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SHORT-TERM, IN-DEPTH

A GUIDE TO RECENT TRENDS IN COMMERCIAL PAPER AND ASSET-BACKED COMMERCIAL PAPER

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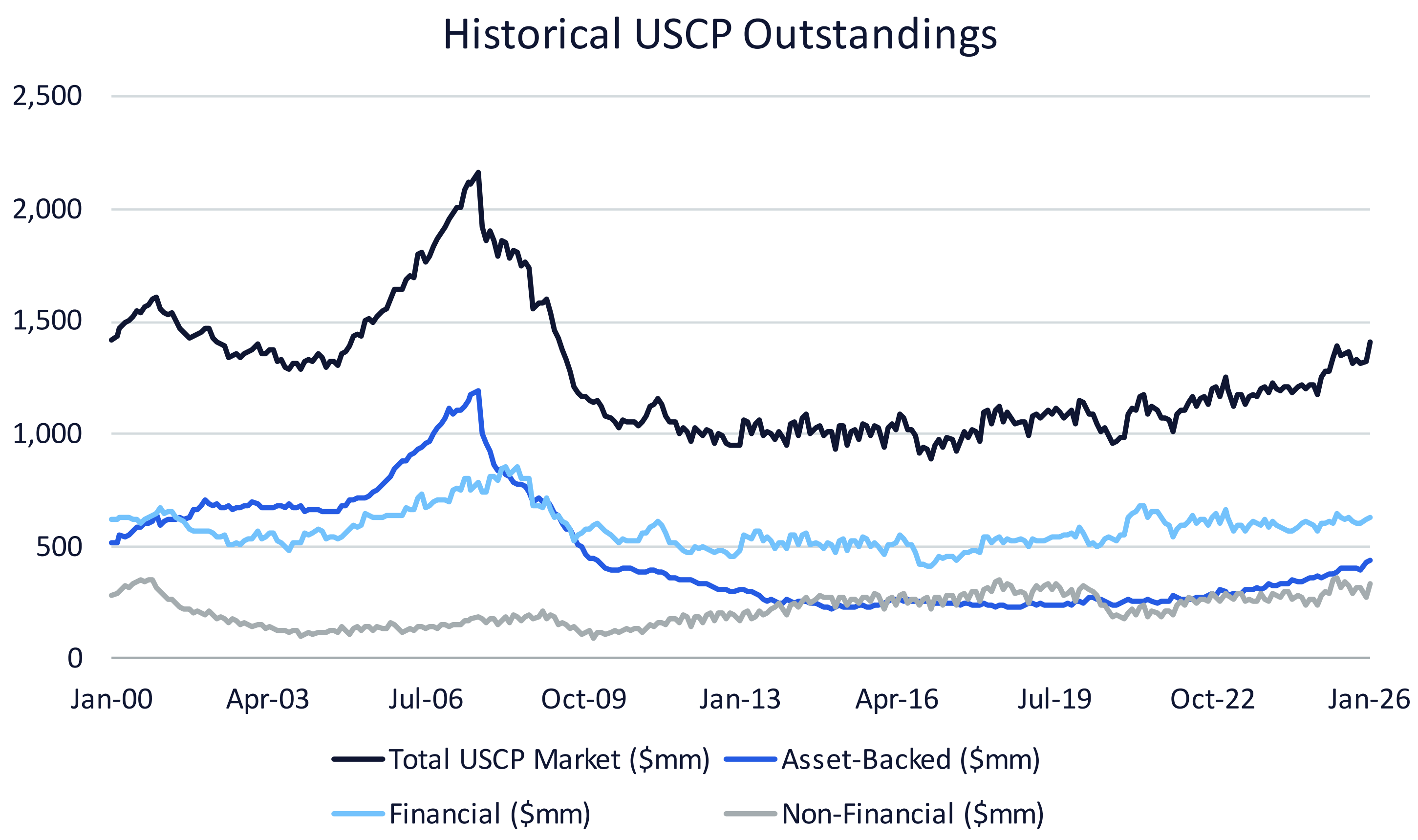
WHAT ARE WE GOING TO DISCUSS TODAY?

- Market Overview
- Short-Term Debt in the Middle East and Islamic Certificates of Deposit
- “Bolting on” ECP
- Regulatory Developments
- Digitalization
- Summing up

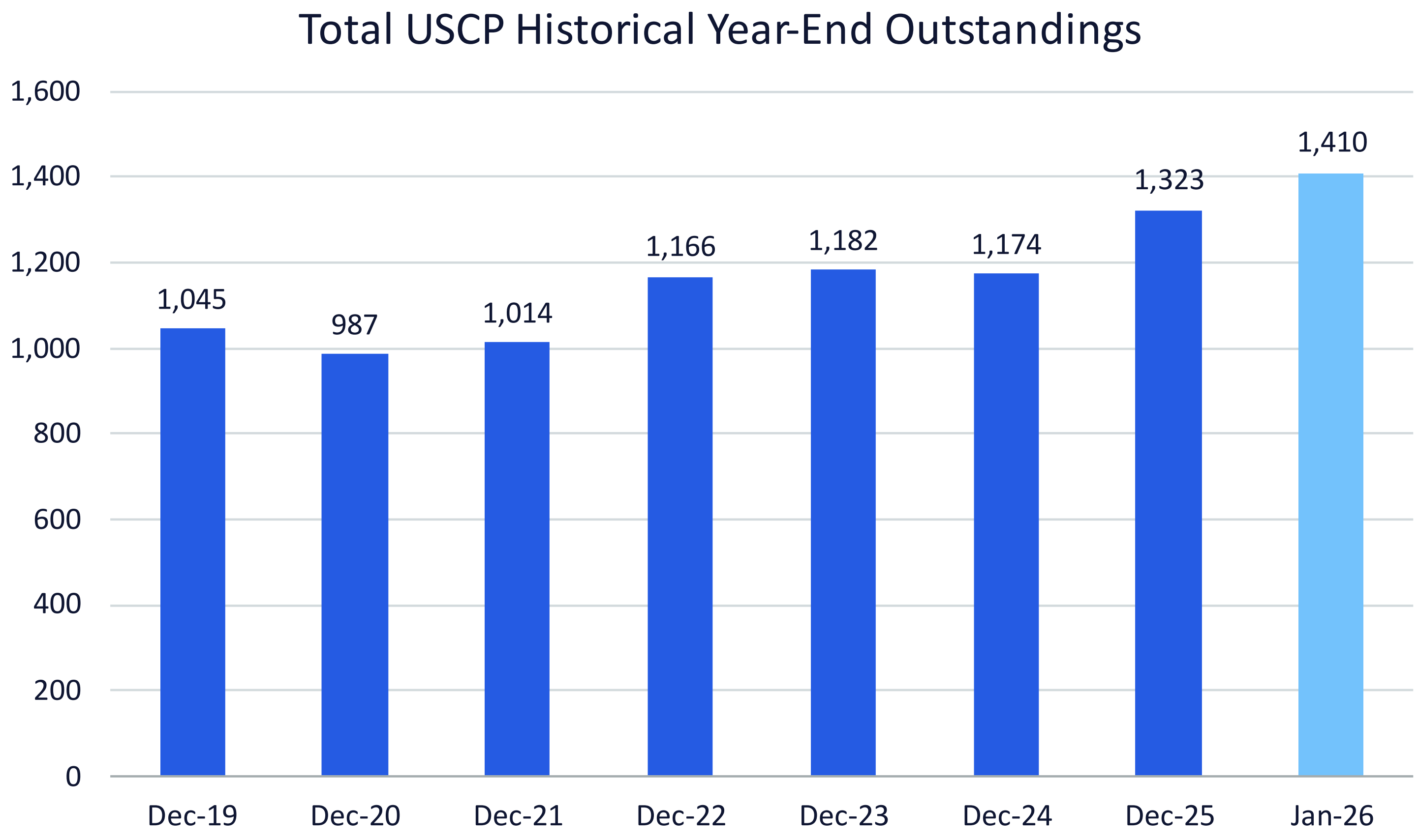
MARKET OVERVIEW

MARKET OVERVIEW - USCP



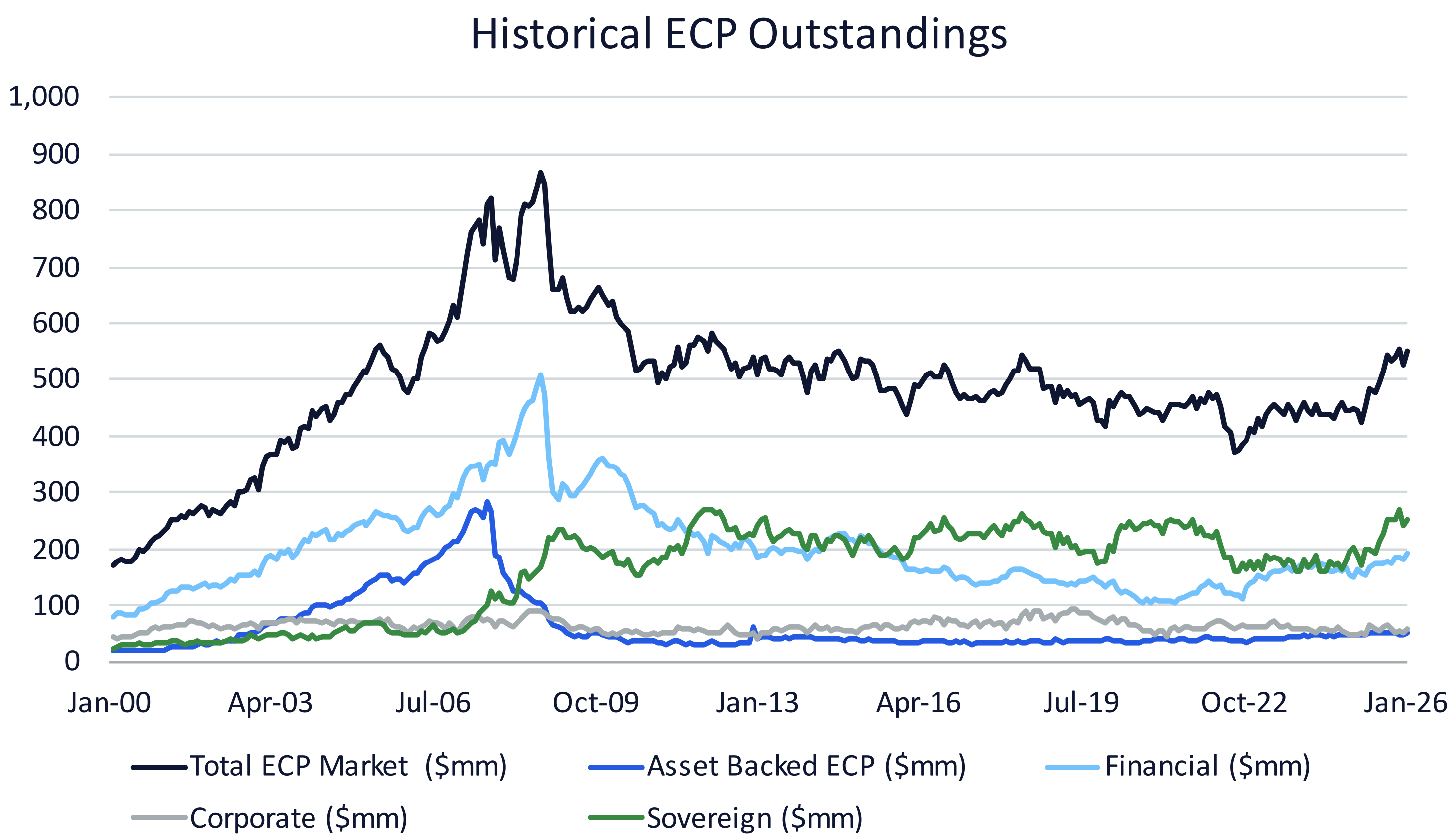
Source: Citi

MARKET OVERVIEW - USCP



Source: Citi

MARKET OVERVIEW - ECP



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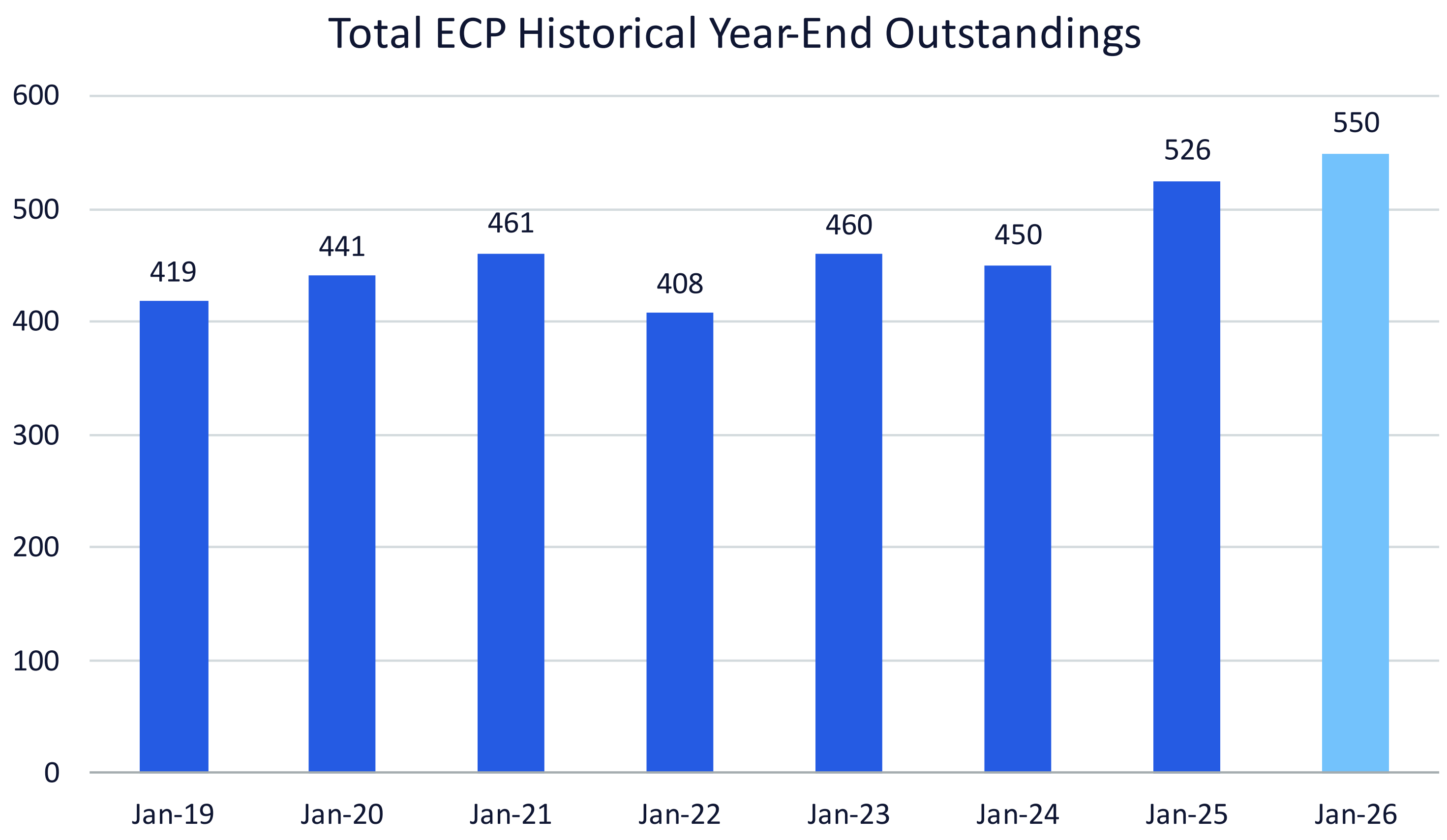
MARKET OVERVIEW - ECP



Source: Citi

SHORT-TERM DEBT IN THE MIDDLE EAST AND ISLAMIC CERTIFICATES OF DEPOSIT

SHORT-TERM DEBT IN THE MIDDLE EAST

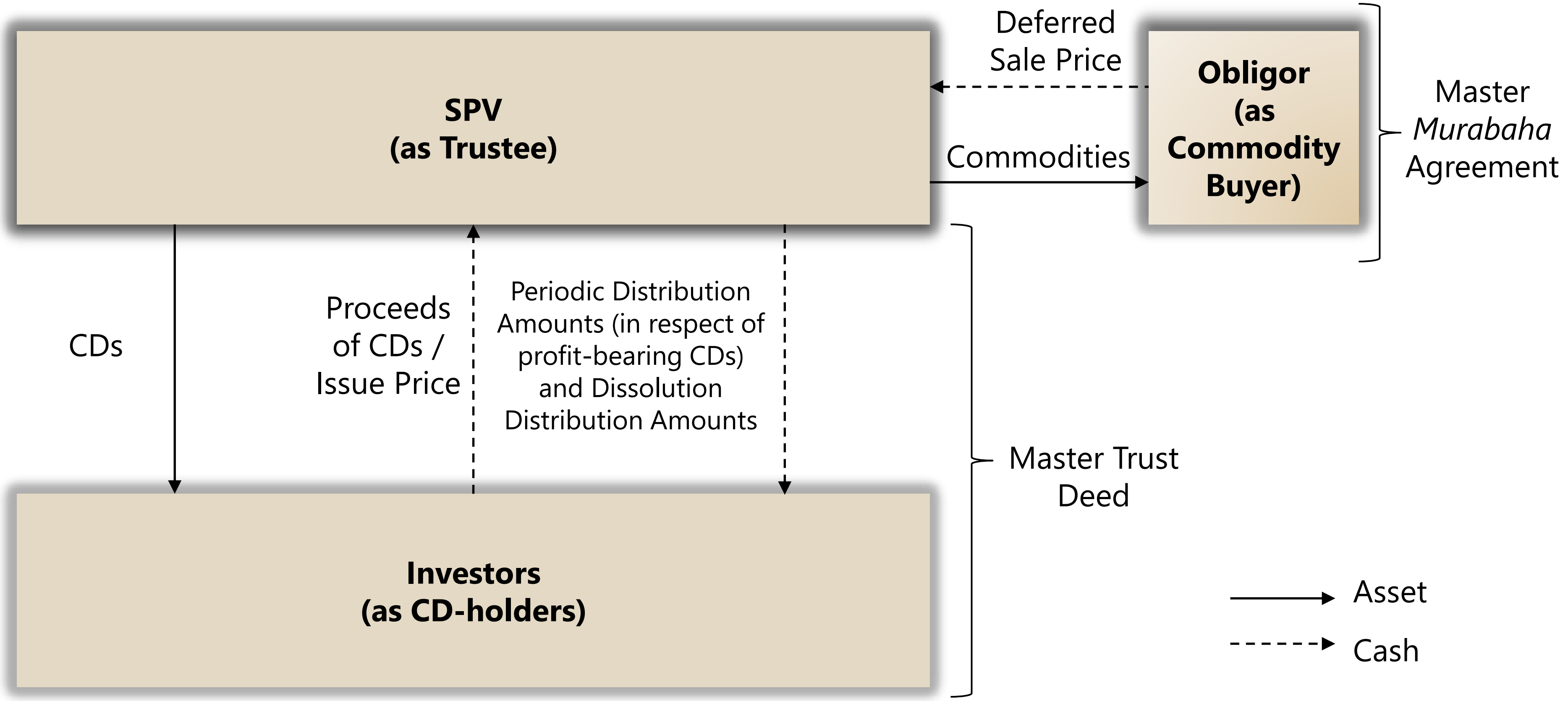
- We are seeing increased interest in short-term debt from the region – **Euro Commercial Paper, US Commercial Paper, Certificates of Deposit and Islamic Certificates of Deposit**
- Economic growth and broader capital markets maturation in the region creates the conditions for money market instruments like commercial paper and certificates to develop
- Commercial paper can provide a lower-cost alternative to traditional bank loans for meeting short-term funding needs
- For corporates and financial institutions with strong credit ratings, this can translate to savings compared to securing continuous bank credit facilities
- For Issuers, allows diversification of funding sources
- Commercial paper programmes are relatively simple to set up
- Commercial paper can be issued quickly, making it attractive for companies that need to raise funds on short notice
- The region's concentration of potential issuers (e.g. sovereign wealth funds, national oil companies and well-capitalised banks) provides a natural base of creditworthy potential issuers suited to this market
- Islamic CDs represent a relatively new form of short-term paper attracting attention

WHAT ARE *SHARI'A*-COMPLIANT CERTIFICATES OF DEPOSIT (*SHARI'A* CDS)

- *Shari'a* CDs are short-dated, wholesale-denominated funding instruments designed to give Islamic banks efficient access to money markets while adhering to *Shari'a* principles.
- Instead of conventional interest-bearing deposits, *Shari'a* CDs evidence an investor's undivided ownership interest in a pool of *Shari'a*-compliant trust assets.
- They may be issued on a discounted or fixed-profit basis, in multiple currencies and with tenors typically ranging from one day to three years.
- *Shari'a* CDs are generally offered outside the United States to professional and institutional investors.

HOW DO *SHARI'A* CDS WORK?

Set out below is a simplified structure diagram and description of the principal cash flows underlying a *Shari'a*-compliant certificate of deposit issuance using a commodity *murabaha* structure.



HOW DO *SHARI'A* CDS WORK?

- On each issuance, investors pay the issue price to a SPV trustee against the delivery of a *Shari'a* CD.
- The trustee applies the proceeds to purchase *Shari'a*-compliant commodities through its commodity agent and immediately sells those commodities to the obligor on a deferred basis under a *murabaha* contract.
- The obligor, as commodity buyer and obligor, agrees to pay the deferred sale price comprising principal plus a profit amount. Periodic distribution mechanics mirror the *murabaha* schedule: on each specified date, the obligor pays the relevant profit instalment into the transaction account to fund distributions under the *Shari'a* CD.
- On the scheduled dissolution date (or earlier upon a dissolution event), the obligor pays the outstanding deferred sale price to fund the redemption of the *Shari'a* CD at the dissolution distribution amount (principal plus any accrued but unpaid profit).
- Payments are administered by appointed agents and registrars and are documented under English-law master trust and *murabaha* frameworks.

HOW ARE *SHARI'A* CDS DIFFERENT FROM CONVENTIONAL CDS?

Feature	Conventional CDs	*Shari'a* CDs
Underlying economics	Interest-bearing deposit	Deferred sale price under a *murabaha* (profit, not interest)
Tradability	Freely tradeable subject to market practice	Not tradeable except in accordance with Shari'a principles of debt trading
Documentation	Information Memorandum, Bearer CD, Agency Agreement and Dealer Agreement	Information Memorandum, Registered CD, Agency Agreement, Master Trust Deed, Dealer Agreement, Master *Murabaha* Agreement, Commodity Broker Documents
Profit/yield basis	Fixed/floating interest or zero coupon	Fixed profit rate or discount
Execution timeline	Intraday	T+2

“BOLTING ON” ECP

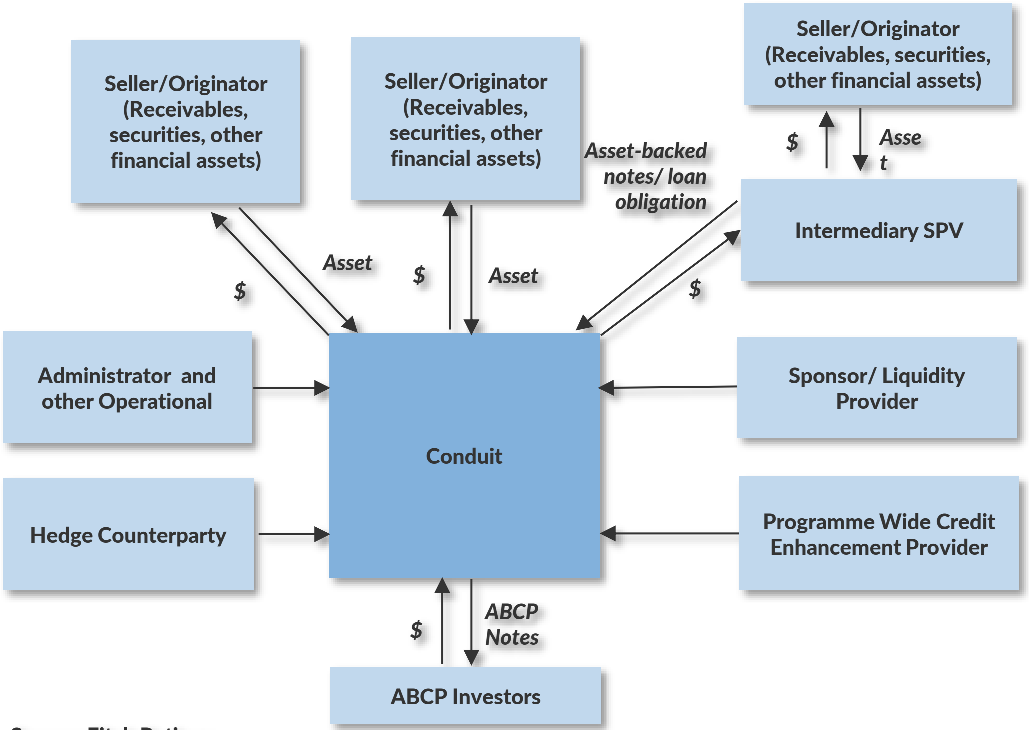
"BOLTING ON" ECP

We have seen increased interest in adding ECP capabilities to existing ABCP conduits

- Currency diversification
- Investor base diversification
- Whilst not as big as the USCP market; the ECP market is sizeable
- Increasing familiarity with the product
- Cost effective funding – particularly attractive in high-interest rate environment
- Cost effective v term debt
- Attractive rate proposition for investors v vanilla ECP debt
- Relatively simple addition to existing conduits

"BOLTING ON" ECP

- Jurisdiction of the Issuer SPV and any Purchaser SPV
- Tax considerations
- Different maturities between ECP and USCP (Up to 397 for USCP vs 364 or even 183 for ECP)
- SIFMA form documents (USCP) v ICMA form documents (ECP)
- A new set of ECP Issuer level documentation (ECP IM, Agency Agreement, Deed of Covenant, Dealer Agreement)
- USCP is issued in registered form; ECP is (typically) issued in bearer format
- Typically requires amendment to the asset level documentation and the USCP PPM
- Conisderation of Hedging Arrangements
- DTC v Euroclear and Clearstream
- Consideration of EU and UK securities regulation; in particular, the EU and UK Securitisation Regulation



Source: Fitch Ratings

EU/UK REGULATORY CONSIDERATIONS

EU/UK REGULATORY CONSIDERATIONS FOR COMMERCIAL PAPER

- **Prospectus regime:** CP is exempt from the requirements of the EU Prospectus Regulation and, in the UK, The Public Offers and Admission to Trading Regulations 2004 (but it is classified as a ‘financial instrument’ for the purposes of EU MiFID II, UK MiFIR and the FCA Handbook). CP is exempt because it is treated as a money market instrument with a maturity less that 12 months and therefore not a “transferable security”. The minimum denomination of CP is always higher than €100,000 which also means there is no obligation to publish a prospectus pursuant to EU and UK prospectus regime.
- **PRIIPS/Selling restrictions:** Market consensus is that Vanilla CP does not constitute a PRIIP and therefore it is not necessary to include the PRIIPs legend in the CP documentation. Investor base is not retail.
- **Product Governance:** Depending on whether the ECP issuer is a MiFID II firm or a FCA authorised firm (and therefore a “manufacturer”) or the relevant dealer considers itself to be a “distributor” and not a “manufacturer”, particular disclosure language will need to be inserted in the Information Memorandum and Dealer Agreement. Generally, underwriters do not consider themselves manufacturers for Vanilla CP.
- **FSMA Deposit Taking:** Where commercial paper is issued by issuers who are not authorised or exempt, the standard ICMA selling restrictions requires that the managers represent and agree that the commercial paper is only offered to investors whose ordinary activities involve them acquiring, holding, managing or disposing of investments. To fall within this exemption, it is also customary for commercial paper to have a minimum denomination of at least GBP100,000 (or equivalent in another currency).

EU / UK REGULATORY CONSIDERATIONS FOR ABCP

EU/UK Securitisation Regulation

- An ABCP transaction may often use the proceeds from the issuance of ABCP to obtain an interest in transactions that have tranched credit exposure and qualify as securitisations for EU/UK regulatory purposes.
- ABCP (and liquidity or asset purchase facilities) will therefore also typically be securitisation positions for the purpose of the EU/UK Securitisation Regulation.
- EU/UK Securitisation Regulation requires:
  - Initial and ongoing due diligence by EU/UK institutional investors in relation to a securitisation position
  - Risk retention of at least a 5% of net economic interest in the securitisation transaction
    - But fully supported ABCP programmes do not require risk retention at transaction level
  - Disclosure to investors, competent authorities and, on request, potential investors
    - Transaction summary
    - Monthly asset-level report and investor report (Annexes 11 & 13 of ESMA templates)
    - ‘Significant event' disclosure

EU / UK REGULATORY CONSIDERATIONS FOR ABCP (CONT'D)

EU / UK Securitisation Regulation

- STS - ACBP transactions or programmes which qualify as STS (simple, transparent and standardised) may result in reduced regulatory capital requirements or other regulatory benefits for bank holders of an exposure to the transaction/programme
  - STS criteria for ABCP transactions include requirements relating to:
    - Simplicity, including true sale and underwriting standards, homogeneity
    - Standardisation, including risk retention
    - Transparency, including provision of information to potential investors
    - Sponsor and sponsor support for the ABCP programme
- criteria for ABCP programmes to be STS require:
  - All underlying transactions to be STS (except that a maximum of 5 % of the aggregate amount of the exposures may temporarily be non-compliant a period of no more than six months)
  - Programme to be fully supported by the sponsor
  - Remaining weighted average life of the underlying exposures to not be more than two years
  - ABCP may not include call options, extension clauses or other clauses that have an effect on final maturity, where such options or clauses may be exercised at the discretion of the seller, sponsor or the conduit
- No resecuritisation at ABCP Transaction level - securitised exposures transferred by the seller to the conduit may not be resecuritisations.

EU MONEY MARKET FUNDS REGULATION – ELIGIBLE ABCP

- ABCP is eligible if (liquid and good credit quality) and "issued by an ABCP programme which:
  - Is fully ***supported*** by a regulated credit institution that covers all liquidity, credit and material dilution risks as well as ongoing transaction costs and ongoing programme wide costs related to this commercial paper if necessary to guarantee towards the investor the full payment of any amount under the asset back commercial paper;
  - is ***not a re-securitisation*** and the exposures underlying the securitisation at the level of each ABCP transaction do not include any securitisation position;
  - does ***not include synthetic securitisations*** as defined by [Art. 242(11) CRR]."
- Maturity limits for eligible ABCP:
  - Short term MMF: residual maturity or legal maturity at issuance is 397 days or less;
  - Standard MMF : legal maturity at issuance or residual maturity is 2 years or less and time remaining until next interest rate reset date is 397 days or less
  - (No limit on maturity of underlying assets, though earlier proposed)
- Diversification limits:
  - Money market funds may invest
    - Up to 20% of their assets in ABCP which is STS
    - Up to 15% of their assets in non- STS ABCP

UCITS VI - DECEMBER 2025 MARKET INTEGRATION PACKAGE

- Proposes amending the UCITS Directive (2009/65/EC) by:
  - raising the single-entity debt limit from 10% to 15% for securitisations that comply with the EU Securitisation Regulation (the Council of the EU has proposed to allow UCITS to acquire up to 50% of a single public securitisation issue).
  - streamlining cross-border marketing of UCITS and AIFs by moving rules into the Cross-Border Distribution Regulation (CBDR)
  - introducing mandatory liquidity management tools (such as redemption gates) which will apply to MMFs from 16 April 2026 to manage liquidity risks associated with holding short-term securitised paper.

DIGITALIZATION

DLT ISSUANCE – OUR RECENT EXPERIENCE

- Mayer Brown advised a consortium of financial entities led by Guggenheim Partners in developing the first tokenized asset-backed commercial paper issuance platform in the United States
- Tokenization brings potential greater efficiency to the CP market: reduced settlement risk, lower issuance costs, and decreased regulatory capital charges for financial institution sponsors
- Advisory scope included structuring, securities law, tax matters and tokenization infrastructure
- Ownership is recorded both in the issuer's books and records and on a public, blockchain-based distributed ledger using Ethereum (open-source, decentralized platform with smart contract functionality)
- Guggenheim has since expanded to working with Ripple, with a focus on the XRP Ledger due to market interest
- This was the first offering of tokenized commercial paper instruments in the United States, which has since been followed by other CP Programmes

DLT ISSUANCE – ADVANTAGES AND CHALLENGES

Advantages	Challenges
Shorter Settlement Cycles	Legal Certainty and Enforceability
Reduced Intermediaries	International Regulatory Patchwork
Lower Operational Cost	Higher Initial Cost
Improved Post Trade Processing	Cash Leg
Enhanced Transparency	Interoperability
Regulatory Reporting Efficiencies	Secondary Market Liquidity
Reduced Settlement and Counterparty Risk	Non-Standardised Documentation
Integration with Digital Cash	Cybersecurity/Key Management
Signals “innovation”	Investors may charge a premium

DLT ISSUANCE – STRUCTURING CONSIDERATIONS

- Which DLT platform to use?
- Form of Security – e.g. “Tokenised Security” v Native Issuance
- Governing Law – Differing governing laws will have differing considerations
- Supervisory Laws – e.g in the EU, the Prospectus Regulation, MiFID II, CSDR, MiCA
- Enforcement of Rights
- Tax Considerations
- Data Privacy
- Cost and Timing

SUMMING UP

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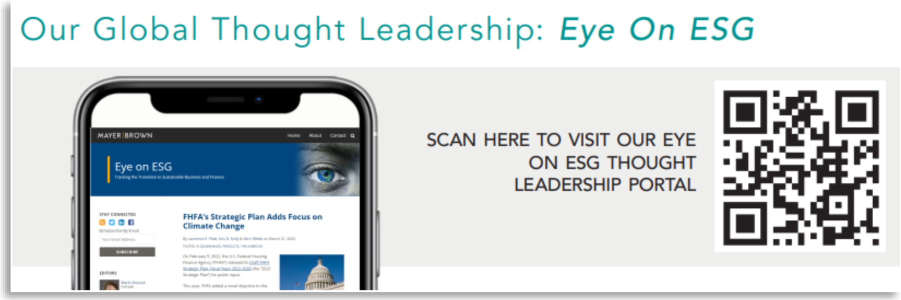
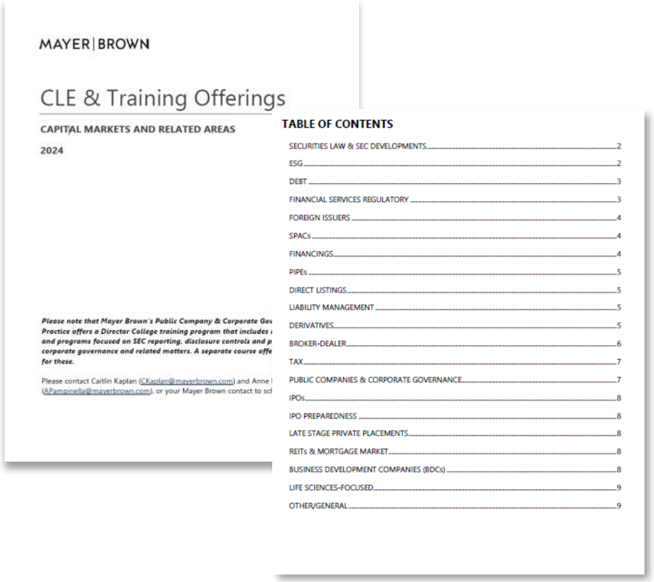
- **A range of reasons why we are seeing increased interest in the space** – cost effective funding, ease of use, range of structures and use cases
- **Growing Middle East interest** in short-term debt instruments driven by cost savings, funding diversification, and the region's strong credit profiles
- **Shari'a-compliant CDs** offer Islamic banks efficient money market access using commodity murabaha structures, with profit-based returns instead of interest
- **"Bolting on" ECP** to existing ABCP conduits provides currency and investor base diversification, cost-effective funding, and is a relatively straightforward addition to existing programmes
- A range of **Regulatory Developments** affecting the market
- **Tokenization/DLT issuance** offers shorter settlement cycles, reduced costs and enhanced transparency, though challenges remain around legal certainty, interoperability and regulatory fragmentation

A SELECTION OF OUR CAPITAL MARKETS RESOURCES

We offer our clients a range of value-add services including access our global capital markets blog, "**Free Writings and Perspectives**", our ESG blog, "**Eye on ESG**" and our compendium of capital markets pointers and explanations, "**What's the Deal**". We also provide clients our annual training offerings on a range of capital markets are related areas.





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CLE & Training Offerings

CAPITAL MARKETS AND RELATED AREAS

2024

Please note that Mayer Brown's Public Company & Corporate Gov
Practice offers a Director College training program that includes
and programs focused on SEC reporting, disclosure controls and p
corporate governance and related matters. A separate course offe
for these.

Please contact Caitlin Kaplan (CKaplan@mayerbrown.com) and Anne
(APampinella@mayerbrown.com), or your Mayer Brown contact to sc

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