

SHORTCOMINGS IDENTIFIED BY AMF REVIEW OF STS SECURITISATIONS

In a summary of findings from its SPOT¹ inspections of STS securitisations published 30 August 2022 (the "**Report**"), the French Autorité des marchés financiers ("**AMF**") identified significant shortcomings in market practices, as well as certain "good" and "poor" practices associated with the use of the STS label. In this briefing we review the findings of the Report and consider its implications for both French and broader European STS market participants.

Background

The Report summarises the AMF's findings of a review of five credit institutions authorised to provide investment services (the "**investment services providers**" or "**ISPs**") by the AMF and covered a period from 1 January 2019 to 30 September 2021 (with inspections taking place between November 2021 and February 2022).

The focus was on (i) the arrangements for determining the STS nature of a transaction and its notification, (ii) control systems and (iii) arrangements for withdrawal and monitoring of the STS label.

The Report therefore has a strong focus on the procedural aspects of the STS label², rather than the substance of how to interpret and apply the STS criteria. The observations on "good" or "poor" practices are not formal regulatory requirements, and the AMF goes out of its way to point out that they are neither a position nor recommendation. Nonetheless, the Report cannot help but be a public pronouncement of the views of the regulator about how the STS label should be administered, and its findings are likely to form part of the future supervisory dialogue with regulated firms about compliance with the STS regime.

The AMF detected significant shortcomings in the practices of investment service providers in relation to STS securitisations. The AMF considers the quality of the arrangements it discovered shows an insufficient level of maturity, sometimes due to a poor understanding of the regulations and the absence of formal processes by one firm. It recognised that the different and

Key issues

- Significant shortcomings identified in the market practices relating to STS securitisations
- Report focusses heavily on control systems and procedural aspects relating to STS
- A number of "good" and "poor" practices were identified, none of which constitutes a "recommendation or a position"
- Establishment of a specific STS committee and use of third party verifiers both encouraged
- Reminder that notification of both ESMA and AMF in a timely fashion is required
- The Report will likely establish a benchmark to be used in further regulatory discussions in France and may well influence national competent authorities in other EU countries.

¹ *Supervision des Pratiques Opérationnelle et Thématique* (Operational and Thematic Supervision of practices).

² Both ABCP and non-ABCP STS transactions were analysed (142 in total); synthetic securitisations were not included in the study.

uneven practices may in part be explained by the different roles (e.g. originator vs. sponsor) the sampled institutions carry out in the transactions which were inspected.

It is not clear whether the AMF is adopting a "one size fits all" approach or whether it will adopt a proportional approach to the level of formal procedures required according to the nature of each institution and its role in STS securitisations. In any case, it is likely that firms will need to develop some level of formalised procedures not only for the grant but also for the on-going monitoring of compliance with the STS label. It is these systems and processes that the AMF identified as lacking, even for the ISPs in the sample that did relatively few STS securitisations and which had adopted the position that they therefore did not need such formal compliance structures in place.

Although the findings are made by the AMF, they may be of relevance as a benchmark as to the expectations of other national and EU level supervisors as to the standards for compliance with the STS label.

KEY RECOMMENDATIONS

The AMF set out a series of both good and poor practices, as well as reminders to market participants of their regulatory obligations. These are set out below.

Good practices

It is good practice to:

- set-up a committee dedicated to the subject of STS securitisations;
- use an authorised third-party verifier to ensure compliance of a securitisation transaction with the requirements of the STS label and to minimise the risk of anomalies;
- include the STS notification sent to ESMA when notifying such a transaction to the AMF as competent national authority;
- automate the process for sending STS notifications;
- formalise, in a specific internal procedure, the operational conditions and timeframes for STS notifications to be made to ESMA and the AMF;
- have an IT tool to verify a transaction's compliance with the STS criteria and to monitor this data;
- identify and to record and present formally events that can lead to withdrawal of the STS label; and
- establish a specific committee for STS transactions to determine whether transactions are eligible or ineligible on an on-going basis.

Poor practices

It is poor practice:

- (i) not to review the verification report or the gap analysis (where the ISP commissions e.g. a law firm to prepare such an analysis in place of employing an authorised third party verifier); and/or (ii) to monitor only the data derived from servicer reports without verifying key control points underlying those reports; and

- not to inform the other parties to the transactions, including the originators in the event that the STS label is lost.

Reminder of regulatory requirements

The AMF issued a reminder to market participants about the following regulatory responsibilities associated with STS securitisation:

- the originator, sponsor or securitisation special purpose entity can use a third-party verifier. However, the entity remains liable for the securitisation transaction's compliance with the requirements of the STS label;
- when they choose to claim the STS label, originators and sponsors must send ESMA a notification when a non-ABCP securitisation transaction complies with the STS criteria. In the case of ABCP, only the sponsor is responsible for STS notification;
- the STS notification is one of the documents to be made available before pricing;
- the final documentation shall be made available to investors at the latest 15 days after closing of the transaction;
- the national competent authority shall be informed of STS notification for each STS transaction;
- a traditional cash STS securitisation transaction must have a securitisation special purpose entity, which acquires the title to the underlying exposures by means of a true sale or assignment or transfer with the same legal effect;
- investment firms shall establish and maintain a permanent and effective compliance function. Compliance with these provisions is especially pertinent for dynamic transactions (e.g. for revolving transactions);
- when a securitisation transaction no longer meets the requirements of either Articles 19 to 22 or Articles 23 to 26, the originator and sponsor shall immediately notify ESMA and inform their national competent authority; and
- investment services providers shall establish rules and procedures enabling them to ensure compliance with the measures applicable to them.

MAIN FINDINGS

The above reminders and examples of good and poor practice come out of the AMF's review of existing procedures and controls in place at the five ISPs it surveyed. Some of those findings are summarised below:

Procedures governing the grant of the STS label

Of the five firms in the sample, two firms had no bespoke procedures. The other three firms had procedures but of uneven quality. Only one firm had a formal procedure including governance, the role and responsibility of market participants specifying direct operational implications.

Committees for granting the STS label

Only one firm had a committee dedicated to the STS certification of its transactions. For the other four firms, certification decisions were taken by the

team structuring the transaction in parallel with a committee supervising the securitisation activity generally.

Use of an authorised third-party verifier of STS compliance

Four of the five firms had used such an authorised independent verifier at least once.

Notification of ESMA and the AMF

All five firms had notified ESMA of all their STS securitisations but the delay for notification varied from one day to fifteen months. The Securitisation Regulation stipulates that the STS notification is one of the documents which must be available before pricing. There were major disparities in practice regarding notifications to the AMF as national competent authority.

Legal documentation

While in most cases the legal documentation was consistent with the information notified to ESMA, for two transactions the inspection found that the STS label had been granted even though no securitisation special purpose entity was being used. The Securitisation Regulation expressly requires "true sale" STS transactions to have a securitisation special purpose entity.

Control systems

Practice in terms of *ex ante* pre-notification controls varies. Three firms had pre-notification controls but level-one only³; two firms had not implemented *ex ante* controls.

No firm in the sample has implemented a level-two control before granting the STS label. The AMF does not consider that use of a third-party verifier or independent law firm justifies the absence of additional internal control.

Ex post controls of the inspected STS transactions were only partially satisfactory. The absence of adequate *ex post* controls could hamper the detection of events which call into question compliance with the STS criteria.

Major disparities were noted in practices regarding the arrangements for monitoring and withdrawal of the STS label – three firms do have such arrangements but two firms had no arrangements for monitoring and withdrawal of the STS label.

CONCLUSION

Market participants will likely wish to review their existing practices surrounding STS securitisations and consider whether they need to adopt a more formal approach. In particular, they may wish to examine the need for a formal STS committee, and the processes and procedures they have in place to ensure existing STS securitisations are effectively monitored on an ongoing basis.

³ A guide to the levels of internal controls is available on p. 2 of this document: https://acpr.banque-france.fr/sites/default/files/20220311_guide_controle_interne.pdf

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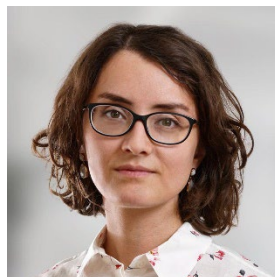
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