corresponding due diligence obligations under Article 5(1)(b) does not refer to the sponsor. The Report confirms that, while not harmful, the inconsistency will be resolved in the next revision of the Securitisation Regulation.

Buy-side obligations – extra-EU effect

While it acknowledged the questions of legal interpretation presented by Article 5(1)(e), the Commission is of the view that the legislative intent of the verification obligation imposed on institutional investors under the article is clear and should apply equally to investments in non-EU securitisations. The Commission hopes that the proposed simplification of the disclosure templates will make it easier for non-EU securitisations to comply with the transparency requirements and reduce the competitive disadvantage for EU institutional investors. The Commission clarified that non-EU AIFMs and sub-threshold AIFMs marketing and managing funds in the EU must also comply with the due diligence requirements under Article 5.

Supervision of securitisations

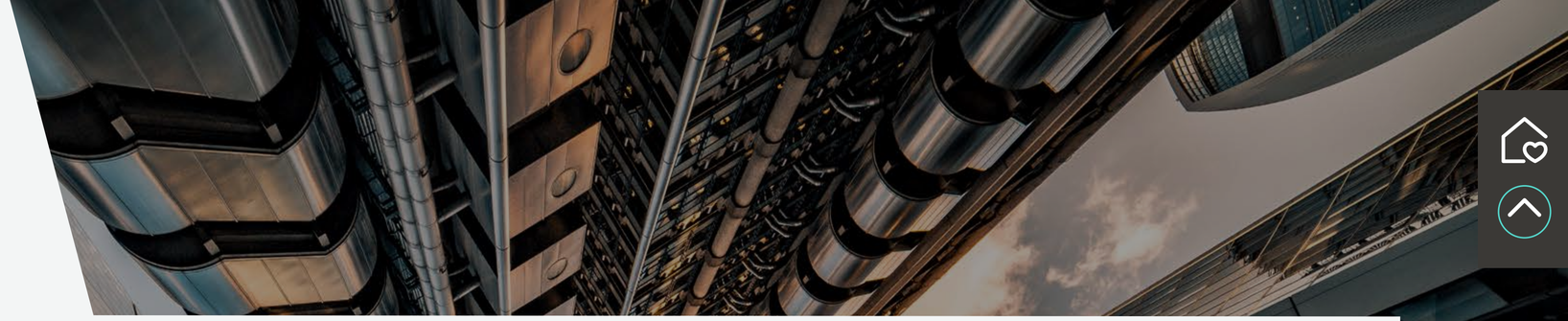
The Commission agrees with the recommendation of the Joint Committee to develop a common EU guide on best practise for national supervisors to avoid the harmful impact diverging practices could have on the development of the market.

Conclusion and recommendations

While the Report confirms the Commission's continued commitment to the aim of creating the framework for a thriving and stable EU securitisation market, it also acknowledges the impact certain issues with the framework are having on the growth of the EU securitisation market. Despite this acknowledgement, the Commission does not propose any legislative changes at this time.

It remains to be seen whether the recommendations of the Commission addressed to ESMA, the Joint Committee and the European Supervisory Authorities will be actioned. A number of the clarifications and recommendations provided are helpful to market participants (e.g. no need for limited-licence banks). Some should be helpful depending on how they are actioned (e.g. ESMA's review of the disclosure templates and preparation of a dedicated disclosure template for private securitisations) and others, while not as facilitative as some stakeholders may have hoped, at least give market participants greater certainty (e.g. in respect of the jurisdictional scope of the Securitisation Regulation). The Commission will continue to monitor the securitisation market and has not ruled out the possibility of amendments to the Securitisation Regulation in the future.

A&L Goodbody



Key contacts

Peter Walker
Partner
+353 1 649 2202
pwalker@algoodbody.com

Jack Sheehy
Partner
+353 1 649 2140
jsheehy@algoodbody.com

Sinéad O'Connor
Partner
+353 1 649 2752
soconnor@algoodbody.com

Ciarán Rogers
Partner
+353 1 649 2204
crogers@algoodbody.com

Michelle Daly
Partner
+353 1 649 2297
mcdaly@algoodbody.com

Sarah Murray
Senior Associate
+353 1 649 2085
samurray@algoodbody.com

Elizabeth White
Knowledge Lawyer
+353 1 649 2787
ewhite@algoodbody.com

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