Certification in the Context of a Regulatory Framework for Securitisation

PCS

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Introduction

Following a number of consultations and position papers in 2014 and 2015, it is clear that the current direction of travel within Europe, when it comes to securitisation, is towards introducing a definition of simple, transparent and standardised securitisations. These securitisations would reflect the characteristics of European securitisations in the traditional asset classes that performed so well during the financial and economic crisis.

Once a definition of simple, transparent and standardised securitisations ("STS securitisations") is crafted, it seems equally clear that the intention is to use to craft a bifurcated regulatory framework in which these safer products could be subject to prudential regulation more appropriate to their inherent characteristics. The regulatory treatment of securitisations that did not meet the STS criteria, in turn, would reflect what we learnt during 2007 and 2008.

This European project for the regulation of securitisation has now also gained an international dimension with the consultation jointly published by the Basel Committee on Banking Supervision and IOSCO.

Having argued since our inception for such a bifurcated regulatory scheme, PCS warmly welcome the work that is being done in this direction both in Europe and globally.

We also welcome the attention being paid to the practical aspects of how such a regulatory scheme would be "operationalised". The Bank of England and the European Central Bank as well as the European Commission raised this issue in their respective consultative documents. This is a key issue if we wish to avoid the new regulatory scheme, explicitly designed to create a strong, deep but safe European securitisation market, from becoming a Phyrric victory: well designed in theory, but not capable of being operated in practice in a manner that would bring back investors into this funding instrument.

In this paper we will set up how we believe the new regulatory scheme could be "operationalised" effectively, cost efficiently and with the necessary prudential safeguards. We will look at the various alternatives, seek to identify the best and resolve the legitimate issues that could be raised around that choice.

This paper reprises a number of arguments that PCS has made in previous publications, particularly in our response to the Bank of England/ECB consultation and our paper on the issues surrounding self-attestation.

Characteristics and challenges of the new regulatory scheme

[A] Complex criteria and stark differences in outcome.

The current thinking regarding STS criteria create a regulatory dilemma. Assuming that the concept of STS securitisation enters the regulatory framework, it will be pulled in two different directions. On the one hand, the lessons of the crisis indicate that securitisations are, like many financial products, quite a complex instrument and that what went wrong with some of these instruments is not uni-dimensional. PCS' own analysis draws attention to four separate potential criticalities revealed by the crisis and probably a number of additional sine qua non conditions for robust securitisations.

This drives the definition of ‘qualifying securitisation’ towards a fairly complex set of conditions.

The various current proposals and existing rules for STS securitisations are indeed fairly complex. Solvency II’s existing definition contains 12 separate conditions that require to be met. When one bears in mind that some of these are multi-part criteria, the real number of conditions to be met is above twenty. The EBA’s generally sensible proposal runs to over fifty.

This complexity is not, in our view, the product of over-zealous regulators but a genuine reflection of the lessons that can be learned from the crisis of 2007 and 2008.

This complexity will also be made all the more difficult by the fact that the current proposed criteria are not all straightforward. It is a reality of all regulation that, notwithstanding the best intentions of the legislative and regulatory draftspeople, the rules when they meet the real world require interpretation. The more complex the rule, the more common the need for various interpretations. The more numerous the rules, the more interpretations are needed. PCS’ own label criteria were designed to be as simple, straightforward and binary as they could be made. Yet, our own experience with our label over three years revealed surprising needs for interpretations.

However, the more complex a regulatory scheme the harder it is for regulators to manage but also for the market to handle. The additional compliance burden can lead investors (or originators, depending on where the burden falls) to turn away from the product – especially if alternative investments can be found which are free of such burden.

A second characteristic of the likely new regulatory framework is that the difference in outcome between the treatment of an STS securitisation and one that does not meet the standard is likely to be very stark. The differences in capital requirements under Solvency II are very substantial. In other cases, such as the Liquidity Cover Ratios and the likely Money Market Funds rules, the difference is absolute: it is the difference between being allowed to hold the securitisation or not.

Considering the stark difference in behaviour between securitisations that met the STS criteria and those that did not, again this does not seem unfair. But the starkness of the difference in outcome indicates that a lot will turn, for investors, on the answers to fairly complex questions.

How can the complexities of the proposed STS criteria be streamlined so as to reduce the likelihood of confusion, regulatory risk and unnecessary costs?

[B] Need for new investors and due diligence

Any revival of the European securitisation market will require a substantial number of new investors. (The old, pre-2008 market was defined by the major involvement as investors of banks and creatures known as “structured investment vehicles” (SIVs). The point of the CMU project is to diminish the role of the former. The latter were liquidated in 2008 and will never – one hopes – be revived).

Such investors are unlikely to be attracted to a market where they run substantial regulatory risk but where such risk can only be mitigated through complex due diligence.

How does the new regulatory scheme not impose such costs and such risks as to deter any new investors from investing in the European economy through the securitisation market? How can the costs be reduced, for example by avoiding endless duplication?

[C] Multiple regulators

For the definition of STS securitisation to play its role in reviving a safe European market, it is generally acknowledged that it must be capable of being used by all types of regulated investors. Without a single definition one would end up with securitisation instruments that would be favourably treated by bank regulators but could not be purchased by money market funds or insurers; others that would be attractive to insurance companies but could not be invested in by funds or banks; etc…

However, as we have seen, complex definitions such as those proposed for STS securitisations require interpretations. The current thinking envisages this definition to be used in regulations that are overseen by a very diverse set of regulators. At the very least EIOPA (for Solvency II), the EBA (and its various component central banks, for CRR) and ESMA (for AIFMD). If the definition is also used, as would make sense, for central bank collateral rules, then every European central bank becomes an additional quasi-regulator.

We understand that it is not allowable, as a matter of law, for a regulator simply to relinquish its regulatory obligation to another regulator.

So, how does the STS definition maintain its universal applicability over time for all types of European investors under the strain of multiple regulatory interpretations and practices? How is the STS approach to be deployed effectively, from a cost and efficiency point of view, without multiple redundancies resulting from multiple regulators performing the exact same tasks?

[D] Appropriate allocation of responsibilities

One of the lessons of the crisis was that through the absence of sufficient information on securitisations and misplaced over-reliance on credit rating agencies, investors failed to understand the nature of the risks that they had taken on board.

Part of the STS criteria focus on transparency and are designed to ensure that appropriate information is always available to investors in STS securitisations. One of the key elements of any new regulatory scheme should be that investors are still required to understand what they have purchased and do the appropriate due dillignence.

Another key element of the new scheme should be that issuers accept the legal and moral responsibility that comes with issuance of STS securitisations. As originators of the securitised assets and structurers of the securitisation, it is proper that they take ownership of the key aspects of what they are selling to investors.

At the same time, in all parts of the capital markets, investors when doing their due diligence are allowed to rely on reliable and trustworthy parties and tools. Equally, the well known conflicts of interest that exists for issuers and credit rating agencies should lead us to be wary of over-reliance on their views.

So how does the STS regulatory framework provide for the relevant parties to take on the responsibilities that are properly theirs without disallowing them the use of legitimate tools and whilst minimizing issues arising from conflicts of interest?

Requirements for an effective operational reality

[A] Need for a functioning market

If one looks at the issues of the applicability of the STS securitisation criteria simply form the point of view of an investor's regulatory position – "can I purchase this?"/"what capital do I need to set aside for this purchase" – the complexity of the proposed definition is "only" a cost issue. The investor must be able to take an independent view of his or her investment and allocate risk and capital correctly based on this view. Once this is done, the regulations have fulfilled their purpose.

However, this approach fails to take into account that capital market investors invest in "markets". They rely on being able to sell their positions if they so wish. To do this, though, they cannot just rely on their own due diligence and regulatory conclusions. They must also have some confidence that other participants in the market, having done their own due diligence, will come to the same conclusions. Since, as we have seen, the proposed securitisation rules are complex, there is a great risk that other investors will come to different conclusions.

This is why, in addition to the risk that it will suffer loss from making a mistake in interpretation – resulting in a regulatory re-categorisation of its investment – the investor in STS securitisations runs the additional risk that of loss - notwithstanding having done what it considers to be an absolutely correct analysis - if other investors have done the analysis differently and reached different conclusions.

The risk of such differing approaches amongst investors is substantially increased in the case of the proposed securitisation regulatory framework since, as we have seen, the framework is intended to apply across different industries each regulated by different supervisory authorities.

Primary market

In the primary market, the absence of a common interpretation of the STS criteria as they apply to any given issuance would make it extremely difficult to price such bond as different investors would require different remunerations for the different levels of capital they believe they need to set aside. The result, of course, is that pricing and distribution would then most likely drift to the most conservative position (since the less conservative investors would happily take the higher coupon but the more conservative ones would not accept a lower one). The probable end result would be to nullify all the benefit of creating a regulatory space for STS securitisations.

Secondary market

The impact of a lack of certification would also likely affect substantially negatively the secondary liquidity. This is for two reasons: consistency and timing. The first, consistency, is merely a mirror of the problem sketched out above for the primary market. If different investors have different interpretations of the application of the definition to any given securitisation, any holder will need to worry about how deep the liquidity for such a 'STS securitisation' really is since he or she will not know how many of the potential investors in this securitisation share his or her interpretation of the regulatory definition.

The issue of timing is even more difficult as it would occur even if the analysis of whether a securitisation meets the STS standards were fairly straightforward. If an investor wishes to sell a securitisation, he or she will approach trading counterparties and ask them for a quote. Normally, a price is given and – if it is acceptable - the trade takes place. However, the differences between STS securitisations and others is stark. And so the price differential is going to be equally stark. In order to quote a price, the trading firm will need to know that it can unload the position to another investor at roughly the same price (minus the bid/offer spread). For this, the trader needs to know that likely purchasers will also consider the securitisation as an STS.

Few trading firms, if any, will be willing to take that substantial price risk on their own books. They will therefore only be willing to broker a sale – find another investor and put the seller and buyer in touch. The buyer, of course, will have to do his or her own due diligence as to whether the securitisation meets the criteria for STS status. This will take time.

So the problem, even for straightforward STS securitisations, is that every sale will be like that of a complex private placement, matching individual sellers with individual buyers and taking time. This is the anti- thesis of the deep, liquid market the authorities are hoping for.

Common currencies

This is why, in market situations such as these, where the value of an investment is not just determined by the analysis of the investor but by that of the investor community as a whole, reliance is placed on a "common currency" which is both public and shared. The most obvious example is the stock exchanges whose public prices for equities provide investors with a common understanding of the market's view. And this is why the European Union has sought to introduce a similar "common currency" in the bond markets with post-trade transparency rules administered by third party institutions (the CTPs).

Such "common currency", to be effective needs to meet a number of conditions:

1. Open: to be common, it must be available to all market participants.

2. Timely: as we have seen, to allow a workable primary market, it must be available at or before pricing on the STS securitisation.

3. Certain: because of the cost to investors of mistake in determination of STS status, it must be – in the absence of fraud or gross mistake – dispositive.

4. Trustworthy: because of the problems caused by misaligned interests (eg. US sub-prime or credit rating agencies), it must to as much as possible free of conflicts of interest.

5. Cost efficient: it must not impose a cost structure so burdensome as to prevent the market from fulfilling its role in funding the economy.

Possible “common currencies”

[A] Self-attestation

Under a “self-attestation” scheme, the originators would certify that the securitisations issued by them met the definition. This solution seems to PCS to go against the general direction of regulatory development that has sought, in the last few years, to diminish the moral hazard that results from conflicts of interest.

From a point of view of political realism, it would also seem that reliance on the banking institutions to police themselves in the area of securitisation could be a difficult message to expect to find broad acceptance, especially after the dent in confidence caused by the EURIBOR and the FX episodes.

We have set out in greater detail why we do not believe self-attestation would lead to any return of a strong but safe securitisation market in our paper “The illusory promise of self-attestation” (April 2015) and invite readers to refer to that paper for a full analysis.

[B] Third party certification

Under a third party certification regime, a third party would examine each securitisation issuance and determine whether it met the STS criteria for regulatory purposes. Those securitisation transactions that met the requirements would be entered on to a publicly available master list which would be dispositive of the securitisation’s status.

Such regime would need to meet the requirements of openness, timeliness, certainty, trustworthiness and cost efficiency set out above. If it did, it would provide the common currency needed for the growth of a strong, deep and liquid European securitisation market.

Certification agents: private or public?

There are two types of institutions that could provide this type of certification: regulators or private sector bodies.

On balance, PCS believes that private sector bodies – provided they can meet essential conditions – are best placed to perform this task. There are a number of reasons for this.

First, this type of certification on behalf of industry is an activitiy that is traditionally left to the private sector. Regulators issue rules and interpretations and supervise private sector bodies. They do not process large amounts of data, accept application forms, perform due diligence and maintain public data bases and liaise with issuers and investors as necessary.

Secondly, as we have seen, for this master list to be effective, the STS status of transactions needs to be publicly available at or before pricing. This is true irrespective of how many transactions are issued any month, any week, any day. This means that any certification agent must be able to demonstrate a scalable business model capable of dealing with any kind of volume (high or low). Without such capacity, the market could grind to a halt during times of high volume. It is our experience that public sector bodies, hemmed in justifiably by fiscal and budgetary disciplines, are not always best placed to achieve this type of scalability.

Thirdly, this activity should be paid for by the securitisation industry. If performed by a private sector (and, as we will see "not for profit") body, the costs will be kept transparent, accountable and low. Should the costs nevertheless rise to points where they threaten the viability of the market, market participants can set up a new alternative provider. This cannot be done with a regulatory body.

Fourthly, as we have seen, the STS regime will need to be overseen by a number of regulators that are not allowed to delegate to each other their responsibilities. By having a third party private sector certification agent habilitated by all the relevant regulatory authorities, the problem of overlapping jurisdictions is overcome.

Fifthly, a private sector certification agent accountable to a variety of regulators will need to have a mechanism to centralise interpretations of the rules. This resolves the issue examine earlier of how to maintain a single STS securitisation definition in the face of multiple regulatory regimes.

Please note, that even though we have written of a certification agent in the singular, it is not intended that a single body should perform that function. We would anticipate that rules be laid down as to the type of entity that could take on the certification agency role and regulatory authorities would then license one or more bodies to perform that function.

Possible issues with private sector certification agents

In the post credit agency/LIBOR/Forex world, PCS is not unaware that the idea of private sector bodies performing quasi regulatory roles in the financial sector is not without issues. We would like to deal with some of them by setting out what we would consider minimum requirements before any body be considered for the role of STS criteria certification agent.

[A] Alignment of interest

We have seen a number of serious problems occur with private sector bodies whose tasks contained a element of regulatory or quasi-regulatory function. The credit rating agencies and the banks in their role in setting LIBOR or forex rates or originators of US sub-prime mortgages.

In all those cases, the problems were traced to the effect of conflicts of interest: the bodies concerned had a financial interest in the way in which they performed these functions.

Not for profit

Although rules were, in some cases such as the rating agencies, introduced to provide for the proper management of these conflicts, we believe that the safest route is always to eliminate the conflict altogether.

This is why we believe that certification bodies should be not for profit bodies. We also believe that the definition of "not for profit" should be very strict and should not allow for what are effectively equity type returns to be extracted from the relevant certification agent through the means of bonuses or excessive loan repayment. In other words, any certification agent must be a genuine not for profit.

In addition, and to reinforce the absence of conflict, additional provisions should be introduced as requirements for potential certification agents.

Codes of conduct

There should be codes of conduct for staff, similar to those that apply to registered Credit Rating Agencies in Europe. These should ensure that there is no linkage between compensation and certification volumes. They should also prohibit the ownership of shares or securities by staff in any entity whose securitisations are certified.

Governance

The governance of potential certification agents should ensure the independence of management.

The composition of the board should be such that there is no majority representing entities whose securitisations are being certified. There should be a minimum of two independent board members whose role is to ensure the integrity of operations of the certification agent. Also, there should be representatives of investors or investor bodies on the board.

[B] Costs

The certification agent would meet its costs by charging issuers who seek to confirm the STS status of their securitisations. However, the certification agent being a not for profit body should not only eliminate a major source of conflict of interest, but should also ensure that costs are kept to the minimum necessary to run the framework efficiently.

In order to ensure that industry provides an economic oversight of the certification agent's activities, it would be a requirement that the accounts of the agent be published at quarterly intervals and be the subject of an independent audit each year. This should ensure that costs only rise when justified.

[C] No private rule making

The purpose of the certification agent is not to define STS securitisations but to certify existing norms defined by the legislator and the regulators.

One of the most problematic aspects of the reliance by regulators on rating agencies is that this is a form of "private legislation". When the agencies change their criteria, in effect, they change the regulatory treatment of certain companies, nations or securities. Yet these changes are made internally by private, for profit companies: they are a form of private sector rule making.

The proposal for private sector certification agents within the STS securitisation framework would not provide for any such type of rule making.

This means that the framework would need to provide for a feedback mechanism should the certification agent encounter an ambiguity in the rules or a new set of circumstances where the application of the rules was uncertain. Any interpretation of the STS criteria would need to be provided by the regulatory authorities, not the certification agent.

[D] Regulatory supervision

As the certification agent performs a role within a regulatory function, it is right that it should do so under regulatory supervision.

First, the certification agent's status, within the STS framework, would be provided by the regulators. They should also have the right to remove that status should they determine for whatever reason that the agent cannot perform its tasks correctly.

To be able to oversee the certification agent's work, the relevant regulators must have full access, at any time, to all the operations of the agent. It must be able to speak to any member of the agent's staff or management. It must be able to peruse any file and check any financial transaction made by the certification agent.

To the extent that the certification agent acts through third parties, the regulators would have sight of all the relevant contracts with any such third parties.

We are agnostic and leave it to the regulators whether they would feel that they need to have members on the board of certification agents.

There are two ways in which the regulatory scheme could work. The certification bodies could be, by legislation, subject to regulation ie be "regulated entities" subject to oversight and penalties by regulatory bodies. Alternatively, the certification agent would not be "regulated entities" but would be defined in the legislation as bodies that had received the status of "STS securitisation certification agent". Such status would, in turn, depend on the agent meeting all the regulatory requirements. If the regulator, at any point, determined the agent was not meeting the requirements, the status could be removed.

The creation of a full "regulated entity" status and the implementation of such formal oversight being more time consuming from a legislative and regulatory point of view, PCS strongly recommends the latter approach. The legislation could provide a 24 month review clause. Should the regulatory authorities determine that they needed the certification agent to be a fully regulated entity, the necessary changes to the legislation could be made at the review date.

How would it work in practice?

PCS has quite extensive experience, through its label, with certifying the structural integrity of securitisation transactions. This section is therefore based on our work and the issues we have encountered.

[A] The certification agent

The certification agent would be set up within the European Union as a not for profit body under relevant legislation.

The body would then apply to the relevant regulatory bodies for status of "STS certification agent". Such status would need to be created within the STS securitisation legislation. Would each regulator with STS securitisation regulation oversight be required to license the certification agent? PCS would recommend that such task be delegated by the legislation to a single regulator.

The single regulator would check compliance by the putative certification agent with all the rules and, if these were met, would grant certification agency status. This would be published on a publicly available list.

[B] Certification

A week or more before a securitisation issue is priced, the originator would file a certification request with a licensed certification agent.

That request would be accompanied by all the supporting documentation necessary for the transactions' STS status to be verified and a "verification checklist".

What supporting documentation would be required would ultimately depend on the actual STS securitisation criteria set out in the legislation. The verification checklist would contain each criteria and a reference to a document (and where in that document) which evidenced this criteria being met.

Amongst the documents we would anticipate might be provided would be:

- the prospectus;
- a legally binding statement by the originator;
- a legal opinion;
- a third party audit of the pool;
- a statement by a data firm and a modeling firm that the originator had entered into the relevant disclosure contracts.

The certification agent, either itself or through third parties, would verify that the criteria were met.

If the agent determined that they were, it would issue a certificate to the issuer and would enter the information on a master list of all STS securitisations. It would also, to the extent it was legally possible, file all the documents and the verification list so that any investor or potential investor could do its own checking.

The issuer would pay a fixed fee for each issue for which it sought certification and an ongoing small annual fee thereafter. The quantum of that fee would be set so as to meet the operating costs of the not for profit certification agent.

[C] Interpretations

Should the certification agent come across a point that was ambiguous and it determined that an STS criterion required to be interpreted, it would communicate this immediately to a regulatory committee.

This committee would be composed of regulatory staff and would need to issue a determination. PCS would strongly urge that the legislation (or delegated acts) setting up the STS securitisation framework clearly set a time frame for such interpretations.

Once the interpretation had been made, it would be published and binding on all certification agents.

[D] Ongoing certification

If some of the STS securitisation criteria were such that they needed to be met on an ongoing basis, rather than merely at the issue of the bonds, the certification agent would need to furnish such ongoing verification.

Questions that should be frequently asked

Earlier we had mentioned certain characteristics that a proper certification scheme would need to have and certain challenges that it would encounter. There are also a number of questions relating to such a scheme that we anticipate will be asked. We therefore anticipate some of these here.

[A] Is this not just an invitation for investors to over-rely on certification agents as they did on rating agencies before the crisis?

No. There is a fundamental difference between relying on a rating and relying on the certification of a regulatory rule: judgment. A rating is a subjective assessment of the credit quality of a debt. Assessing the credit quality of what you are investing in is the key requirement of an investor. If an investor relies on a rating, it is substituting the judgment of a third party for its own.

The STS criteria are not subjective. They are objective criteria set out by the legislator that describe the structure of a given securitisation. When the agent certifies a securitisation as meeting the STS criteria, it is verifying the fact. It is not making a subjective call.

Therefore, relying on third party verification of objective fact is not an abdication by the investor of its obligations but the use of a verification tool. It is more like using a calculator. It is no different from all the other tools we accept investors are entitled to use when seeking to understand what it is considering to purchase: the investor can look at the price of a security quoted by a stock exchange or a CTP, without being required to verify it independently; the investor can rely on the audited accounts of a company without being required to verify the P&L number independently; the investor can buy a computer model of a securitisation waterfall to understand how cash flows work in certain scenario's without verifying them independently; an investor can use publicly available data on inflation without verifying it independently.

In other words, a certification from an agent of the STS criteria is an objective tool. It would be costly and wasteful to require each investor to do independently this verification when it can be centralised.

[B] Is the licensing of a private third party certification agent not an incredibly novel and therefore risky new departure? Should we be willing to experiment in this way with something that could cause great damage if it goes wrong?

Actually, the licencing of a private third party certification agent whose job is to verify that a product is in conformity with European regulation far from being novel is the norm.

European Union law uses such agents in over thirty different industries. Such bodies are called "notified bodies" and a list of them can be found on the EU web site. They are used in precisely the circumstances which are contemplated in the STS securitisation framework: manufacturers (here securitisation originators) who are required to conform to specific quality criteria but where the market (consumers or businesses) need to relying on these criteria but where their checking individually by each purchaser would be incredibly expensive and the manufacturers have a conflict of interest which makes self-attestation unwelcome. In fact, notified bodies are most usually utilized in industries where the risk of something going wrong can lead to dire consequences: eg food safety, medical equipment, medicines, safety equipment and nuclear power stations.

As with the approach proposed here by PCS, "notified body" status is set out in the primary legislation that creates the norms that producers must meet. There is a regulatory body charged with licensing the notified bodies and supervising their quality.

[C] Should investors not be required to understand what they are purchasing and perform necessary due diligence?

Yes. But as we have stated above, in performing their due diligence investors are entitled to rely on objective tools. Whether a securitisation meets the STS criteria is an objective fact that investors need to ascertain in the way they need to ascertain the nature of the securitised assets. But they are also entitled to ascertain these things based on information provided by trustworthy sources.

The certification agent being a not-for-profit licensed entity is such a source of objective data.

Also, STS criteria do not provide any information on the absolute credit quality of a securitisation. These criteria very explicitly only speak to the structural integrity of the securitisation. Therefore, it would be impossible for any investor to look only at the STS status of a securitisation in deciding its purchase. This would be like buying an equity based solely on the fact that it was listed without doing any enquiry on the company of which it was a share!

Therefore, the risk that the verification by a certification agent of the STS nature of a securitisation would lead an investor to suspend its due diligence is, to say the least, remote.

In addition, it is proposed that – as is currently done with the checklists for the PCS label – all the information that allows the certification to reach a conclusion on STS status should be available publicly. This would allow any investor to double check the work of the agent.

[D] Shouldn't issuers be liable for the quality of what they sell? Would a third party certifying the STS criteria not let them off the hook?

Yes, to the first and no, to the second.

Most, if not all, of the information provided to the third party certification agent is provided by the issuer[1]. That information should be certified. In fact, such certification should be part of the legislative requirements. Therefore, if a certification agent erroneously certifies a transaction as meeting the STS criteria because of incorrect information, the liability should and would remain with the issuer. This is similar to

[1] We are using the word "issuer" here slightly inaccurately since, in most securitsations, the "issuer" of the bonds is a special purpose vehicle. Technically, the entity we are speaking about should be called the "originator". However, this is a term of securitisation art and so we prefer to use the word "issuer" (as does much of the market) to mean the "originator".

audited accounts which remain the responsibility of the company being based, as they are, on company numbers.

Of course, there is always the remote possibility that an error is made by the certification agent. The possibility should be remote since the criteria are designed to be objective. In such case, the agent would have to accept liability. However, the possibility of such error would exist in *any* STS securitisation framework (as it exists in any regulatory or human endeavour) irrespective of the existence of an certification agent.

[E] **Doesn't the fact that the STS securitisation framework rely on these certification agencies create dangerous dependencies for the market? What would happen if an agent were to disappear?**

Such dependencies of course exist throughout all of finance: Clearstream, Euroclear, stock exchanges, commodity exchanges, auditors, the European Data Warehouse etc…

Here, however, the dependencies generate very limited risks.

First, the creation of one or more small not for profit institutions to replace a failing certification agent as a market utility requires very little time and not a lot of money. One would anticipate that market participants would therefore be able swiftly to jump into the breach.

Secondly, the fact that certification agents are single purpose not for profit bodies limits considerably the risk that they would encounter the kind of financial stresses that could occur in fully commercial enterprises.

Finally, the fact that such agents will be under regulatory oversight further limits the risks as the regulators would ensure that no such body was licensed unless it could demonstrate the technical and financial wherewithal to perform the task.

Conclusion

The best way to ensure that a STS securitisation framework can play its role in bringing back a strong and safe European securitisation market is to ensure that a publicly available master list of STS securitisations is available to all investors.

The best and most cost effective way to achieve this is to provide for third party private sector not for profit certification agents under appropriate regulatory supervision.

This can be done without undermining the obligations of issuers or investors and should ensure a robust regulatory framework as it already does in countless European industrial sectors.

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