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# FCA VS PRA SECURITISATION RULES: TACKLING THE UNNECESSARY BURDEN OF DUAL COMPLIANCE

Since the new "Smarter Regulatory Framework" rules for securitisation came into force on 1 November 2024, there has been a fair bit of back and forth in the market about the right approach to compliance – and in particular whether it is necessary to have contractual undertakings to comply with more than one set of UK rules. In this briefing, we review the situation and suggest what we think is the best approach to these undertakings, attempting to balance certainty with the ability to take advantage of the less prescriptive approach permitted by the new regime in the UK.

## BACKGROUND

As part of the UK Government's wider "Smarter Regulatory Framework" ("**SRF**") initiative, it replaced the "assimilated" version of the EU Securitisation Regulation with a Statutory Instrument and rules made by the Financial Conduct Authority ("**FCA**") and Prudential Regulation Authority ("**PRA**"). This change took effect on 1 November 2024.

Since then, the market has been working through its approach to these new rules and, in particular, to the fact that different UK rules can apply to different entities on a single transaction. One approach we are seeing, and that gives us pause, is a sort of "dual compliance" approach similar to the one that had evolved since the end of the Brexit transition period. Since then, it has been relatively common for, e.g., a UK originator to undertake contractually to comply to some degree with EU disclosure and risk retention rules, on top of undertaking to comply with UK rules that apply directly to it. This is done in order to ensure EU institutional investors are able to comply with their own regulatory due diligence obligations and to invest.

What we are now seeing is some market participants taking a similar approach as between the FCA and PRA securitisation rules. In the most extreme case, a bank investor (subject to PRA rules) might ask a non-bank originator (subject to FCA rules, or indeed subject to no UK rules because it is based overseas) to agree contractually to comply with both FCA and PRA disclosure and risk retention rules. It seems to us this is unnecessary in the context of the new UK due diligence rules – as to which see below – and we are concerned that it may be imposing unnecessary additional compliance

**Key issues**

- Since 1 November 2024, the UK Securitisation Framework has two sets each of risk retention and disclosure rules
- We have seen some market participants seeking "dual compliance" with both the FCA and PRA rules, which is not necessary and has the potential to lead to unnecessary compliance costs
- Change of law risk is often cited as the reason for requesting these types of undertaking, but we do not see this as a compelling argument.
- We are concerned that, if this approach becomes widely-accepted market practice, the market may effectively lose the benefit of the greater flexibility deliberately provided by the FCA and PRA in their new rules.

costs for market participants that they will find difficult to move away from if this market practice becomes bedded in.

## RISK RETENTION

The new due diligence rules imposed by both the FCA and the PRA are explicit that their respective regulated institutional investors may invest in a securitisation position if **either** the FCA or PRA rules are complied with.[1] In other words, the regulators have contemplated the precise issue of having both FCA- and PRA-regulated parties (and indeed overseas parties subject to neither set of rules) on a single transaction and they have been explicit that this type of "dual compliance" undertaking is unnecessary. A similar approach has been taken by HM Treasury in the due diligence rules it imposes on occupational pension schemes ("**OPS**") in respect of UK retainers[2].

### Overseas retainers

While the PRA and FCA due diligence rules take the same agnostic approach to whether overseas retainers comply with PRA or FCA risk retention rules, the same cannot be said of the due diligence rules applicable to OPS. Those rules require an OPS investing in a securitisation with an overseas retainer to verify compliance with:

> "…rules made by the FCA or PRA relating to risk retention requirements **which would be applicable FCA or PRA rules** were the originator, sponsor or original lender to be established in the United Kingdom" (emphasis added)

As a result, even though both the PRA and FCA rules are agnostic, the rules applicable to OPS require them to engage in an exercise of determining whether the PRA or FCA risk retention rules would be applicable to the retainer if they were established in the UK. We understand informally that it may not have been the intention to require OPS to go through this exercise, but we nonetheless consider that additional certainty can be gained by doing so given the primacy given to "plain meaning" in UK statutory interpretation.

In any case, compliance with one or the other of the FCA or PRA risk retention rules is required, but never compliance with both.

## DISCLOSURE

The case against a "dual compliance" approach to disclosure is even clearer. Each of the FCA rules, the PRA rules and the due diligence rules applicable to OPS empowers the relevant institutional investor to decide what information they need, provided (a) it is sufficient for them independently to assess the risks of the investment and (b) that at least some information is provided in each of several broad categories. That is to say, even where the originator, sponsor and SSPE are in the UK, there is no specific requirement for a UK institutional investor to check that they are getting any kind of UK-prescribed reporting template. Where – as there often is – there is an undertaking from the reporting entity to report on EU templates as they exist on the date the deal is done, that should plainly be sufficient for investors to conclude they have received "sufficient" information.

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[1] See SECN 4.2.1R(1)(c) and (d) in the FCA Handbook and Article 5(1)(c) and (d) of Chapter 2 of the Securitisation Part of the PRA Rulebook.
[2] See Regulation 32B(1)(c) the Securitisation Regulations 2024/102.

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Clearly it is reasonable to ask for an undertaking to comply with the law (including applicable disclosure rules), so requiring an undertaking to comply with any rules directly applicable to a relevant UK-established sell-side party will be sensible on the basis that investors want to know that their transactions are compliant. But asking for compliance with both sets of rules "just to be sure" is unnecessary and unhelpful unless required by the – admittedly common – circumstances (e.g., where there is both a UK bank originator subject to PRA rules and a UK SSPE subject to FCA rules on the same deal).

Nonetheless, we have seen a number of cases where investors/lenders are requesting the delivery of templates contemplated by one or both of the FCA or PRA securitisation rules, even where the relevant sell-side parties are overseas. Although we understand that this may provide a comforting security blanket[3], we can't help but think this practice of voluntarily relinquishing the flexibility granted by the FCA and PRA in their "SRFing" of the securitisation rules may be unwise, because it may result in the creation of a market practice whereby full UK templated disclosure is considered necessary despite the clear intention of the regulators that it should not be.

There are also a number of less egregious cases, such as a UK investor/lender wanting an undertaking from the sell side to provide any information they might need to fulfil their regulatory due diligence requirements in the future. This, too, is a holdover from the old due diligence rules which were highly prescriptive, but not 100% clear, leading to the possibility that a regulator might later tell an institutional investor they needed a further piece of information to "tick a box" in order to comply. Now that it is up to institutional investors to decide what information is sufficient, that risk has gone, and the related undertaking should in our view go as well, or at least be qualified by reference to a specific regulatory intervention requiring the investor to obtain the specific additional information. All of these points will need to be considered with extra care on extensions of existing transactions.

## THE BOTTOM LINE

All this leads to a conclusion that it is only ever necessary for a UK investor to obtain an undertaking for a risk retainer to comply with one of the FCA or PRA risk retention rules, but never both. Even in the case of overseas retainers who want to ensure UK OPS can invest, there is an exercise that is relatively simple in most cases, to determine which set of rules should be complied with.

Likewise, it is not necessary (on the basis of UK due diligence rules) to request that reporting entities provide templated disclosure as contemplated in both the FCA and PRA rules, but it will often be sensible anyway as a matter of ensuring compliance with the law applicable to the sell side. Even then, reporting covenants should take account of the fact that the FCA and PRA templates are currently identical and make clear only one report need be prepared – a practice we have seen a number of times.

Where all sell-side parties are outside the UK, it will generally not be appropriate to have undertakings to provide UK-style disclosure at all. UK institutional investors are required to assess the sufficiency of the disclosure they are (and will be) getting before investing, so the disclosure package should be contractually agreed and fixed for the life of the transaction.

[3] It would be hard for a regulator to tell you the information you had received was not "sufficient" if it was everything they themselves required on the disclosure side.

Regardless of where the sell-side parties are located, we can see no justification rooted in the UK due diligence rules for any undertakings to produce further information (beyond that agreed in the original transaction documentation) in order to comply with any applicable UK regulatory due diligence obligations. Since UK institutional investors are in any case required by law to assess the sufficiency of the disclosure package before investing, we cannot see that including such a right to require further information would be particularly helpful for this purpose in any case.

### What about change of law risk?

An argument is sometimes made that compliance with both FCA and PRA rules is desirable because there may be a change of law in the future. Such a change of law may make it useful for investors to have contractual undertakings from the sell side to comply with both the FCA and PRA rules in order to limit investors' change of law risk. While we understand the appeal of this argument, we think on balance that it should not carry the day.

The main reason for this is that second-guessing such fundamental changes in approach is impossible and trying to do so almost certainly creates more problems than it solves. This is not like a provision requiring the sell side to make best efforts to adapt to a changed reporting template or fill in a new tax form to avoid withholding. While we acknowledge that it is not impossible the due diligence rules might change to require compliance with each authority's own risk retention rules, or to require investors once again to obtain disclosure in the form required by their own regulator's rules, both the FCA and PRA have been very clear this is not their approach, and HM Treasury have gone so far as to impose a legal requirement on the FCA and PRA to have regard to the "coherence of the overall framework for the regulation of securitisation"[4] when making their rules. For public deals, at least, one solution would of course be to rely on the provision included in most deals now allowing the issuer to agree changes to the documentation necessary to comply with any regulatory requirements.

More prosaically, the UK has historically had a firm commitment to legal certainty, and has accordingly always provided grandfathering when changing conduct rules (even if the authorities sometimes need reminding to put it in). They also have a history of being generous in providing lead times between rules being finalised and being implemented. These features of the UK legal system should obviate the need to amend most existing transactions even if there is a change of law. They should also provide the rest with a sensible window to decide how to deal with any future change of law once they have specific knowledge of what it will be.

## CONCLUSION

While we understand that it is a sense of wishing to take a "conservative" approach that is largely driving requests for dual compliance, we are concerned the market may be acting against its own interests by hesitating to take advantage of the additional flexibility provided by the new due diligence rules adopted by the UK authorities as part of the SRF process. We hope that on further consideration, more parties will conclude that a less prescriptive approach will lead to lower compliance costs, less regulatory friction, and will end up being better for everyone.

[4] See Regulation 8(1) of the Securitisation Regulations 2024/102.

This publication does not necessarily deal with every important topic or cover every aspect of the topics with which it deals. It is not designed to provide legal or other advice.

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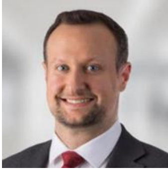

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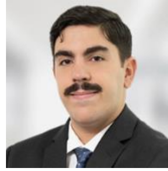

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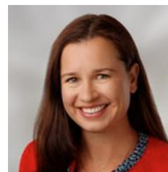

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