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STS Compliance and Ki

On 17 January 2018, the EU Regulation introduced a new regulatory framework for securitisation transactions. This was published in the Official Journal of the European Union. The regulation covers:

- » Due Diligence
- » Risk Retention
- » Transparency
- » Criteria for granting credit
- » A ban on re-securitisations
- » Requirements for SSPEs (Securitisation Special Purpose Entities)
- » Establishment of and procedures related to Securitisation Repositories
- » Framework for STS

The attached document highlights some of the key provisions of the regulation, as an aid to our current and future clients, along with, where applicable, an explanation of how Moody's can help address the applicable tasks. This document is not meant to be an exhaustive review of the regulation and Moody's recommends organisations review the regulations on their own.

Article	Item	Moody's Value Add
Article 3: Selling of Securitisation to retail Clients	<p>This article sets forth that the seller must perform a suitability test in accordance with Article 25(2) of Directive 2014/65/EU and communicates the outcome of the suitability test to the retail client.</p> <p>This article further covers the fact that the retail client must provide the seller with accurate information on its portfolio including any investments in securitisation instruments</p>	
Article 4: Requirements for SSPEs	Sets forth where SSPEs can be established	
Article 5: Due Diligence Requirements for Institutional Investors	<p>Among other things, this article establishes the key elements of due diligence that investors must perform prior to holding a securitisation. This includes verifying items such as: the fact that the Issuer has sound and well- defined criteria for "approving, amending, renewing, and financing" underlying exposures and that they have "effective systems in place to apply those criteria and processes"</p>	<p>This item, while having an onus on the Investor for verifying will require Issuers to have robust systems in place for various aspects of its business.</p> <p>Ki provides a controlled, auditable solution that will help Investors to gain confidence in the funding process and verify that the appropriate systems and controls are in place.</p>
Article 6: Risk Retention	<p>a. This article sets forth that, unless certain key conditions are met (e.g. guarantee by central bank, regional government, etc.) originators, sponsors or original lenders must hold a net interest of at least 5%</p> <p>b. Originators may not select assets that will likely have higher losses over the life of the deal than those that remain on balance sheet and where there is a situation where a "competent authority" finds evidence suggesting the contrary, the originator may be subject to sanctions</p>	<p>a. Ki provides the ability to calculate the valuation of the net interest held by the originator, sponsor or original lender using Moody's Analytics cash flow engine used to model over 10,000 deals.</p> <p>b. Ki ensures assets are randomly selected for inclusion in the securitisation and avoids any semblance of "cherry picking". A powerful funding optimization solver selects assets based on eligibility criteria, covenants and optimizing elements selected by the originator. The tool also allows users to compare the assets that remain on balance sheet with those selected for inclusion in the securitisation in a single step.</p>
Article 7: Transparency Requirements	<p>a. Originators, sponsors and SSPE must make available to "holders of a securitisation position, to the competent authorities...and upon request, to potential investors"</p> <p>I. Information on underlying exposures - quarterly</p> <p>II. Underlying documentation (prospectus, derivatives and guarantee agreements, etc.)</p> <p>III. In the case of STS, the STS notification</p> <p>IV. Quarterly investor reports (including information on events that would change the waterfall priority of payments)</p> <p>b. The above information must be made available via a "securitisation repository" or a website that includes:</p> <p>I. Proper controls</p> <p>II. Adequate protection and integrity of information received</p> <p>III. Historical record retention</p>	<p>a. Ki will provide the automated creation of investor reports and templates required ESMA submission. This includes support the following asset classes: Mortgages, Leases, Corporate Loans, Auto loans and leases, Consumer loans and Credit Cards Furthermore, Ki fully automates the general investor reporting requirements. While an organisation may have something in place this today, Ki provides a high level of control and auditability which will be critical to ensure STS compliance.</p> <p>b. Moody's Global ABS Portal provides an established mechanism for organisations post the information required and make available to investors</p>
Article 8: Ban on Re-securitisations	Unless specific authority is granted by a "competent authority" no securitisation may	

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	contain portions of existing securitisations (i.e. no re-securitisations)	
Article 9: Criteria for credit-granting	This article specifies that the originators, sponsors and original lenders shall treat those exposures to be securitised with the same "clearly established processes" for approving credits as well as renewing and/or refinancing them. It also specifies that the loan pool may not include any loan that was not verified by the lender.	Ki ensures that all exposures selected for inclusion in a pool are randomly selected. This helps ensure that there is no biased selection of assets. Furthermore, once assets are selected dynamic reporting is available to allow business users to review all aspects of the selected pool quickly and to the level of detail required. Ki allows for full automation of the funding process.
Articles 10 through 17	<p>Articles 10 – 17 define the general conditions and procedures for a "Securitisation Repository". This includes but is not limited to:</p> <ul style="list-style-type: none"> a. registering with ESMA, items that are required to be submitted and ESMA's requirement to develop applicable regulatory technical standards b. Notifications of the Securitisation Repository c. How ESMA goes about examining the application of a Securitisation Repository d. Powers of ESMA e. Terms for ESMA withdrawing the registration of a Securitisation Repository f. The fees to be charged to Securitisation Repositories g. The conditions for making data in the Securitisation Repositories available including to whom access shall be provided (ESMA, EBA, EIOPA, Investors, Potential Investors, etc.) 	
Articles 18 – 19	Articles 18-22 are focused on the requirements for STS designation for non-ABCP securitisation. If Securitisations meet all of the requirements below and ESMA has been notified, then the originator, sponsor or SSPE may use the designation "STS"	
Article 20: Simplicity	<ul style="list-style-type: none"> a. There must be a true sale of the underlying exposures and the title to the SSPE shall not be subject to any "severe claw back provisions" b. Sellers must represent and warrant that the underlying exposures included in the securitisation are not already encumbered c. The pool must consist of underlying exposures that meet "clear and documented eligibility criteria" which also includes no active portfolio management (other than for breaches or reps and warranties which would result in removal from the pool) d. If there are exposures transferred to the pool after closing then they must meet the same eligibility criteria as the original pool e. There must be homogeneity in terms of the underlying exposures (asset types, contractual credit-risk, prepayment characteristics). f. The exposures must contain obligations that are contractually binding and can be enforced. g. There must be defined periodic payment streams on the underlying exposures 	<ul style="list-style-type: none"> a. Ki prevents assets from being dual-encumbered at all stages of the pooling process. b. Ki allows Issuers to have a repository of all the eligibility criteria used in selecting assets that will be part of a securitisation c. Ki has functionality to allow users to automatically provide the same eligibility criteria to potential new assets as those used during the initial establishment of the pool d. Ki not only automatically selects assets on a random basis and according to specific compliance rules but also provides simplified reporting and analysis to help Issuers ensure that there is homogeneity with the underlying exposure pool e. Ki includes the ability to systematically exclude a loan based upon the type of payment stream as well as other user-defined parameters. f. Ki selects assets for inclusion in a pool based upon specific exclusion criteria and compliance rules and do so in a randomized manner.

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	<ul style="list-style-type: none"> h. There must not be a securitisation position as an underlying exposure i. Exposures must be originated in the same manner and the same methodologies as those exposures on the originators balance sheet. j. There must not be any exposures where information has not been verified by the lender k. The originator must have expertise in originating assets of the kind similar to those that are securitised l. There must be a transfer of the assets to the SSPE after selection without any "undue delay" m. There may not be any exposures where the debtor is insolvent or, at the time of origination was on a public registry of individuals with adverse credit history n. There must have been at least one payment made on the exposure at the time of transfer to the SSPE o. The credit scores of the underlying exposures must not be shown to be lower (i.e. have a higher risk of default) than those exposures which are not securitised. 	<p>Analysis tools within the applications make it easy for users to compare the resulting selected asset pool with those loans remaining on the balance sheet. Reports are also available to archive results for audit purposes.</p> <ul style="list-style-type: none"> g. Ki supports the ability to provide specific exclusion criteria and store the fact that they were utilized in the selecting the pools h. Please see "j" above i. Please see "j" above j. Ki allows users to target pools with specific weighted average credit scores. The tools allow business users to calculate the credit scores of the assets on balance sheet before and after selecting a new pool and comparing them to ensure adherence with this requirement.

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<p>Article 21: Standardisation</p>	<ul style="list-style-type: none"> a. The risk retention requirements established in Article 6 must be adhered to by the originator, sponsor or original lender b. SSPEs are not allowed to enter into any type of derivatives except for those related to hedging interest rate or currency risk. Further, the pool may not include any derivatives contracts c. Interest rate calculations on the assets or liabilities must not be complex and have to reference only commonly used market indices d. Organisations must adhere to standards related to what happens upon an "enforcement or acceleration" notice including – not keeping more cash in the SSPE than is necessary, paying the note holders sequentially based on seniority and not having any auto liquidation provisions of the underlying assets at market value e. Triggers must be in place and have a pre-determined threshold whenever there is a waterfall with non-sequential payment priorities. These triggers, if hit, would cause a change to sequential payout as set forth above f. For any revolving securitisations, the deal documents must specify early amortisation events or triggers to end the revolving period for a number of items (credit quality deterioration, insolvency of the originator or servicer, lowering of the value of underlying exposures held by the SSPE, inability to generate a certain amount of new exposures that meet the pre-determined credit requirements) g. The transactions documents must have clear terms setting forth the responsibilities of the trustee and servicer along with specific processes for replacing the servicer, derivative counterparty, liquidity provider or account bank in the case of insolvency h. Any servicer used must be one with expertise in the applicable underlying exposures i. The transaction documents must have clear information around addressing things such as delinquencies and defaults of debtors, losses, charge-offs and 	<ul style="list-style-type: none"> a. Ki supports the ability to set up the securitisation deal model and value the owned interest in the transaction b. Ki provides a controlled, auditable waterfall capability which allow organisations to establish, audit and monitor all structural components including triggers, early amortisation events, etc. The system will automatically divert cash, adjust the waterfall, change from non- sequential to sequential, etc. in an automated fashion. This eliminates the risk of having spreadsheets or other tools which require manual intervention. These types of "switches" in the manner in which the waterfall works are automatically triggered based upon asset performance parameters as defined in the transaction documents c. Please see above d. Please see above
<p>Article 22: Transparency</p>	<ul style="list-style-type: none"> a. Originators and sponsors are required to provide static pool and historical information (a minimum of 5 years) related to defaults and delinquencies. This information must be made available prior to pricing and be on "substantially similar" exposures to those that are being securitised. b. Sample data from the underlying exposures must be externally verified and deemed to be "accurate" by an "appropriate and independent" third party c. Prior to pricing and on an ongoing basis, a liability cash flow model must be made available to investors and potential investors (upon request) d. For auto loans and leases and residential mortgages information on the "environmental 	<ul style="list-style-type: none"> a. Moody's platform stores multiple years of history and automates the creation of historical/static pool reports. Users are able to run dynamic funding scenarios and compare the historical performance of the selected pool with the assets which remain on balance sheet b. Moody's Global ABS Portal provides a mechanism for Issuers to share not only the data associated with their deals but also the liability side model.

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	<p>performance" of the assets must be made available pursuant to Article 7.</p> <p>e. The information on the underlying exposures must be made available prior to pricing upon request and the remaining information must be available in draft form prior to closing and in final form within 15 days of closing. There is joint responsibility for this between the originator and the sponsor.</p>	
Articles 23 – 26: ABCP	Articles 23-26 cover the ABCP aspects of STS and are outside the scope of this document	
Article 27 - 37:	a. Articles 27 – 37 are outside the scope of this document.	

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