A Q&A guide to securitisation in the UK (England and Wales).
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Market and legal regime

1. Please give a brief overview of the securitisation market in your jurisdiction. In particular:
   > How active and/or developed is the market and what notable transactions and new structures have taken place recently?
   > To what extent have central bank liquidity schemes assisted the securitisation market in your jurisdiction? Were retained securitisations common in the last 12 months?
   > Is securitisation particularly concentrated in certain industry sectors?

The securitisation market was, until mid-2007, both active and well developed, for public and private transactions, with one of the first mortgage-backed securitisations (MBS) taking place in 1987. However, since then, the securitisation market has been severely affected by turbulence in the financial markets, and investors have largely shunned securitisation, in particular, the more complex structures such as collateralised debt obligations (CDOs). After an extended dearth of new primary market issuances, the securitisation market appears to have partially recovered in the second half of 2009.

For the last two years, issuance has been sustained through retained securitisations and many financial institution originators have used these structures. These structures involve the issue and retention by the issuer of asset-backed securities (ABSs) in an innovative way to:
   > Refinance existing debt.
   > Obtain liquidity by accessing various central bank liquidity schemes (such as the Bank of England’s Special Liquidity Scheme and Discount Window Facility, and the European Central Bank’s (ECB’s) open market operations) through repo transactions.

Retained securitisations were common in the UK but their use has decreased as central banks have tightened their eligibility criteria both:
   > In recognition of the fact that these securities have not been created with marketability to third party investors in mind.
   > To encourage originators to return to a self-sustaining market.

As a result, some European originators have started to issue covered bonds backed solely by legacy residential mortgage-backed securities (RMBS). This trend may be duplicated in the UK.

There were very few securitisation transactions in the public domain of UK originators in 2009. A handful of deals were concentrated in the RMBS, commercial mortgage-backed securities (CMBS) and asset-backed securities (ABS) sectors, with no issuance in the more complex collateralised debt/loan obligation (CDO/CLO) sectors.
Notable transactions included:

> In the CMBS sector, Tesco originated three corporate securitisations in 18 months, backed by rental income from its retail stores and distribution warehouses. Land Securities raised GB£360 million (about US$591.9 million) through a sale of bonds secured by the cash flows from a London property lease held by the UK government through Sceptre Funding No. 1 Plc.

> In the RMBS sector, Lloyds’ GB£2.8 billion (about US$4.6 billion) issuance under its Permanent master trust programme and Nationwide’s Silverstone GB£3.3 billion (about US$5.4 billion) AAA-rated UK RMBS in November 2009.

> Volkswagen’s EUR519 million (about US$763.5 million) auto lease ABS in September 2009.

> In the WBS sector, Wales and West Utilities’ GB£250 million (about US$411 million) secured bond containing “flipper” language (that is, allowing bonds to migrate into a securitisation structure within 24 months) and Yorkshire Water’s GB£650 million (about US$1.1 billion) WBS three-tranche bond.

> Barclays Bank’s six issues through a new covered bonds programme backed by loans to local authorities in the UK, the first deal of its type in the country.

For further details on the classes of receivables referred to in this chapter, see Model Guide, table, Classes of receivables.

2. Is there a specific legislative regime within which securitisations in your jurisdiction are carried out? In particular:

> What are the main laws governing securitisations?

> Is there a regulatory authority?

Other than certain tax laws relating to the taxation of securitisation companies (see Question 26), there are no laws specifically providing for securitisation transactions.

Unless there is a specific reason otherwise, the contractual documents for securitisations of assets situated in England and Wales are usually expressed to be governed by the law of England and Wales.

In relation to issuing the securities, the relevant laws applicable to offers or listing of securities, which are primarily derived from EU legislation (including Directive 2003/71/EC on the prospectus to be published when securities are offered to the public or admitted to trading (Prospectus Directive)), are:


The FSMA confers on the FSA the functions set out in Part VI of FSMA, which include acting as competent authority for the purposes of making the Prospectus Rules, Listing Rules and Disclosure and Transparency Rules. As competent authority, the FSA (as the UK Listing Authority) is responsible for vetting and approving prospectuses for the purposes of the Prospectus Directive.

Banks, insurers and other entities regulated by the FSA must have regard to the rules of the FSA’s General Prudential Sourcebook. The two most significant aspects of the General Prudential Sourcebook in relation to securitisation transactions are the:

> Rules relating to the risk weighting that must be attributed by FSA-regulated entities to investments in capital markets instruments.

> Capital treatment of securitisations for FSA-regulated originators of securitisations. The rules relating to the capital treatment of securitisation are set out at chapter 9 of the Prudential Sourcebook for Banks, Insurance Companies and Investment Firms (BIPRU).
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The Regulated Covered Bond (RCB) Regulations 2008 came into force on 6 March 2008, in compliance with Directive 85/611/EEC on undertakings for collective investment in transferable securities (UCITS Directive). This regime ensures that UK covered bonds can be UCITS-compliant and so obtain the same treatment as other EU covered bonds for regulatory capital purposes.

Reasons for doing a securitisation

3. Which of the reasons for doing a securitisation, as set out in the Model Guide, usually apply in your jurisdiction? In particular, how are the reasons for doing a securitisation in your jurisdiction affected by:
   - Accounting practices in your jurisdiction, such as application of the International Financial Reporting Standards (IFRS)?
   - National or supra-national rules concerning capital adequacy (such as the Basel International Convergence of Capital Measurement and Capital Standards: a Revised Framework (Basel II Accord) or the Capital Requirements Directive)? What authority in your jurisdiction regulates capital adequacy requirements?

Usual reasons for securitisation
Securitisations can be carried out for all the reasons specified in the Model Guide (see Model Guide, Reasons for doing a securitisation (www.practicallaw.com/2-501-2997)).

Accounting practices
All UK listed companies are required to use the international accounting standards (IAS) when preparing their consolidated accounts for accounting periods on or after 1 January 2005. Their individual accounts can, but are not required to, be prepared according to the IAS.

Non-listed companies and entities other than companies can, but are not required to, prepare their accounts according to IAS. It is still open to those companies and entities to use UK generally accepted accounting principles (GAAP).

IAS39 is of particular relevance to securitisations because it determines, for accounting purposes, the extent of the recognition and measurement of financial instruments in a company’s financial statements. Securitisations are often undertaken to derecognise the receivables in the originator’s financial statements (see Model Guide, Balance sheet benefits) and, therefore, the application of IAS39 is important.

Capital adequacy
Securitisations are undertaken to manage the regulatory capital risk weighting of assets on an originator’s balance sheet (see also Questions 2 and 27).

The special purpose vehicle (SPV)

Establishing the SPV

4. How is an SPV established in your jurisdiction? Please explain:
   - What form does the SPV usually take and how is it set up?
   - What is the legal status of the SPV?
   - How is the SPV usually owned?
   - Are there any particular regulatory requirements that apply to the SPVs?

An SPV is normally established with its own corporate identity and independent legal status. An SPV is usually established as a private or public limited company incorporated under the Companies Acts. Occasionally, an SPV may be a limited liability partnership under the Limited Liability Partnership Act 2000.

If it is desirable that the SPV is not a subsidiary of the originator or other transaction party, the SPV’s shares are usually directly or indirectly held by a corporate services provider. The corporate service provider often holds the shares of the SPV on trust for discretionary charitable purposes.
There are no specific regulatory requirements applying to securitisation SPVs in particular, but the following general regulatory requirements apply:

> Issuers (and guarantors) of securities admitted to the Official List must comply with the applicable Listing Rules of the UK Listing Authority.
> Issuers of securities admitted to trading on a regulated market must comply with the Disclosure and Transparency Rules.
> SPVs must also comply with the requirements under the Companies Act 2006 or other generally applicable legislation.

5. **Is the SPV usually established in your jurisdiction or offshore? If established offshore, in what jurisdiction are SPVs usually established and why? Are there any particular circumstances when it is advantageous to establish the SPV in your jurisdiction?**

The SPV’s jurisdiction of establishment is often England and Wales. This has the advantage of increased legal certainty in terms of enforcement and familiarity of market participants with the legislative regime applicable to companies. However, there may be a variety of reasons for the SPV to be established in other jurisdictions.

In determining the SPV’s jurisdiction of establishment, regard must also be had to any tax implications for the participants in the securitisation. These implications may also depend on wider factors, such as the jurisdiction where management and control of the SPV is exercised and where the SPV carries on its trade.

A further issue under insolvency law relates to the SPV’s “centre of main interests” (COMI) and its “establishment” for the purposes of Regulation (EC) No. 1346/2000 on insolvency proceedings (Insolvency Regulation) and the Cross-Border Insolvency Regulations 2006 (SI 2006/1030) (which implemented the UNCITRAL Model Law on Cross-Border Insolvency in the UK).

Despite the amendments introduced by the Companies Act 2006, Chapter VI of Part V of the Companies Act 1985 continues to prohibit financial assistance being given by a public company or its subsidiaries for the acquisition of its own shares (although there are certain exceptions). In circumstances where this prohibition would otherwise apply to a transaction, it may be appropriate to establish the SPV in a different jurisdiction with more relaxed rules, such as the Cayman Islands.

**Ensuring the SPV is insolvency remote**

6. **Is it possible to make the SPV insolvency remote in your jurisdiction? If so, how is this usually achieved?**

The SPV is often a separate corporate entity with no trading history and so no initial contingent liabilities. The following contractual provisions are commonly inserted in the applicable transaction documents to assist in insulating the SPV from creditor claims:

> Limited recourse provisions are used to limit the liability of the SPV to a creditor. Typically, recourse is limited to the net proceeds of disposal or enforcement or by a mechanism to convert securitisation debt to equity on enforcement.
> Non-petition provisions are also used in English law governed securitisation transactions. These purport to prohibit a creditor from taking legal action or commencing insolvency proceedings against the SPV. It is likely that a non-petition clause is valid, although there is little authority either way in English law.
> The SPV will typically covenant in the applicable transaction documents not to incur liabilities or to undertake activity outside those contemplated by the securitisation transaction.

It is not possible to be certain that an SPV will be completely insolvency remote. For example, the SPV may always incur tax liabilities and the UK tax authority, HM Revenue & Customs, may not be bound by the contractual provisions set out above.
Ensuring the SPV is treated separately from the originator

7. Is there a risk that the courts can treat the assets of the SPV as those of the originator if the originator becomes subject to insolvency proceedings? If so, can this be avoided/minimised?

Under English law, the principle of separate corporate identity is upheld.

Only in limited circumstances will the English courts pierce the corporate veil and treat the assets of the SPV as those of the originator (the doctrine of "substantive consolidation"). These limited circumstances include, among others, where separate legal identity is being used:

> For fraud or other illegal or improper purposes.

> To dishonestly place assets beyond the reach of creditors.

There is limited precedent for a court sanctioning the consolidation of two companies, both of which are in liquidation, but it is thought very unlikely that this would be sanctioned where one of the companies is still solvent. Although not substantive consolidation, insolvency set-off applies automatically on liquidation (and administration), with the effect that debts owed between the SPV and the originator can be set off against each other.

The securities

Issuing the securities

8. Are the securities issued by the SPV usually publicly or privately issued?

Securities are issued publicly and privately.

9. If the securities are publicly issued:

> Are the securities usually listed on a regulated exchange in your jurisdiction or in another jurisdiction?

> If in your jurisdiction, please briefly summarise the main documents required to make an application to list debt securities on the main regulated exchange in your jurisdiction. Are there any share capital requirements?

> If a particular exchange (domestic or foreign) is usually chosen for listing the securities, please briefly summarise the main reasons for this.

If the securities are to be listed, the usual exchanges (but by no means the only ones) are the regulated markets of the:

> London Stock Exchange.

> Irish Stock Exchange.

> Luxembourg Stock Exchange.

If listed in the UK, most debt securities are traded on the London Stock Exchange's Regulated Market.

An issuer’s securities must be admitted to the Official List of the UK Listing Authority and admitted to trading by a regulated stock exchange. The main documents that are required for an application to listing on the UK Listing Authority’s Official List and admission to trading on the regulated market of the London Stock Exchange are:

> A prospectus approved by the UK Listing Authority.

> UK Listing Authority Checklists.
In choosing the relevant market, market participants are influenced by several factors:

- Whether the applicable market has experience in, or developed a reputation for, the type of security being issued and the level of liquidity in securities of the applicable type. This may vary for different types of securitisation transactions. For example, whole business securitisations are often listed in Luxembourg or Ireland, while RMBSs of UK originators are usually listed in London.

- The identity of the competent authority in the applicable member state of the regulated market, which is responsible for vetting and approving any prospectus for the securities. Certain competent authorities are perceived as having a greater flexibility, consistency of approach or speed of response.

- Implementation of the Prospectus Directive in the EU has led to a difference in approach to the form and content of prospectus disclosure in EU member states, (particularly in relation to the assets underlying the securitisation) which influences the choice of exchange.

A company incorporated in England and Wales offering securities to the public must generally be a public limited company under the Companies Act, which requires a minimum authorised share capital of GBP50,000 (about US$82,200), of which a quarter must be fully paid.

**Constituting the securities**

**10. If the trust concept is not recognised in your jurisdiction, what document are the securities issued by the SPV constituted by and how are the rights in them held?**

Since English law recognises the law of trusts, the securities issued by an English SPV are generally constituted by trust deed.

**Transferring the receivables**

**Classes of receivables**

**11. What classes of receivables are usually securitised in your jurisdiction? Please explain any particular reasons (for example, the strength of the origination market) why such receivables are usually securitised and the progress of the market in securitising new classes of receivables.**

A wide range of receivable classes are securitised, including:

- Mortgages.
- Loans of all types.
- Lease and rental receivables.
- Credit card receivables.
- IP royalty receivables.
- Insurance receivables.
- Healthcare receivables.
- Ticket receivables.
- Receivables from public utilities.
The strength of the origination market for receivables in general, and the familiarity of securitisation as a financing tool in the market, are particular reasons why receivables are usually securitised.

Progress of the market in securitising new classes of receivables is constantly evolving. Two recent but diverse examples are:

> The securitisation of healthcare receivables from governmental bodies under the International Finance Facility for Immunisation.

> Electricity North West’s first of its kind securitisation of an electricity distribution utility and a holding company.

**The transfer of the receivables from the originator to the SPV**

12. How are the receivables usually transferred from the originator to the SPV (for example, assignment, novation, sub-participation, declaration of trust)? How is the transfer perfected? Are there any rules, requirements or exemptions that apply specifically to transferring receivables in a securitisation transaction?

Most classes of account receivables are usually transferred by assignment, which operates as a “true sale” transfer.

For perfection, English law makes a distinction between legal and equitable assignments. To take effect at law:

> The assignment must be absolute and not purport to be by way of charge only.

> The assignment must be in writing signed by the assignor.

> Express notice of the assignment (in writing) must be given to the debtor.

An assignment which does not comply with these conditions takes effect as an equitable assignment.

Other transfer methods include novation and declaration of trust.

There are no rules, requirements or exemptions that apply specifically to transferring receivables in a securitisation transaction as opposed to any other type of receivables sale.

13. Are there any types of receivables that it is not possible or not practical to securitise in your jurisdiction (for example, future receivables)?

Receivables, as contractual rights between originator and debtor, can be sold to a buyer under English law, with certain limited exceptions (see Question 15).

Contractual restrictions on transferring receivables, such as non-assignment clauses, may in practice result in it not being possible or practical to securitise those receivables. Certain receivables, such as deferred receivables from equity release mortgages, can be practically difficult to securitise given their inherent uncertainty of expected payment.

It is possible to securitise future receivables. An agreement to assign future receivables takes effect (without any further action required by the parties) as the future receivables come into existence. However, if the originator becomes insolvent, any prior agreement to assign future receivables only transfers those receivables automatically as they arise if no further action is required by the originator to originate or collect the receivables.

14. How is any security attached to the receivables transferred to the SPV? What are the perfection requirements?

The method of transferring the security attached to a receivable depends on how the security itself is constituted. Typically a security interest is created by an agreement or deed between the originator and debtor and in general can be transferred to the SPV by assignment, novation or declaration of trust.
Certain formalities apply when perfecting the assignment of security attaching to the receivable depending on what property the security is granted over. For example, to perfect an assignment of security over real estate, registrations must be filed at the Land Registry.

**Prohibitions on transfer**

15. Are there any prohibitions on transferring the receivables or other issues restricting the transfer? For example, is a negative pledge enforceable, or are there any legislative provisions that affect the transfer of receivables (such as consumer or data protection rules)?

**Contractual restrictions**

It is open to the parties to a commercial contract (such as a receivable contract) to agree that assignment is prohibited. If the contract does not prohibit assignment or is merely silent on the matter, then the originator can assign his rights under the contract without the consent of the debtor.

Even if there is a prima facie prohibition of assignment, it is important to establish whether the clause has in fact been breached. A non-assignment clause may in fact be drafted to permit novation or declaration of trust. However, breach of this clause will render the transfer ineffective against the debtor, meaning the debtor can continue to make payments to the originator/assignor in satisfaction of the debt. The assignment agreement between the assignor and assignee remains valid however, so the assignor will usually be in breach of contract itself.

**Legislative restrictions**

Although there are in general no legislative restrictions on assigning rights under commercial contracts, the assignment of certain rights is, however, prohibited by statute. For example, it is unlawful under the Social Security Administration Act 1992 to assign social security benefits. In certain other circumstances, assignment may be void on the grounds of public policy. The courts have in the past held that the salary of a public officer cannot lawfully be assigned, for example. However, commercial contracts rarely fall within these exceptional categories.

A buyer of consumer loans is likely to require a licence under the provisions of the Consumer Credit Act 1974, as amended by the Consumer Credit Act 2006.

The processing of information about living individuals is regulated by the Data Protection Act 1998. A buyer of receivables under which individuals are debtors is therefore likely to be a data controller within the meaning of the Data Protection Act, which means it must comply with the provisions of the Data Protection Act relating to the processing and keeping of information on the individuals.

**Avoiding the transfer being re-characterised**

16. Is there a risk that a transfer of title to the receivables will be re-characterised as a loan with security? If so, can this risk be avoided and/or minimised?

English courts look at the substance of a transaction, and whatever labels the parties have given to a transaction are not determinative. There is therefore a risk that a transfer of title will be re-characterised as a secured loan.

English courts have identified three essential differences between a sale and a secured loan:

> In a true sale transaction the originator is not entitled to have the sold assets returned to him if he returns the purchase price to the buyer. A secured loan such as a mortgage would feature this right.

> If a mortgagee sells the secured property for an amount in excess of the outstanding balance on the loan, he has to account to the mortgagor for any surplus. In a true sale, however, if the buyer sells the sold assets to a third party for a profit, there is no duty to account to the original seller for the profit.

> If a mortgagee sells the secured property for an amount that falls short of the outstanding balance on the loan, the mortgagor has to account to the mortgagee for any deficit. In a true sale, however, if the buyer sells the sold assets to a third party for a loss, there is no right to recover this loss from the seller.
The following features of securitisation transactions will not result in a true sale being re-characterised:

> Servicing arrangements.
> Derivative transactions to hedge interest rate risks.
> Profit extraction techniques.
> Obligations to repurchase assets that are in breach of warranty (assuming this is a genuine remedy for breach of warranty at the time of sale and not related to subsequent performance).

There is also a more remote risk that a sale may be classed as a sham transaction. This will only happen if the court detects an element of impropriety or dishonesty, in which case the court may hold that the sale agreement is merely a cover-up masking the real intention of the parties. The court may then ignore the terms of the sale agreement and rewrite the agreement according to how it views the respective rights and obligations of the parties.

**Ensuring the transfer cannot be unwound if the originator becomes insolvent**

17. Can the originator (or a liquidator or other insolvency officer of the originator) unwind the transaction at a later date? If yes, on what grounds can this be done and what is the timescale for doing so? Can this risk be avoided or minimised?

The Insolvency Act 1986 (as amended) provides for three situations in particular when an insolvency official (such as an administrator or liquidator) can unwind transactions at a later date.

**Transactions at an undervalue**

Where a company has entered into a transaction at an undervalue with any person and subsequently enters administration or goes into insolvency, a court can make an order restoring the position to what it would have been if the company had not entered into the transaction.

Undervalue is defined as gifts/transfers for no consideration and transactions where the consideration received in money or money’s worth is significantly less than the value of the assets disposed of by the company.

A defence will apply, however, where the court is satisfied that both:

> The company entered into the transaction in good faith for the purposes of carrying on its business.
> At the time of the transaction there were reasonable grounds for believing that the transaction would benefit the company.

**Preferences**

Where a company has given a preference to any person and subsequently enters administration or goes into insolvency, a court can once again make an order restoring the position to what it would have been if the company had not entered into the transaction.

A company gives a preference to a person if that person is one of the company’s creditors (guarantors are also included) and the company does anything which improves the position of that person beyond that which it would have been if the preference had not been given. When giving the preference, the company must have been influenced by a desire to improve the position of the creditor. This final requirement is presumed where the preference has been given to a person who is “connected” with the company. Directors, spouses and family relatives, among others, are connected persons for these purposes.

**Fraud or wrongful trading**

Although not technically unwinding transactions, actions for fraudulent or wrongful trading or actions in tort or restitution such as conversion or dishonest assistance (respectively) may result in contributions having to be made to the insolvency estate.
**Time restrictions**

Important time restrictions apply to both transactions at an undervalue and preferences. Transactions at an undervalue can be unwound if they have been entered into during the two years before the onset of insolvency, regardless of the relationship between the parties. A preference can be unwound if it has been entered into during the same two-year period, but only if the parties are connected. If the parties are not connected, preferences can only be unwound if they have been entered into within six months of the onset of insolvency.

**Establishing the applicable law**

18. Are choice of law clauses in contracts usually recognised and enforced in your jurisdiction? If yes, is a particular law usually chosen to govern the transaction documents? Are there any circumstances when local law will override a choice of law?


However, if a foreign law is chosen to govern a contract between two parties both located in England with contract performance also to take place in England, the courts continue to apply mandatory rules of English law regardless of the parties’ choice of foreign law.

There are several exceptions to the Contracts (Applicable Law) Act 1990 rules governing the choice of law for certain contracts (for example, certain insurance contracts). In such cases, the pre-existing common law applies, which generally gives effect to the parties’ choice of law.

If a governing law clause is omitted from a contract, and if the choice of law of the parties cannot be determined with reasonable certainty by the terms of the contract, the English courts apply the law of the country which the contract is “most closely connected” with (Contracts (Applicable Law) Act 1990). For corporate or unincorporated entities, this is presumed to be the location of the central administration (or, if the contract has been entered into during the course of trading, the location of the principal place of business) of the party who is to carry out the characteristic performance of the contract. Characteristic performance is usually not the payment of money, but performance of the obligation for which that money is due, such as the delivery of goods in a sale of goods contract.

English law is usually chosen to govern securitisation transaction documents in an English securitisation transaction. Sometimes there is a distinction between the choice of law for the receivables sale, where the local law governing the receivable may be chosen, and the bond issuance, where English law will usually govern the transaction documents.

The Contracts (Applicable Law) Act 1990 will not apply to contracts signed on or after 17 December 2009. From that date, The Law Applicable to Contractual Obligations (England and Wales and Northern Ireland) Regulations 2009 (reflecting Regulation (EC) No. 593/2008 on the law applicable to contractual obligations (Rome I)) will take effect. Rome I will not change the position in relation to choice of law, except that:

- It incorporates existing EC law applicable to insurance contracts.
- It makes small changes to the rules applicable to consumer contracts.
- Where the parties choose the law of a non-EU member state as the applicable law, but all relevant elements are located in the EU, the choice of law does not prejudice the application of the provisions of EC law which cannot be derogated from by contract.
Security and risk
Creating security

19. Please briefly list the main types of security that can be taken over the various assets of the SPV in your jurisdiction, and the requirements to perfect such security.

Security over a receivable is typically created by way of a charge (either fixed or floating) or assignment by way of security. Depending on the asset, security over the SPV’s assets can also be granted by way of mortgage or, for certain types of negotiable instruments, by way of pledge.

Requirements to perfect security interests depend on the property that is secured:

- An assignment by way of security is perfected in the same way as an outright assignment (see Question 12).
- A mortgage requires transfer of title to the mortgagee.
- A fixed charge requires control to be taken over the property.

Registration of the security may be required within 21 days after its creation under the Companies Acts. Security is void against third parties if it is not registered when required. The registration requirement applies to both:

- Any charge by a company registered in the UK.
- Any charge over property in England and Wales by a company incorporated outside Great Britain but with an established place of business in England and Wales.

Where the security is a financial collateral arrangement, it will also be governed by the Financial Collateral Arrangements (No. 2) Regulations 2003 (as amended), which relax certain perfection requirements.

For further information on taking security over assets in England and Wales, see PLC Cross-border Finance Handbook 2010/11, Country Q&A, UK (England and Wales).

20. How is the security granted by the SPV held for the investors? If the trust concept is recognised, are there any particular requirements for setting up the trust (for example, the security trustee providing some form of consideration)? Are foreign trusts recognised in your jurisdiction?

The security is usually held under a trust. An express trust, intentionally created, is used in securitisation transactions. The essential requirements for the creation of an express trust are as follows:

- Property or rights capable of being subject to a trust. This is readily satisfied in securitisation transactions, since it has long been established that the benefit of a right under a contract can be the subject of a trust.
- The declaration of trust must be by a person competent to create a trust. This is also easily satisfied in securitisation transactions, since any person or corporation capable of disposing of property or rights capable of being subject to a trust has capacity to create a trust.
- Certainty of intention must be manifested. Although no specific words are needed to show an intention to create a trust, the word trust itself will provide strong evidence that a trust was indeed intended.
- Certainty of subject matter. A trust will be void for uncertainty if the subject matter of the trust (the property held on trust) is not either expressly identified or defined in a manner that enables the subject matter to be capable of being identified.
- Certainty of objects. A trust will also be void for uncertainty if the beneficiaries of the trust are not either expressly identified or defined in a manner that enables the beneficiaries to be capable of being identified. In a securitisation transaction, this will be the noteholders.
- Lawful purpose.
The Hague Convention on the Law Applicable to Trusts and on their Recognition 1985 (Hague Trusts Convention) has been ratified in England and Wales by the Recognition of Trusts Act 1987. This provides for the recognition of foreign trusts according to whichever law is identified to govern the trust.

**Credit enhancement**

21. **What methods of credit enhancement are commonly used in your jurisdiction? Are there any variations or specific issues that apply to the credit enhancement techniques set out in the Model Guide?**

Creating subordinated tranches of notes is a method of credit enhancement commonly used. Letters of credit are used less frequently in securitisation transactions. The use of monoline insurance was a common structural feature but is now extremely rare due to the effect of the turbulent global markets on the monoline insurance sector.

Over-collateralisation (broadly where the expected income and principal proceeds from the underlying assets exceeds the amounts payable to investors) is also a commonly seen feature of securitisation transactions.

The use of credit enhancement techniques may vary on a transaction-by-transaction basis.

For further information on these methods of credit enhancement, see Model Guide, Credit enhancement.

**Risk management and liquidity support**

22. **What methods of liquidity support are commonly used in your jurisdiction? Are there any variations or specific issues that apply to the provision of liquidity support as set out in the Model Guide?**

Cash reserve funds and loans from the originator or a third party bank to the SPV are both methods of liquidity support commonly used in securitisation transactions (see Model Guide, Risk management and liquidity support).

Loans from the originator are usually heavily subordinated in any priorities of payment waterfall. Originators can also provide liquidity support by equity participation in the relevant SPV. However, FSA-regulated originators who are seeking to exclude their securitised exposure from the calculation of risk weighted exposure and expected loss amounts (see Question 3, Capital adequacy and Model Guide, Capital adequacy) must have regard to chapter 9 of BIPRU, which provides that it can only do so where there has been transfer of significant credit risk.

**Cash flow in the structure**

**Distribution of funds**

23. **Please explain any variations to the Cash flow index accompanying Diagram 9 of the Model Guide that apply in your jurisdiction.**

There are no specific variations applicable. Cash flow waterfalls are negotiated on a case-by-case basis. The order depends on the negotiating position of the parties involved and also any rating agency requirements. However:

> Typically, the originator can extract a senior fee income in its capacity as servicer, manager or other similar role near the top of the cash flow waterfall and, as specified in the Cash flow index (see Model Guide, box, Cash flow index), receive a subordinated equity return towards the bottom of the cash flow waterfall. This equity return may often be in the form of deferred consideration for the sale of assets to the SPV.

> Termination payments to the swap counterparty in the cash flow waterfall are usually subordinated in circumstances where the swap counterparty has defaulted.

> Separate cash flow waterfalls applicable to income and principal receipts from the assets may also be used.

> The cash flow waterfall may make provision for cash trapping in a reserve account in circumstances where principal repayments are required which do not match the expected cash flow.
Profit extraction

24. What methods of profit extraction are commonly used in your jurisdiction? Are there any variations or specific issues that apply to the profit extraction techniques set out in the Model Guide?

All the methods of profit extraction specified in the Model Guide are used (see Model Guide, Profit extraction).

The role of the rating agencies

25. What is the sovereign rating of your jurisdiction? What factors impact on this and are there any specific factors in your jurisdiction that affect the rating of the securities issued by the SPV (for example, legal certainty or political issues)? How are such risks usually managed?

Rating agencies may be concerned about a wide variety of legal risks depending on the underlying asset class and type of transaction. It is usual for rating agencies to closely examine transaction legal opinions. To the extent that a significant specific legal risk cannot be adequately mitigated in the structuring of the transaction, the risk may be identified in the risk factors section of the prospectus in respect of the securities.

The right of a floating charge holder to appoint an administrative receiver of the SPV is of particular interest to the rating agencies. An administrative receiver has the power, when appointed, to manage a company’s affairs in the interests of secured creditors, rather than creditors as a whole. The Insolvency Act 1986 (as amended) provides that the right to appoint an administrative receiver is retained for certain types of security that form part of a capital markets arrangement that broadly involves both:

- Indebtedness of at least GB£50 million (about US$82.2 million).
- The issue of a capital markets investment.

Tax issues

26. What tax issues arise in securitisations in your jurisdiction? In particular:

- What transfer taxes may apply to the transfer of the receivables? Please give the applicable tax rates and explain how transfer taxes are usually dealt with.
- Is withholding tax payable in certain circumstances? Please give the applicable tax rates and explain how withholding taxes are usually dealt with.
- Are there any other tax issues that apply to securitisations in your jurisdiction?

Transfer tax

Stamp duty, at 0.5% of the consideration, is chargeable on a document effecting a transfer of stocks or marketable securities. Stamp duty reserve tax, also at 0.5% of the consideration, is payable on an agreement for the sale of chargeable securities. Chargeable securities include loan capital issued by a UK company or held on a UK register, or paired with securities that are so issued or held.

There is an exemption from these charges where the transfer is of loan capital. This exemption does not apply where, at the time of execution of the transfer instrument, the loan capital either:

- Carries a right to convert into, or acquire, shares or other securities (including loan capital of the same description).
- Has other characteristics of equity (such as a right to interest exceeding a commercial rate or dependent on results).

Stamp duty and stamp duty reserve tax are generally payable by the buyer. Stamp duty is payable to HM Revenue & Customs at the time of the transfer instrument’s presentation for stamping. Presentation for stamping must occur within 30 days of execution (if executed in the UK) to avoid penalties. Stamp duty reserve tax becomes chargeable on the day the agreement for sale is made or, if the agreement is conditional, the day the condition is satisfied.
Withholding tax
Withholding tax on loan receivables is payable on interest arising in the UK where the payment is made either:

> To a person not resident for tax purposes in the UK.

> By a corporate borrower (or a partnership which includes a corporate borrower) other than a “bank” making payments of interest in the ordinary course of its business.

There is an exception from the duty to deduct withholding tax where the borrower is a company (or a partnership which includes a corporate partner) and, broadly, it believes its recipient to be within the charge to UK corporation tax.

Subject to any claims for set-off, this tax is payable by the borrower on the date by which the tax return on which the relevant payment must be included is required to be delivered.

There is also withholding tax on rent receivables payable to a non-resident landlord, in certain circumstances. There is generally no withholding tax on trade or lease receivables.

Value added tax (VAT)
VAT is chargeable at 15% from 1 December 2008 to 31 December 2009. It will then revert to the previous rate of 17.5% on supplies of goods or services made in the UK by taxable persons in the course of their business (unless the supplies are exempt, zero-rated or payable at a reduced rate).

The issue or transfer of loan receivables from a person who “belongs” in the UK is exempt for VAT purposes. The concept of “belonging” is complex and involves considering, among other things, the location of the business, whether the business has foreign branches, and how and from which business entity services are supplied.

Where a person “belonging” in the UK receives a supply of banking, financial, insurance, consultancy, legal, accounting and other similar services from a person who “belongs” in a country other than the UK, both:

> The supply is treated as being made in the UK.

> The person who “belongs” in the UK is liable to account for the applicable VAT.

Securitisation companies tax
The Taxation of Securitisation Companies Regulations have now been introduced to provide a permanent tax regime for securitisation companies.

A securitisation company (as defined in the regulations) is taxed on its "retained profit" rather than on the profit shown in its accounts.

The regulations apply to any securitisation company for accounting periods beginning on or after 1 January 2007. If a company is a securitisation company before the commencement date of the regulations, it must elect into the regime to be within its scope. Without this election, the company will continue to be taxed according to "unfrozen" UK GAAP.

Synthetic securitisations
Synthetic transactions are possible. The originator can transfer the risk of ownership of assets through a variety of structures, of which credit default swaps (CDSs) are commonly used. Credit protection structures may be funded by the issuance of securities by the credit protection provider, collateralised by other investments.

Synthetic transactions are commonly used where a regulated originator wishes, or is contractually required, to retain the ownership of assets, but wishes to reduce or eliminate the regulatory capital risk weighting assigned to these assets.
Other securitisation structures

28. Which of the various structures, set out in the Model Guide or otherwise, are commonly used in your jurisdiction?

All of the various structures set out in the Model Guide may be used (see Model Guide, Other securitisation structures). There is also likely to be variation on a case-by-case basis for more sophisticated transactions (such as CDOs, SIVs and synthetic structures).

Reform

29. Please summarise any reform proposals and state whether they are likely to come into force and, if so, when. For example, what structuring trends do you foresee and will they be driven mainly by regulatory changes, risk management, new credit rating methodology, economic necessity, or other factors?

Basel II revisions

On 13 July 2009, the Basel Committee finalised its package for revising the Basel II framework. The revisions include enhancements to:

> The regulatory capital treatment for trading book exposures.
> Strengthen Pillar 1 (minimum capital requirements, in addition to those covered under the trading book proposals), Pillar 2 (supervisory review process) and Pillar 3 (market discipline).

The first phase of amendments are already in force in the form of Directive 2009/111/EC on banks affiliated to central institutions, certain own funds items, large exposures, supervisory arrangements and crisis management, which:

> Requires originator and sponsor banks to retain at least 5% of the securitised products that they originate and sell, to give them a direct interest in assessing risk.
> Tightens definitions of core capital.
> Limits the amount of short-term exposure banks can have to one another.
> Will require setting up “colleges of supervisors” for each cross-border bank, so regulators can work more closely.

The second phase of proposed amendments are intended to be implemented by member states by 31 December 2010 and relate to:

> Capital requirements for re-securitisation.
> Disclosure for securitisation exposures.
> Capital requirements for trading book and remuneration policies and practices.

The third phase of amendments (the consultation for which closed in September 2009) comprise, among other things:

> Amendments on through-the-cycle expected loss provisioning.
> Specific incremental capital requirements for residential mortgages denominated in a foreign currency.

On 10 December 2009, the FSA issued a consultation paper setting out their proposals for implementing changes required as a result of the Basel Committee’s first and second phases of amendments. The consultation period closes on 10 March 2010. The rules must come into effect on 1 January 2011 and will lead to further legislation or regulations affecting securitisations.
Regulation (EC) No. 1060/2009 on credit rating agencies (Credit Rating Agencies Regulation)
The Credit Rating Agencies Regulation came into force on 7 December 2009 and is binding in all member states. It requires Prospectus Directive-compliant prospectuses to state whether or not ratings (if referenced in the prospectus) are issued by a credit rating agency established in the EC and registered under the Credit Rating Agencies Regulation. Credit rating agencies are also making numerous amendments to their criteria and methodologies for ABSs.

IAS39: Derecognition
The International Accounting Standards Board is aiming to replace, by the end of 2010, IAS39 with IFRS9 in a phased process. Part of the replacement will involve developing new requirements for derecognition (see Question 3).

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Areas of practice/expertise. Guy joined the firm in 1998 and made partnership in 2007. Guy’s practice covers a wide range of banking and financing work, including international capital markets, securitisations, structured finance and bank lending. He has advised originators, issuers and banks on a range of WBS, RMBS, CMBS and ABS securitisation structures, including in the context of the ECB and Bank of England repo arrangements, tender offers, buybacks and unwinds. He has also been involved in structuring regulated covered bonds in the UK. Since 2007, he has advised H.M. Treasury on the temporary public ownership and subsequent restructuring of Northern Rock, the administration of Icelandic banks Kaupthing Singer & Friedlander and Heritable, the sale of Bradford & Bingley’s retail deposit business to Abbey National plc and most recently in connection with the 2009 Asset-backed Securities Guarantee Scheme for RMBS and on certain aspects of the Banking Act 2009.

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