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United Kingdom

SECURITISATION

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This country-specific Q&A provides an overview of securitisation laws and regulations applicable in United Kingdom.

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UNITED KINGDOM
SECURITISATION

1. How active is the securitisation market in your jurisdiction? What types of securitisations are typical?

The securitisation market in England and Wales is very well established and is one of the largest securitisation markets on this side of the Atlantic. According to the Association for Financial Markets in Europe ("**AFME**"), as at the end of Q3 2020, securitisation of UK-originated assets amounted to (i) EUR 8.1 billion out of a European total of EUR 18.1 billion of placed issuance and (ii) EUR 249.6 billion of outstanding issuances out of a European total of EUR 985.6 billion with UK residential mortgage-backed securities (RMBS), pan European CLOs and French RMBS leading issuance totals.

The UK securitisation market covers a wide range of assets in addition to those mentioned above, such as trade receivables, commercial mortgage-backed securitisations (CMBS), whole business securitisations, credit card receivables etc. and both traditional (i.e. 'true sale') and synthetic (using credit derivatives) securitisation structures are utilized in the market.

It is also worth noting that publicly available data does not account for any privately placed securitisation transactions and the UK market is also very active in this respect. Furthermore, securitisation transactions without UK-originated assets can still have a UK element, for example by submitting the transaction documents to English law in pan-European transactions such as CLOs or incorporating a transaction's special purpose or receivables seller/originator entity in the UK.

2. What assets can be securitised (and are there assets which are prohibited from being securitised)?

Regulation (EU) 2017/2402 of the European Parliament and of the Council (the "**EU Securitisation Regulation**") regulates securitisation in the European Union member states. The EU Securitisation was implemented into domestic law within the United Kingdom in 2018 and in 2019. Following the UK's departure from the European Union and notably the end of the transition period on 31 December 2020, the EU Securitisation Regulation has formed part of domestic law within the United Kingdom, including certain amendments to ensure its operation on a domestic level, through several pieces of legislation. The relevant legislation includes the Securitisation Regulations 2018, the European Union (Withdrawal) Act 2018, the European Union (Withdrawal Agreement) Act 2020 and the Securitisation (Amendment) (EU Exit) Regulations 2019.

Pursuant to the EU Securitisation Regulation as implemented into domestic law within the United Kingdom, assets that are themselves "securitisation positions" (as defined in the EU Securitisation Regulation) cannot be securitised.

Assets that arise from commercial contracts or loan agreements or other contractual documents that contain clauses that seek to restrict the assignor of the receivable, loan or other asset from assigning its rights under such agreement or contract are also restricted in many cases from being securitised from an English law perspective.

Leaving these two points aside and provided that for a particular asset it has the commercial characteristics allowing it to constitute an underlying exposure for a securitisation, there is no legal restriction under English law restricting the ability of particular assets to be securitised.

3. What legislation governs securitisation in your jurisdiction? What transactions fall within the scope of this legislation?

The main legislation directly regulating securitisation is the EU Securitisation Regulation implemented into the domestic laws of the United Kingdom and amended in certain respects to ensure its operation on a domestic level. The key legislation is therefore the Securitisation Regulations 2018, the European Union (Withdrawal) Act

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2018, the European Union (Withdrawal Agreement) Act 2020 and the Securitisation (Amendment) (EU Exit) Regulations 2019.

Any transaction that falls within the definition of "securitisation" under the EU Securitisation Regulation (as implemented into the domestic laws of the United Kingdom) will be subject to the above legislation. The definition of "securitisation" for these purposes does not relate only to any traditional structure or concept of securitisation but is governed by the following definition that focuses on there being a tranching of credit risk associated with an underlying exposure or a pool of exposures:

"'securitisation' means a transaction or scheme, whereby the credit risk associated with an exposure or a pool of exposures is tranched, having all of the following characteristics:

(a) payments in the transaction or scheme are dependent upon the performance of the exposure or of the pool of exposures;

(b) the subordination of tranches determines the distribution of losses during the ongoing life of the transaction or scheme;

(c) the transaction or scheme does not create exposures which possess all of the characteristics listed in Article 147(8) of Regulation (EU) No 575/2013."

The transaction also needs to fall within the jurisdictional scope of the UK legislation.

Outside of the EU Securitisation Regulation as implemented into the domestic laws of the United Kingdom, there are other elements of English law that do apply to securitisation transactions.

These include but are not limited to:

- English law on assignment under the Law of Property Act 1925 including equitable assignment and legal assignment including relevant decisions of English courts concerning the same;
- Decisions of the English court (in some cases pre-dating the Law of Property Act) concerning the characteristics of irrevocable transfers of assets, commercially referred to as "true sale" in securitisation transactions;
- English law relating to particular assets to be securitised including any consumer credit regulation or other financial regulatory rules applicable to the securitisation of particular assets or regulation of notification of debtors to underlying exposures including methods of payment such as negotiable instruments; and
- English law on security and registration of the same which may impact securitisations including exposures that benefit from registered security.

4. Give a brief overview of the typical legal structures used in your jurisdiction for securitisations and key parties involved.

A typical securitisation structure usually involves the transfer of a portfolio of assets (e.g. receivables) generated and/or owned by an originator to a special purpose vehicle ("**SPV**") incorporated in England or in another tax favourable jurisdiction such as Ireland, Luxembourg or the Netherlands. In order to fund the purchase price of the assets, the SPV issues securities, in the form of notes or other debt securities, to investors. The securities may be privately or publicly issued, depending on the individual circumstances of a transaction.

Under English law, the transfer of the underlying assets in a standard securitisation can be made by equitable assignment, legal assignment, novation or declaration of trust. Synthetic securitisations on the other hand utilise guarantees and credit derivatives.

The most common method of transfer in English law securitisations is through an equitable assignment of the beneficial title in the underlying asset from the originator to the SPV. This method is advantageous to the parties since the debtor of the underlying asset does not need to be notified of the transfer to the SPV (and will only be notified upon the occurrence of certain trigger events set out in the transaction documents such as default or insolvency of the originator) and any security associated with such underlying asset can also be transferred without any further formalities. The transfer of the underlying assets is structured by the parties as a 'true sale' so that the assets cease to belong to the originator or form part of the originator's estate upon its insolvency.

Transfer of the underlying assets through novation or a legal assignment is undesirable and impractical because an originator does not usually plan on disclosing to its customers that it is selling its assets in a securitisation transaction (unless there are any contractual restrictions in the underlying asset documents which require the consent or disclosure of any transfer to be made to the debtor).

The SPV's obligations to the investors under the debt securities it issues are limited to and secured by a

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security interest created by the SPV (usually granted in favour of a third party entity appointed as a security trustee) over the assets purchased by the SPV from the originator.

On each payment date set out in the transaction documents, following receipt by the SPV of amounts paid in respect of the underlying assets, those amounts are applied to repay the investors in its securities and to discharge its other payment obligations in the transaction.

In a standard securitisation, some of the key parties and their roles in the transaction are:

- The SPV/issuer. As briefly mentioned above, the SPV is the legal form of the issuer and is usually a bankruptcy remote orphan company incorporated for the purposes of the securitisation who will purchase the assets from the originator and issue the debt securities to investors to fund the purchase of a specified pool of assets from the originator. Following the UK's departure from the European Union and notably the end of the transition period on 31 December 2020, pure UK securitisations continue to use a UK based SPV whereas securitisations containing both a UK and a non UK element (for instance European CLOs, or pan-European trade receivables securitisations) utilise SPVs located mostly in Ireland or Luxembourg.
- The originator. This the user (the end user) of the funds raised in the securitisation. In the course of its business, it deals with customers, supplies goods or services etc. and that gives right to a receivable which is the claim of the originator against the customer for the previously supplied goods or services (and this is the asset ultimately sold to the securitisation SPV).
- The servicer and back-up servicer. It is customary for the originator to also act as servicer in the transaction documents so that it can continue to maintain its relationship with its customers by administering the receivables on the SPV's behalf. The originator is appointed by the SPV to assume its servicing capacity and will receive a servicing fee for this role. To address the circumstances where the servicer fails to meet its obligations in such capacity, a back-up servicer may be appointed at the outset or at some point during the life of the transaction to assume the servicing role in the event of default by the servicer. Such back-up servicer entity will have the necessary experience and capabilities to assume all the tasks carried out by the servicer.
- The arranger. Since asset backed securities are capital market instruments and securitisation structures can become very complex, an investment bank usually acts as arranger in a securitisation and is responsible for, inter alia, structuring the transaction, analyzing the risk profile of the assets and managing the set up and closing of the transaction.
- The investors. These are typically financial institutions, insurance companies, pension funds, hedge funds, companies etc.
- Other parties which may be involved in a securitisation are: (i) a security trustee who will hold the security granted by the issuer on behalf of the investors; (ii) a paying agent to administer payments of interest and principal on the securities; (iii) a listing agent if the debt securities are publicly listed; (iv) a hedge counterparty (i.e. a financial institution with derivative capabilities) if derivative contracts are used in the securitisation to address currency or interest rate mismatches between the assets and the securities, (v) an investment/collateral manager and a collateral administrator if the pool of assets is dynamic and actively managed throughout the life of the transaction; (vi) rating agencies to rate the securities issued by the SPV; (vii) credit insurers to cover securitised portfolio credit risk, especially in the context of de-consolidated transactions; and (viii) statutory accountants to validate GAAP or IFRS de-consolidation in the context of de-consolidated transactions.

5. Which body is responsible for regulating securitisation in your jurisdiction?

The Prudential Regulatory Authority ("**PRA**") is responsible for regulating compliance by credit institutions, investment firms and insurance undertakings with their obligations under the EU Securitisation Regulation (as implemented into domestic law of the United Kingdom) either in their capacities as regulated institutional investors or as originators, sponsors, SSPEs or original lenders.

The Financial Conduct Authority ("**FCA**") is responsible for regulating compliance by alternative investment fund managers, undertakings for the collective investment in transferable securities and otherwise unregulated

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entities that participate in a securitisation (for example, general corporates) either in their capacities as regulated institutional investors or as originators, sponsors, SSPEs or original lenders.

In relation to the EU Securitisation Regulation, as implemented into domestic law of the United Kingdom, the FCA and the PRA are responsible for receiving certain information that is required to be made available as part of the transparency requirements of the legislation.

Although we do have clarity that the FCA and the PRA will regulate securitisation in the UK following Brexit, it remains to be seen how the FCA and the PRA will exercise their powers under the legislation and whether in time different interpretations of existing requirements or even if amendments to legislation will eventually be bought forward to amend the operation of the legislation in the UK.

6. Are there regulatory or other limitations on the nature of entities that may participate in a securitisation (either on the sell side or the buy side)?

In relation to the EU Securitisation Regulation, as implemented into domestic law of the United Kingdom, an entity that "has been established or operates for the sole purpose of securitising exposures" is prohibited from qualifying as being an originator.

In addition, there are criteria under the EU Securitisation Regulation, as implemented into domestic law of the United Kingdom, that must be satisfied by a particular entity in order for such entity to qualify as an "originator", a "sponsor" or an "SSPE".

Finally, under certain regulatory restrictions (for example relating to consumer credit or relating to data protection), a transaction specific special purpose vehicle may not be eligible to be a purchaser of certain regulated exposures from sellers without obtaining certain regulatory authorisations, making certain registrations or implementing certain structural features to fall within regulatory exemptions.

Aside from this we are not aware of any restrictions under English law on the nature of entities that may participate in a securitisation.

7. Does your jurisdiction have a concept of "simple, transparent and comparable" securitisations, following the BCBS recommendations?

In relation to the EU Securitisation Regulation, as implemented into domestic law of the United Kingdom, there is the concept of simple, transparent and standardised ("**STS**") securitisations. In most respects, the STS label applies in UK domestic law as it did as part of EU Securitisation Regulation. Following 31 December 2020 and the end of the Brexit implementation period, the STS label in the UK is a label that is available only for domestic UK transactions and only benefits investors located in the UK (including subsidiaries of EU prudentially regulated groups) from a capital treatment perspective.

We understand that pursuant to Article 18 of the EU Securitisation Regulation, securitisations with an originator, a sponsor or an SSPE that is not located within the Union cannot qualify for the EU STS label.

8. Does your jurisdiction distinguish between private and public securitisations?

Yes. There is a distinction in the EU Securitisation Regulation (as implemented into the domestic laws of the United Kingdom) between securitisations that do require a prospectus to be drawn up (pursuant to Directive 2003/71/EC or Regulation (EU) 2017/1129) and securitisations that do not require a prospectus to be drawn up (pursuant to Directive 2003/71/EC or Regulation (EU) 2017/1129).

The EU Securitisation Regulation (as implemented into the domestic laws of the United Kingdom) stipulates different requirements for securitisations that do require a prospectus to be drawn up including as to the transparency requirements for these kind of transactions.

9. Are there registration, authorisation or other filing requirements in relation to securitisations in your jurisdiction (either in relation to participants or transactions themselves)?

Yes. Pursuant to the EU Securitisation Regulation, as implemented into domestic law of the United Kingdom, it is required to send to the FCA or PRA (as indicated in the FCA and PRA direction as published on 20 December 2018 and other publications) a notification of the creation of a securitisation. There are templates for these notifications that are publicly available.

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It is also required to provide the FCA or PRA (as indicated in the FCA and PRA direction as published on 20 December 2018 and other publications) with on-going reporting in relation to the requirements of Article 7(1)(f) of the EU Securitisation Regulation (inside information reporting) and Article 7(1)(g) of the EU Securitisation Regulation (significant events reporting).

Any security created by an English company including any English special purpose vehicle as part of the securitisation needs to be registered at Companies House.

Regulatory authorisations or permissions can be required for entities using securitisation as part of a regulated activity particularly in relation to the origination and servicing of regulated loans or receivables arising from regulated contracts.

10. What are the disclosure requirements for public securitisations?

All of the disclosure requirements under Article 7 (Transparency requirements for originators, sponsors and SSPEs) of the EU Securitisation Regulation (as implemented into the domestic law of the UK) apply to public securitisation.

Certain disclosure elements apply only to securitisations for which a prospectus is required to be drawn up (pursuant to Directive 2003/71/EC or Regulation (EU) 2017/1129). In particular, the disclosure information to be made available to holders of securitisation positions and competent authorities must be made available by means of a securitisation repository or, if no securitisation repository is appointed by means of a website that means the requirements of the EU Securitisation Regulation, as implemented into the domestic law of the UK.

Securitisation repositories are regulated entities responsible for receiving, storing and making available disclosure information to transaction participants. The UK Government and the FCA has implemented rules relating the licensing of securitisation repositories and the oversight of the same.

The other disclosure elements are not securitisation specific.

11. Does your jurisdiction require securitising entities to retain risk? How is this done?

Yes. The risk retention requirement for a securitisation falling within the scope of the UK legislation (being the EU Securitisation Regulation as implemented into the domestic law of the UK) is for the originator, sponsor or original lender in a securitisation to retain a material net economic interest in the securitisation, being a five per cent. (5%) retention of risk.

The risk must be retained by an entity that falls within the requirements of the legislation for this purpose and the securitisation must be structured in a way that results in the five per cent. (5%) retention of risk being held in one of the specific ways permitted under the legislation. The permitted methods of retaining the 5% material net economic interest are:

- the retention of not less than 5% of the nominal value of each of the tranches sold or transferred to investors;
- in the case of revolving securitisations or securitisations of revolving exposures, the retention of the originator’s interest of not less than 5% of the nominal value of each of the securitised exposures;
- the retention of randomly selected exposures, equivalent to not less than 5% of the nominal value of the securitised exposures, where such non-securitised exposures would otherwise have been securitised in the securitisation, provided that the number of potentially securitised exposures is not less than 100 at origination;
- the retention of the first loss tranche and, where such retention does not amount to 5% of the nominal value of the securitised exposures, if necessary, other tranches having the same or a more severe risk profile than those transferred or sold to investors and not maturing any earlier than those transferred or sold to investors, so that the retention equals in total not less than 5% of the nominal value of the securitised exposures; or
- the retention of a first loss exposure of not less than 5% of every securitised exposure in the securitisation.

12. Do investors have regulatory obligations to conduct due diligence before investing?

Yes with respect to institutional investors (as defined in the EU Securitisation Regulation as implemented into the domestic law of the UK). Institutional investors are required, prior to holding a securitisation position, to verify the compliance of the securitisation with certain

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regulatory requirements under the EU Securitisation Regulation as implemented into the domestic law of the UK including:

- compliance by the originator or original lender with credit granting criteria requirements;
- compliance by the originator, sponsor or original lender with the risk retention requirement; and
- compliance by the originator, sponsor or SSPE with the pre-pricing transparency requirements.

In addition, institutional investors are required, prior to holding a securitisation position to carry out a due diligence assessment of all the risks involved in the securitisation including:

- the risk characteristics of the individual securitisation position and of the underlying exposures; and
- the structural features of the securitisation that can materially impact the performance of the securitisation position.

There are additional requirements for institutional investors to implement certain monitoring practices and procedures for the life of the securitisation transaction.

13. What penalties are securitisation participants subject to for breaching regulatory obligations?

There are direct regulatory obligations on originators, sponsors and original lenders and SSPEs under the EU Securitisation Regulation (as implemented into the domestic law of the UK) and on holders of securitisation positions.

Failure to comply with the requirements under the UK legislation may lead to regulatory consequences for individuals or firms from the FCA or the PRA that fall within the jurisdictional scope of the FCA or the PRA. These penalties may include financial penalties on individuals or firms, temporary prohibitions on individuals from exercising management functions of an entity that is an originator, sponsor, SSPE or a holder of a securitisation position and public censure (in a published statement) from the FCA or the PRA. These are in addition to any other penalties that the FCA or PRA may be able to impose on its regulated firms or authorised persons.

14. Are there regulatory or practical restrictions on the nature of securitisation SPVs?

English law does not set out specific legislation regarding the establishment of SPVs for securitisation transactions but there is a special corporation tax regime for 'securitisation companies' in the UK (see Question 21). An SPV incorporated in England and Wales typically takes the form of a private or public limited company (subject to the Companies Act 2006) or a limited liability partnership (under the Limited Liability Partnership Act 2000) and will be subject to English laws that are applicable to such types of entities such as the Insolvency Act 1986.

An SPV in a traditional securitisation is (i) usually established as a bankruptcy remote orphan company with a separate legal personality, (ii) incorporated in a tax favourable jurisdiction, (iii) owned by a charitable trust and administered by a third party service provider (to ensure it is treated as being outside of the originator's group if this is the intended structure) and (iv) limited in activity to those contemplated in the securitisation transaction.

15. How are securitisation SPVs made bankruptcy remote?

As briefly mentioned in Question 14 above, an SPV is often a newly created orphan entity with its own legal status and structured to achieve bankruptcy remoteness. A number of elements must be considered when structuring the SPV as insolvency remote (some of them have been communicated on a non-exhaustive basis by rating agencies):

- ensuring the SPV is operated on a solvent basis by making sure that it does not conduct any business except with parties that have agreed to limited recourse and non-petition covenants;
- ensuring the SPV is incorporated with its own legal personality and operated separately from the originator or any other transaction party;
- appointing one or more directors who are independent of the originator (and none of the directors must be nominated by the originator);
- placing restrictions on the SPV (in its constitutional documents and in the transaction documents themselves) that prevent it from incurring any liabilities outside those contemplated by the securitisation by limiting its activities to those anticipated in

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the transaction;
- disallow the SPV to have its own employees apart from its independent directors of course;
- including 'non-petition' clauses in agreements between the SPV and the other transaction parties from commencing insolvency procedures against the SPV;
- including limited recourse language in all transaction documents to which the SPV is a party to restrict the recourse of a counterparty who takes enforcement action in respect of the SPV's assets to the secured assets of the SPV; and
- limiting the SPV's ability to voluntarily file for insolvency proceedings.

Any rating agencies providing a rating in a securitisation transaction will scrutinise and conduct its due diligence on the above factors in order to become comfortable that the SPV satisfies its bankruptcy remoteness criteria. Private or non-rated securitisation transactions still require, in most cases, that the above factors/criteria are complied with for the sake of the securitisations investors involved (including balance sheet investors, asset backed commercial paper conduits and their own institutional investors).

However, even if all of the above measures are present in a securitisation, it is not possible to have absolute certainty that a UK SPV (or any other EU SPV set up as a corporate) will be insolvency remote since any third party creditors will not be bound by the contractual restrictions in the transaction documentation (for example, the UK tax authority, HM Revenue & Customs). It is worth noting however that some EU securitisation vehicles, such as the *fonds communs de titrisations* in France are completely insolvency remote by statute (i.e. they simply cannot become subject to insolvency proceedings).

16. What are the key forms of credit support in your jurisdiction?

Credit support (or credit enhancement) is the use of various finance techniques in a securitisation to improve the creditworthiness of a security (i.e. the notes issued by an SPV) by reducing the probability of default by the issuer/SPV or (depending on the structure) simply mitigate the credit risk of the securitised portfolio of assets. Credit support features protect the repayments to be made by the issuer under the notes in the event that any losses arise from the underlying securitised assets.

The typical forms of credit support utilised in a securitisation and commonly used in English law transactions are:

- Over-collateralisation. This is when the originator transfers underlying assets to the SPV which are greater in value than the consideration paid by the SPV to the originator for such assets. The excess in value provides protection in the event that the underlying debtors of the assets default on their payment obligations.
- Creation of subordinated tranches. This can take the form of junior notes and/or a subordinated loan and provides credit enhancement to the more senior tranches by absorbing the first losses on the underlying collateral. The senior tranche holders will be repaid by the issuer in priority over the junior tranche holders and the latter's enforcement rights against the issuer will not be exercisable until the senior tranche holders are repaid. The holder of the junior tranche is normally the originator (or another entity in its group) in order, inter alia, to satisfy risk retention requirements.
- Creation of "retained spread". Cash reserves are often utilised to provide credit enhancement in securitisations and one way of funding such cash reserve is through retained (or excess) spread. Retained spread is created when the amounts received by the issuer in respect of the underlying assets is greater than the amount of the issuer's liabilities under the securities issued by it. The difference is then used to fund the cash reserve and can be used to cover costs and expenses of the transaction.
- Purchase Price mechanisms. In UK securitisations, the purchase price of receivables will generally equal the face amount of the receivables minus a small discount to cover expected losses on the purchased receivables and other costs of the SPV. In addition, a "Deferred Purchase Price" or "DPP" mechanism can be implemented whereby a portion of the purchase price due from the SPV to the originator is not paid upon the transfer of the receivable but at a later date and is paid out of collections received on the receivables. Similar to the discount feature, the DPP is a credit enhancement tool used to cover potential losses on the purchased assets.
- Letters of credit, credit insurance or guaranteed liquidity facilities. These types of

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credit enhancement provide additional risk mitigation and liquidity support to the SPV should it not have sufficient funds to pay the entirety of amounts due by it in the transaction and are usually granted by a creditworthy source such as a third party bank or a credit insurer.

It is worth mentioning that credit risk is just one risk among others in a securitisation transaction; other risks that a securitisation structure needs to address are, notably, dilution risk, FX risk, interest rate mismatch risk (notably floating vs fixed) etc.

17. How may the transfer of assets be effected, in particular to achieve a ‘true sale’? Must the obligors be notified?

In English law, the most common methods of transfer of receivables are assignment, the declaration of a trust over the receivables or novation.

Assignment

Assignment is the most common method of transfer of receivables under English law. An assignment can take effect at law or in equity. To take effect at law, an assignment must comply with the requirements of section 136 of the Law of Property Act 1925 which provides that an assignment must be: (i) in writing and signed by the assignor, (ii) of the whole of the debt, (iii) absolute and unconditional and not by way of charge and (iv) notified in writing to the person from whom the assignor would have been entitled to claim the debt.

Where an assignment does not meet all of the requirements of section 136 of the LPA, it will take effect in equity only. If an assignment takes effect in equity only, a subsequent purchaser may take priority over the claims of the initial purchaser and may require the obligor to make payment to such subsequent purchaser if it notifies the obligor before the initial purchaser does so.

Parties may choose to rely on equitable assignment if they decide not to notify the debtors of the assignment. This approach is often adopted when, due to the number of obligors, it would not be practicable to notify them or where the commercial interests of the originator prevent it for example. In such cases, the documentation will often provide that the debtors may only be notified upon the occurrence of certain trigger events. The effects of not serving notice on an obligor are that (i) the obligor may continue to validly discharge its debt by making payments to the seller, (ii) the purchaser will not be able to bring an action in its own name against the obligor, (iii) the obligor may set off claims against the seller arising prior to receipt by the obligor of the notice of assignment and (iv) the seller may amend the receivables contract without the purchaser’s consent (unless contractually restricted of course).

Declaration of Trust

An originator can continue to hold the receivables but declare a trust over them for the benefit of the purchaser. This allows the purchaser to obtain the beneficial interest of the receivables with the originator continuing to act as settler and trustee of the trust assets.

Novation

Novation allows both the seller’s rights and obligations under the receivable contract to be transferred. As a result, it requires the consent of the obligor, the seller and the purchaser.

18. In what circumstances might the transfer of assets be challenged by a court in your jurisdiction?

A transfer of receivables can be contested by a liquidator, administrator or creditor of the seller in an insolvency of the seller on the basis that, instead of transferring to or holding to the order of the purchaser the entire legal interest (or the right to require the transfer thereof) and the entire beneficial interest of the seller in the receivables in question, charges were created over those receivables pursuant to the terms of the transfer agreement and in such case such charges will be void against such liquidator, administrator or creditor for lack of registration unless registered pursuant to Part 25 of the Companies Act 2006.

To determine whether a transaction characterised as a sale by the parties is a “sham” and should be recharacterised as a secured financing, the English courts will look at the substance of the transaction irrespective of the labels that the parties have given to the transaction. Case law has established the following key questions to be considered to establish whether the transaction is a true sale rather than a secured financing:

(i) Do the transaction documents accurately reflect the intention of the parties and are the terms consistent with a sale as opposed to a secured financing?

(ii) Does the seller have the right to repurchase the receivables sold?

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(iii) Does the purchaser have to account for any profit made on a disposition by it of the receivables?

(iv) Is the seller required to compensate the purchaser if it ultimately realises the acquired receivables for an amount less than the amount paid?

The courts have made it clear however that none of these factors are determinative so the presence of one or more of the characteristics of a secured financing will not automatically result in the transaction being re-characterised as a secured financing. The English courts will instead consider the transaction as a whole and take into account factors such as whether by their subsequent conduct the parties have departed from the terms of their agreement which would otherwise be held to effect a true sale, and whether or not the legal effect of their agreement accurately represents the true nature of the transaction intended by the parties.

19. Are there data protection or confidentiality measures protecting obligors in a securitisation?

Yes in relation to obligors that are individuals and/or in relation to which personal data is transmitted as part of the securitisation. For obligors such as this, the provisions of the General Data Protection Regulation ("**GDPR**") apply and the securitisation will need to comply with the provisions of the GDPR including in certain cases filing registrations with the Information Commissioner's Office.

Confidentiality provisions contained in underlying contracts or loan agreements benefiting obligors may be considered to be a restriction in certain circumstances to the assignment of the exposures arising under such contract or agreement in a securitisation particularly if the assignment of the underlying exposure may breach the confidentiality provision or give rise to a claim against the assignee. However, in many cases it is considered that either the assignment of the exposure does not breach the confidentiality provision or alternatively that any potential breach of the relevant provision may not give rise to a claim against the assignee.

20. Is the conduct of credit rating agencies regulated?

Since the end of the Brexit transition period, Regulation (EC) No 1060/2009 (European Rating Agency Regulation) as it forms part of retained EU law ("**CRA**") regulates the conduct of UK-registered credit rating agencies. The CRA in particular requires UK based credit rating agencies to be registered with the FCA, the body responsible for their ongoing supervision.

21. Are there taxation considerations in your jurisdiction for originators, securitisation SPVs and investors?

<u>In relation to originators, the key taxation considerations include:</u>

Corporation tax treatment of asset sales into the securitisation structure

The corporation tax treatment of the assets sold to the SPV will depend on the nature of those assets and the way the securitisation is accounted for. Generally speaking, where a securitisation is accounted for as a financing by the originator, it should be possible for a UK-based originator to be taxed as if it had borrowed the funds raised by the securitisation, and continued to own the assets that had been disposed of. This treatment may not be appropriate where the assets being securitised are certain non-financial assets, or where the securitisation is not treated as a financing; in which case, the tax treatment of the sale will depend on the nature of the underlying assets and may give rise to corporation tax charges on any gain resulting from the disposal. The current rate of UK corporation tax is 19 per cent.

Generally speaking, the securitisation should not give rise to a VAT cost for the originator, although the exact VAT consequences can be complex.

Other than in the case of certain interests in real estate and certain equity-like securities, there are no stamp duties or other transfer taxes in the UK on the disposal of financial assets to an SPV.

<u>In relation to securitisation SPVs, the key taxation considerations include:</u>

Most UK public true sale securitisations will be structured to fall under the Taxation of Securitisation Companies Regulations 2006. The regulations allow securitisation companies to be subject to corporation tax simply on the cash profit retained within the company after the payment of its disbursements under the transaction waterfall. Broadly, in order to fall within this tax regime, the securitisation SPV must qualify as a securitisation company. Generally:

- an SPV that issues notes (valued at least GBP 10 million at the date of issue) wholly or mainly to independent investors and holds financial assets as security for those notes (a

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note-issuing company);
- an SPV that is funded by a note-issuing company or intermediate borrowing company, and holds financial assets as security for the capital market arrangement entered into by a note issuing company (an asset-holding company);
- an intermediate borrowing vehicle that is funded by a note-issuing company or another intermediate borrowing company (an intermediate borrowing company);
- an SPV that acquires or holds financial assets for the purpose of transferring them to an asset-holding company or note-issuing company (or itself becoming the same) (a warehouse company);
- satisfy the 'payment condition' at all times (ie, that all amounts received flow through to investors within 18 months of the end of the accounting period, other than the SPV's retained profit in the waterfall, and any amounts reasonably required to cover losses and support creditworthiness);
- not be party to any transactions for which avoiding UK tax was one of the main purposes; and
- as a general rule, not be involved in any business activities other than those that are incidental to its role as an SPV in the securitisation.

Certain types of receivable, particularly receivables arising from loans, royalties and real estate rentals, are subject to UK withholding tax unless an exemption applies. Generally, where the receivables are sold to a UK resident SPV, an exemption should apply to the underlying receivable so that no withholding tax is due from the underlying obligor. It is therefore usual for loan portfolios to be securitised through a UK resident SPV; trade finance and other trading payments are more frequently securitised via SPVs in other jurisdictions.

In relation to investors, the key taxation considerations include:

Withholding tax

Interest paid on securitisation notes issued by an SPV in the UK will be subject to UK withholding tax at 20 per cent unless an exemption, or a relief, applies.

An exemption that is often used, particularly where notes are intended to be widely distributed, is the "quoted Eurobond" exemption that applies where the notes are "listed on a recognised stock exchange". Many exchanges qualify for these purposes, including the London Stock Exchange, Euronext Dublin, the Luxembourg Stock Exchange and the International Stock Exchange of the Channel Islands.

Where notes are privately placed with investors resident in jurisdictions which are party to a double tax treaty with the UK that includes a "non-discrimination" article, the "qualifying private placement" exemption is sometimes used. Alternatively, for example in the case of a structured trade receivable securitisation that is ultimately funded by the issue of commercial paper, relief may be obtained by virtue of a double tax treaty (utilising, where appropriate, HM Revenue and Customs' Double Taxation Treaty Passport Scheme).

Stamp duty

Notes that fall within the loan capital exemption from UK stamp duty and stamp duty reserve tax are exempt from such duties and securitisation notes are usually structured to qualify as such.

22. To what extent does the legal and regulatory framework for securitisations in your jurisdiction allow for global or cross-border transactions?

In terms of governing law, multi-jurisdictional securitisation transactions are often governed by English law due to the flexibility offered by English contract law and the English legal system. It is not unusual for securitisation transactions with an English law element to involve transaction parties from a multitude of locations globally.

From a European perspective, following the end of the Brexit implementation period on 31 December 2020, any securitisation with an originator, SSPE or sponsor that is not located within the European Union is no longer eligible to qualify for the EU Securitisation Regulation "STS" label.

It is possible that the UK Government could amend the legislation that implements the EU Securitisation Regulation into the domestic laws of the UK in order to remove barriers to investment in domestic and international securitisation transactions.

23. To what extent has the securitisation market in your jurisdiction transitioned from IBORs to near risk-free interest rates?

Since Andrew Bailey, the Chief Executive of the FCA, announced in July 2017 that the FCA would no longer compel panel banks to submit rates to enable LIBOR to be calculated after 2021, considerable work has been

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done to move away from LIBOR and towards near risk-free rates. In the sterling markets, the Sterling overnight index average ("**SONIA**") has been identified as the preferred risk-free rate, SONIA having been administered and published by the Bank of England since April 2018.

Significant progress has been made in the sterling markets in the transition to SONIA and, according to the Q3 2020 AFME report, SONIA is now the market norm for new issuance of floating rate notes for securitisations. As at the end of Q3 2020, the total issuance of SONIA-linked floating rates notes for securitisations since 2018 was GBP 27 billion.

24. How could the legal and regulatory framework for securitisations be improved in your jurisdiction?

We would see the following areas in which the regulatory framework for securitisations could be improved:

- under the laws of certain European countries and under New York law clauses in contracts that seek to restrict the ability of parties to assign rights (including receivables) thereunder (ban on assignment clauses) are rendered void or ineffective in order to allow companies to generate finance from their accounts receivable arising from such contracts. In secondary legislation under the Small Business, Enterprise and Employment Act 2015, the UK Government implemented a tool like this but with heavy restrictions, only applying to certain small businesses. The market for certain securitisations would be liberated by the extension of this kind of legislation.
- the UK Government and the FCA and PRA could consider changing certain reporting obligations under the EU Securitisation Regulation, as implemented into the laws of the UK, in order to remove or reduce some of the burdens of the legislation on transactions.
- some of the reporting templates under the EU Securitisation Regulation, as implemented into the laws of the UK, are unclear or difficult to apply to certain asset classes. The UK Government in connection with the FCA and the PRA could seek to improve this.
- the range of transactions that fall within the scope of "securitisations" for the purposes of the EU Securitisation Regulation, as implemented into the laws of the UK, is very wide and indeed larger than the traditional conception of a securitisation. This has resulted in certain simple transactions being required to comply with burdensome rules that may arguably have been designed for larger, more complex securitisation transactions. The UK Government could consider exempting certain transactions from the legislation.

We would note in relation to the regulation of securitisation in the UK that although we do have clarity that the FCA and the PRA will regulate securitisation in the UK following Brexit, it remains to be seen how the FCA and the PRA will exercise their powers under the legislation and whether in time different interpretations of existing requirements or even if amendments to legislation will eventually be bought forward to amend the operation of the legislation in the UK.

25. To what extent has the impact of COVID-19 changed practice and regulation in relation to securitisations in your jurisdiction?

The Corporate Insolvency and Governance Act 2020 ("**CIGA**") came into force on 26 June 2020 and introduced changes to the UK's insolvency regime, some temporary and some permanent. Although these changes do not directly regulate securitisation transactions they may be relevant to securitisation transactions in certain instances.

On the temporary changes (most due to expire on 30 March 2021, though they may be extended), creditors were prevented from presenting winding-up petitions based on unpaid statutory demands or unpaid judgment debts, the bar on entry into a moratorium (for companies who had been in a moratorium in the preceding 12 months) was extended and there was a statutory override implemented on 'ipso facto' insolvency clauses in English law contracts – clauses that provided for automatic termination upon the insolvency of one of the parties – in order to assist companies to "trade out" of insolvent conditions.

Permanent changes in CIGA are two new rescue mechanisms, the scheme or arrangement for companies in financial difficulty and a 20 days moratorium during which no legal action can be taken. There is also a new restructuring plan (under part 26A of the Companies Act 2006) which allows for a "cross-class cram-down", similar to US Chapter 11 proceedings.

The EU Securitisation Regulation (as implemented into domestic laws of the UK) provides that when certain "significant events" occur in relation to a securitisation,

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this should be reported by the entity responsible for transaction reporting. This reporting should be sent to the holders of the securitisation positions and the competent authorities. The FCA and PRA have published guidance clarifying that significant events that occur in relation to securitisation transactions should be reported to the relevant regulator for that transaction. Due to the economic uncertainty and difficulties that have arisen from COVID-19, this may lead to significant events reporting obligations being triggered due to COVID-19.

A more detailed discussion of the impact of COVID-19 on securitisation transactions including significant event reporting can be found at https://www.gide.com/en/news/covid-19-effects-of-the-crisis-on-european-securitisation-transactions.

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