

White Paper: Simplifying Market Practice in Wholesale Funding of Lending Platforms

Current Market Practices and Challenges

During the period between 2019 to 2022/2023 there was a significant increase in funding made available to lending platforms in the UK, driven, in part, by a near-zero interest rate environment.

However, as interest rates have risen, many business models have come under pressure, resulting in consolidation in the market. Our sense is that loan originators (in this paper, “originators”) are currently facing a particularly challenging phase, influenced by an uncertain socio-political landscape, persistently high interest rates, rapid technological advancement (especially in artificial intelligence), and access to funding. In addition, current market practices are often unnecessarily complex, leading to inefficiencies and increased costs. These factors collectively increase the pressure on the sector, making certainty of costs and deliverability increasingly important for originators.

While the sector has faced significant challenges, several positive developments have emerged since the pre-COVID period, contributing to a changing landscape. For example:

- **capital regulations** (both Basel and the Solvency regime) have evolved and there is increasing appetite from insurance companies, pension schemes, and challenger banks to fund loan assets;
- the **expansion of private credit** and alternative investments with a growing number of funds established to invest in assets before they become part of a public capital markets programme;
- **consolidation in the non-bank lender sector**, particularly where large independent originators have been acquired; this has left investors with fewer opportunities to deploy capital at scale;

- the **“new” interest rate environment** provides opportunities for non-bank lenders to use price as a differentiator and investors to place less reliance on public markets compared to the rate cycle post 2008; and
- **the emergence of forward flow structures** in recent years, driven by the following factors:
 - diversification of funding;
 - drive for simplified funding documents;
 - pressures on cost and speed; and
 - strategy, as these structures provide off-balance sheet funding without risk retention funding requirements.

There is **an inherent friction between the value proposition of fintechs and alternative lenders – speed of deployment of capital – and the often-protracted process of an originator securing its own wholesale funding line** which, depending on deal complexity, may have an execution period of more than two months. Further, if lawyers default to traditional and highly bespoke processes, this can exacerbate delays and complexity, contributing to unnecessarily lengthy negotiations, increased costs, and a misalignment with the principals’ commercial objectives.

The Case for Simplification

The lending sector has seen comparatively little innovation compared to other fintech verticals (e.g. payments).

With an increased interest in alternative or private credit, the sector has started a catch-up movement with digitalisation across the value chain: origination and underwriting, servicing, investor reporting, and funding. However, there are participants that consider that the sector remains stuck in habits and market standards which feel outdated, especially for funding where innovation could drive significant simplifications, automations, and efficiencies.

There is a compelling case for simplifying market practice in wholesale funding, with benefits for all stakeholders. For example:

- **reduced transaction costs:** standardisation of documents and processes would reduce legal and operational costs;
- **faster execution:** streamlined processes would enable quicker deployment of capital and certainty of funding, supporting the business models of originators in terms of reduced cost and time;
- **enhanced transparency:** consistent documentation, processes, and robust data would improve funder confidence; and
- **scalability:** simplified practices would facilitate the growth and expansion of lending platforms.

Framework for Simplification

Originator Institutionalisation and Operational Standardisation

Funders typically expect a certain standard of operational discipline and a level of standardisation and documentation of processes from originators.

Every originator, even within the same asset class, has certain specificities in terms of loan origination procedures, underwriting process, and servicing rules.

Originators' perceived (or actual) idiosyncrasies are one of the main reasons why funders require in depth operational and legal due diligence as part of a funding transaction; funders want to understand how an originator operates and the funding documentation needs to reflect the originator's operational processes and documentation.

The standardisation of operational documentation and definitions would facilitate and expedite the due diligence process and the transaction documentation drafting. For example, underwriting policies, servicing manuals, arrears management, and recovery processes could all follow a standard template adopted by originators in their market. This would be especially valuable in fragmented markets with many smaller originators, such as the UK bridging and development

sector. Further, such standardisation would also facilitate secondary transactions (e.g., back leverage, refinancing, and portfolio transfers) and contribute to overall market liquidity and access to funding for originators.

Originator Readiness for Funding

A significant amount of time and cost is incurred on all (or almost all) wholesale funding transactions addressing a recurring set of issues. For early-stage or rapidly scaling originators, the requirements of institutional funders can appear daunting and resource-intensive, particularly if they have scaled quickly.

An "originator readiness checklist" would standardise the information and documentation required by funders. This could be used at any stage; completed prior to early-stage meetings with funders or at term sheet stage.

By addressing common issues in advance (e.g., tax structuring, anti-money laundering compliance, and cash flow structures), the checklist would reduce transaction times and costs which are currently dealt with as part of the transaction execution process.

See the [Appendix](#) for a proposed checklist, with explanatory notes on the benefits of each section.

Standardisation of Transaction Documentation

Standardisation could be achieved by considering the following factors:

- **model agreements:** develop industry-standard templates for common funding structures (e.g., warehouse facilities, forward flow agreements, servicing agreements) or common terms in these deals (e.g., “Servicer Termination Events” and “Stop Purchase Events”). We would draw parallels to the work undertaken by International Swaps and Derivatives Association (“ISDA”) and the Loan Market Association (“LMA”) in developing standardised capital markets and lending documents;
- **transaction features:** similar to standard form ISDA and LMA documentation, standardised documents could include a list transaction features with the option to include or exclude them and to set their level. For example, a list of fees paid first in the waterfall, cash reserve (yes/no), cash reserve minimum/maximum amount, a list of cash flows from interest or principal collections, and principal deficiency ledger (yes/no); and
- **risk allocation:** standardise provisions relating to representations, warranties, covenants, and events of default.

Execution Process

The execution process could be simplified and made more predictable by considering the following key factors:

- **optimised term sheet review:** a service to conduct a high-level review of term sheets, providing a “score” linked to pricing. This would assist the parties identify the best starting point for instructing legal counsel or beginning to draft the transaction documents. We also suggest a pre-term sheet review stage where all commercial points and commercial red lines are discussed before entering into documentation stage. This could be aided by a pre-transaction checklist. Certain themes tend to recur during the legal phase which could be avoided if the parties had considered the commercial implications at term sheet stage (e.g., servicer / originator covenants, consumer duty and regulatory risk obligations, materiality thresholds, back up servicing provisions, wind down plans);

- **negotiation protocols:** establish a negotiation protocol at the outset of the deal. This could include, for example, setting maximum time limits for grace periods and applying materiality qualifiers to certain key clauses only. Commercial matters such as reporting requirements and eligibility criteria should be included as schedules to the legal documents to facilitate negotiation between principals directly; and
- **transaction protocols:** establish a transaction protocol at the outset of the deal. This could include, for example, how mark-ups and comments will be managed and exchanged so that outstanding points can be tracked and resolved efficiently. This would reduce the number of channels for comments and revisions as well as email traffic.

Operational Processes

While operational processes will be specific to transaction parties, we recommend considering the following:

- **operational “dry run”:** conducting a dry run of drawdown and reporting processes prior to closing to identify and resolve practical issues before they impact live transactions. It is, unfortunately, fairly common for transaction documents to require amendment before the first waterfall payment date, once operational issues become apparent; and
- **standardised reporting and data requirements:** while the appetite for standardised reporting may vary (particularly outside of securitisation-regulated deals), establishing baseline data and reporting standards would improve transparency and facilitate ongoing monitoring by funders.

The Opportunity of Digitalisation

Manual processes, lack of standardisation, and automation result in a variety of inefficiencies: exceptions handling, unreliable data, and handling errors contribute to increased operational costs, lack of transparency in the origination business, and difficulties in fund raising.

The digitalisation and automation of an originator's business would force a certain level of standardisation or, as a minimum, a requirement that their processes and exception handling are documented in detail and reviewed by funders. This would benefit originators directly through more data-led management, operational scalability, and cost-efficiencies. It would also benefit funding transactions which could leverage reliable and standardised data, automated workflows, and pre-agreed rules and decisioning.

Centralised and Reliable Data

A full end-to-end loan management system would enable originators' data to be stored in one single point of truth which is always up to date and which is accessible to all stakeholders. Subject to access permissions and rules, transaction parties including borrowers, brokers, investors, legal counsel, trustees, rating agencies, and any other stakeholders would all access the same data ledger, trusting that the data is correct and up to date. This approach means that data is not distributed in various formats across multiple channels; incurring cyber risk, data breaches and leaks, and data inconsistencies between different versions (as well as any additional processes required for manual reconciliation).

Single Point of Truth for Trust and Access

Harnessing blockchain technology (or similar) could deliver a single point of truth with read-write access and real-time data access. Further, data confirmation by the ecosystem of participants and/or AI agents could bring further efficiencies by removing the need for manual third-party checks of data and processes. Cloud data architecture today already offers 24/7 access to up to date reliable data through digital portals and other channels.

Standardised Data and Reporting

Digitalisation together with sector wide standardisation would enable baseline reporting standards to be established to the benefit of all transaction parties.

Certain systems available as at the date of this paper can automatically produce Bank of England loan tapes, stratification tables, and baseline loan performance data from a central data ledger which is always up to date.

Standardised templates could automate investor reporting in offering circulars and during the life of a transaction for the benefit of investors, servicers, back-up servicers and other stakeholders; they could feed into investment management systems such as Intex or ABS Suite or proprietary investor systems built on the standard template output.

Artificial Intelligence

AI systems can process borrower data in real-time for quicker and more accurate credit decisions. Incorporating non-traditional data, such as account activity, payment histories, social media activity, and customer engagement to assess creditworthiness increases accuracy further.

Since financial institutions are required to justify decisions to regulators (and customers) they are leaders in adopting explainable AI models. They are also developing combinations of AI and human in or on the loop systems to balance oversight with decision accuracy.

AI (or smart automations) in the flow of underwriting and funding advances sits across applications and funding to detect anomalies in real-time, in underwriting platforms to bring streamlining that reduces turnaround times and operational costs but increases consistency, and in post-trade analysis and reporting, monitoring both the underlying receivables and the operation of the portfolio management tools.

Often the greatest advantage of AI models is that they are dynamic and, therefore, better at the job after being in use for a period. The amount of data parsed and the ability to adapt to changes in data at macro and micro levels means that users benefit from more accurate, resilient, and precise outputs once adoption and implementation is complete.

Call to Action

- production of standardised documentation and processes at:
 - **originator level:** origination and underwriting policy, servicing manual, etc.; and
 - **funding structure level:** master definitions agreement including eligibility criteria and portfolio concentration limits, servicing agreement, back-up servicing agreement;
- setting standards of data definitions, raw data capture and maintenance, and reporting templates;
- process driven approach to transaction documentation and production, with emphasis placed on the work undertaken prior to producing the transaction documents;
- implementation of technology including blockchain (or similar) and AI (or smart automations); and
- **industry collaboration:** working groups with originators, funders, technology providers, and legal advisors to discuss and develop new ways of working.

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Appendix

To be completed by the originator

Disclaimer: this checklist should be used as a starting point at the beginning of a transaction to gather information and confirm structure. It can be tailored for originator or funder side deals and will need to be tailored on a transaction by transaction basis (not all questions will be relevant, and some questions assume we have not yet been provided with a draft term sheet).

Originator Checklist

Date:

Question / Information Required	Response
Commercial	
Please provide copies of all your lending policies	
[include KYC requirements]	
[include financial DD requirements]	
[include any other commercial information required]	
Structuring / Legal – Roles of Entities	
Please provide a copy of the group structure chart (including originator)	
Which entity will be the purchaser?	
Which entity will be the originator and the seller (the lender of record in respect of the customer loans)?	
Which entity will be the servicer (the entity that services the collections of the customer loans; typically this is also the originator)?	
Is a back-up servicer required?	
Does this need to be in place at completion, or will this be a post-closing action?	
Will the appointment be cold/warm/hot?	
Structuring / Legal – Cashflows	
Does the corporate group have any existing debt (including shareholder debt) in place. If so, please provide the details.	
Is it intended that this debt will be paid off, or will there be subordination arrangements put in place?	
Are any consents required?	
If the funder will not fund 100% of customer loans, how will the remaining percentage be funded (the 'top-up' amount)?	



Question / Information Required	Response
<p>Does the transaction create receivables which fulfil all of the following characteristics:</p> <ul style="list-style-type: none">— exposure is to an entity created specifically to finance / operate assets / is an economically comparable exposure (e.g. where an SPV is to be created);— lender to be given a substantial level of control over the assets and income generated by such assets (e.g. to be included within long form documentation); and— repayment is to be by income generated by assets being financed.	
Tax	
<p>Have you had tax advice on the structure of the transaction? <i>[NB tax leakage in the structure can make securitisations uneconomic. Funder will expect tax memos/opinions]</i></p>	
<p>Does the SPV need to be registered for FATCA purposes? Does it need a GIIN?</p>	
<p>Is the originator/seller/servicer registered for VAT?</p>	
<p>Is there a servicing fee? How much is it, and what are the services being provided? Which entity is carrying out the servicing? Have you received VAT advice in respect of the servicing fee and confirmation that the servicing fee is exempt from VAT? <i>[NB this affects the VAT analysis.]</i></p>	
<p>Are the underlying assets loans to customers, or some other arrangement (sale of receivables / invoice discounting)? <i>[NB this affects the tax analysis, for instance the availability of the loan capital exemption from stamp duty. Consider also the transfer of the assets to the SPV / orphan SPV in light of stamp and other taxes.]</i></p> <p>Is there any withholding tax due and payable in respect of payments made under the underlying loans? Do the underlying loans contain a tax gross up clause? Please confirm no UK stamp duty is due on the transfer of the underlying loans.</p>	
<p>Are any customer loans made to customers located outside the UK? If so, please confirm if any local withholding tax is triggered and if you have had tax advice on this. Please confirm that the underlying customer agreements include a tax gross-up clause.</p>	
<p>Does the beneficial owner have any subsidiaries, branches, offices outside the UK and if so, does it lend through these? <i>[NB if so, tax implications to be considered e.g. transfer taxes on the transfer of these assets to the SPV]</i></p>	
Data Protection	
<p>If the customer loans are being made to individuals/small partnerships/other 'consumer' type customers, will the loan reporting be provided on an anonymised or non-anonymised basis?</p>	
<p>Please provide a copy of your Privacy Notice.</p>	
Other	
<p><i>[Consider any additional questions required specific to the transaction.]</i></p>	