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The impact of legal advisor-issuer cooperation on securitization pricing

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Abstract

We examine the impact of cooperation between legal advisors and issuers on bank securitization pricing using 6,624 European ABS tranches issued in the European market over the period of 1998 to 2018. We find that previous cooperation is negatively related to initial yield spreads of ABS. Investors seem to attach value to previous cooperation between issuers and legal advisors and consider such transactions less risky by asking for lower yields. We observe that the magnitude of the past relationships is also of importance. Moreover, previous cooperation becomes more important as the risk of the transaction increases. This is especially noticeable when prime (AAA rated) tranches are compared to non-prime (non-AAA rated) tranches. Our results also show that the number of legal advisors in a deal does not matter for investors.

KEYWORDS
Europe, legal advisors, pricing, Securitization

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G21, G28

1 | INTRODUCTION

Bank securitization has grown greatly over the last four decades. Its systematic significance became apparent during the 2007–2009 Global Financial Crisis (GFC), where asset-backed securities (ABS) were central to the contagion of the crisis from the US housing market to the global financial system.[1] ABS are complex financial instruments with

significant information asymmetries prevalent in the securitization process. As a result, investors are exposed to various risks[2] and it is often challenging for them to accurately assess these[3], leaving them reliant on rating agencies' valuations. However, it is evident that in the pre-GFC period rating agencies underestimated the risk embedded in ABS (Brennan et al., 2009; Coval et al., 2009a;b) and inflated the ratings (Efing & Hau, 2015). Nonetheless, the empirical evidence also shows that in assessing ABS risk investors transcended assigned credit ratings. They considered various other factors such as the external credit enhancement and the quality of collateral (Fabozzi & Vink, 2012a, b), the possible rating shopping of originators (Fabozzi & Vink, 2015; He et al., 2012), the size of issuers and rating inflation (He et al., 2012), and the reputation of issuers and trustees (Deku et al., 2019a, b). This strand of the literature shows that issuance price of ABS is responsive to all available data, including the information on relevant parties involved in both the structural and transactional stages of securitization.

Although various counterparties' impact on the securitization process have been examined empirically, one significant omission is the *legal advisors*. Legal advisors play a key role in structuring ABS deals by providing and managing the full legal process, assisting in 'structuring the ABS, and selling the securities to investors' (Botlik et al., 2016, p.8). They provide legal opinion on the asset pool transfer and coordination with rating agencies, ensure that the transaction complies with all the regulations and the requirements of issuers and investors are met. More importantly, they offer investors legal advice on the *true sale* of the transaction, or *bankruptcy remoteness* of the issuer's Special Purpose Vehicle (SPV) from the originator (Fabozzi and Kothari, 2008).[4] It is challenging for investors to grasp the underlying legal context of ABS fully without the support of the legal advisors, as the prospectus is such a complex document often consists of hundreds of pages and drafted in legal terminology. At the same time, legal advisors work closely with issuers and they may repetitively interact with them over-time, structuring ABS deals. This repetitive interaction could potentially create close relationships between legal advisors and issuers that may potentially compromise the expected neutrality of legal advisors. Therefore, given the legal advisors critical responsibility in the securitization process, it is important to understand the potential influence of issuer and legal advisor interactions on the securitization process. In particular, we are interested in how investors perceive such interactions when assessing ABS risks at issuance.

Against this background, we investigate two issues in relation to legal advisors and issuer interaction and past collaboration in securitization transactions. First, we study whether the number of legal advisors participating in structuring an ABS matters for investors. In a securitization deal there could be two legal advisors representing the issuer and manager separately or one legal advisor representing both. There could be a potential for conflicts of interest or collusion between all parties if there is only one legal advisor in charge of legal structuring of the deal, particularly in relation to *true sale*. Two separate legal advisory teams each working for the benefit of their clients may be perceived more secure by investors. On the other hand, a securitization transaction consummated by two different legal advisory teams may be seen less risky by investors. Second, we examine how investors perceive previous long-term partnerships between a legal advisor and an issuer. Past cooperation between legal advisors and issuers could be viewed as a negative sign as longer partnerships can make parties more susceptible to conflict of interests. On the other hand, previous co-operation could be viewed as a positive sign as such experience between counterparties are likely to be highly valued when structuring complex ABS programs (Lupica, 1998).

We test our arguments by examining the information content of yield spreads of ABS at issuance as investors influence the price formation substantially during the issuance process.[5] Utilising this mechanism we investigate investors' perception of legal advisors and issuer interaction by analysing its impact on yield spreads at the pricing stage of ABS (Fabozzi & Vink, 2012a, b, 2015; He et al., 2012; Deku et al., 2019a; Deku et al., 2019b). Our sample includes 6,624 ABS tranches from seven major European countries[6] covering a 21-year period between 1998 and 2018. We hand-collect key variables regarding legal advisor identity from ABS deal prospectuses. We employ cross-sectional regressions controlling for a battery of factors including type of collateral, asset origin, issuer's identity, credit rating, amongst others.

Our results show that investors are indifferent as to whether or not there is only one or more legal advisor in a securitization deal. We find that investors value previous cooperation between issuers and legal advisors and consider such transactions less risky. They ask for lower yields if the issuer and the legal advisors have had an experience

of working together in the past. We observe that the magnitude of the past relationships also matters. Moreover, previous cooperation becomes more important as the risk of the transaction increases. This is especially noticeable when prime tranches (AAA rated) are compared to non-prime (non-AAA rated) tranches. Comparing the pre- and post-GFC periods, we find some evidence that investors started to attach even more value to close working partnership between the issuers and legal advisors in the post-GFC period.

Our contribution to this literature is twofold. For the first time in the literature, we examine whether ABS investors value information regarding the legal advisors engaged in securitization. Although the impact of various counterparties –such as issuers, trustees, rating agencies– on securitization pricing are considered by the literature, the possible impact of legal advisors in relation to prevalent information asymmetries is unknown. Given legal advisors important role in structuring financial instruments, drafting deal prospectuses and reviewing asset transfers, their significance is considerable. Legal advisors can help reduce information asymmetry between issuers and investors of complex structured bonds, thus assisting market participants in setting appropriate prices. In particular, we are not aware of any research on how investors perceive the relationships between legal advisors and issuers and legal advisor reputation. Investors' reaction to the information regarding legal advisors, and their interaction with issuers, when information asymmetry is high could unveil their potential importance. Secondly, we contribute to the literature by compiling a unique hand-collected data on legal advisor identities from prospectuses of over 10,000 ABS tranches. The coverage of our data is one of the largest in this literature, covering a period of over 20 years including the post-GFC period.

The rest of the paper is structured as follows. The next section explains the role of legal advisors in securitization and Section 3 describes the data and methodology used. Section 4 presents the results, and Section 5 provides the concluding remarks.

2 | LITERATURE REVIEW AND HYPOTHESIS DEVELOPMENT

2.1 | Legal advisors' role in designing ABS contracts

Securitization is a multiparty and multi-stage transactional process involving various complex legal processes completed by the legal advisors. Alongside rating agencies, servicer and financial advisors, legal advisors are considered one of the key parties involved. The role of legal advisors' in structured finance can be defined as assisting in 'structuring the securitization and selling the securities to investors' (Botlik et al., 2016, p.8). Their main tasks involve drafting deal prospectuses and asset sale and purchase agreements, developing agreements on the transfer of the underlying assets, and offering legal advice on the *true sale* or *bankruptcy remoteness* of the transaction (Fabozzi and Kothari, 2008; Botlik et al., 2016; Deloitte, 2018). They also provide legal opinion on the asset pool transfer and coordination with rating agencies. While making sure transaction complies with all the regulations, legal advisors also need to ensure that the requirements of issuers and investors are met. Therefore, issuers may also need legal advisors' guidance when they turn to securitization as a strategy of financing, risk transferring, or balance-sheet loan reduction.[7] One or several legal advisors can be required in a transaction to carry out the documentation on issues such as allocating the benefits, duties and risk distribution between the parties involved. Issues related to the collection and disbursement of receivables, insurance, liquidity, financial statements and other reporting, as well as provisions on default related matters come in many forms and have different impact on different parties. Although standard terminology is often used in such provisions, the risks or the consequences for the parties can considerably change due to possible different manners of expressions on a given matter (NABL, 2014) and the inclusions of many exceptions (Hughes, 2017).

In structured finance, in particular with off-balance sheet financing, the concept of *true sale* is essential. Hence, the most crucial feature of securitization is that the originator of the receivables and the ABS issuing entity (i.e. SPV) are legally separated. In other words, SPVs should be independent entities who are also bankruptcy remote (i.e. if the originator goes bankrupt the SPVs are immune) (Ayotte & Gaon, 2011; Schwarcz, 2013). It is this aspect of ABS that makes the resulting financial instruments particularly appealing. In order to ensure that an SPV's obligations are secure, even

in the case when the parent company goes bankrupt, credit rating agencies and investors are in need of legal opinions confirming the true sale of a transaction (Fabozzi and Kothari, 2008). On the one hand, investors do not need to evaluate the financial state of the originating lender, as they only need to assess the performance of the collateral underlying the securities. Hence, it is not unusual to see cases of an originating company having its credit rating downgraded, whilst at the same time its securitised products maintain high ratings due to various credit enhancements (Lupica 1998; Fabozzi & Vink, 2012b). On the other hand, prospective buyers need assurance that the assets have been transferred from the originator to an SPV as a true sale and that they are bankruptcy remote (Schwarcz, 2002; 2003; Fabozzi and Kothari, 2008). If the legal wording on the issue is not clearly expressed and fails to capture the complexities of the particular transaction, it can cause significant problems to the investors of the relative securities. Moreover, if the originator goes bankrupt, any legal weakness in the structure can be used to reverse the transferred assets back to the bankrupt owner (Lupica, 1998). The deal prospectus usually details all the main aspects of the transaction. However, such complex document often consists of hundreds of pages and drafted in legal terminology. Therefore, it is extremely challenging for a non-sophisticated investor to grasp the underlying context fully. Hence, legal opinions provided by legal advisors are crucial as they assure the transaction as a legal sale, that the assets are sold to a separate entity (i.e. SPV), and this entity is the legal owner of the assets (Hughes, 2017; Pinto & Alves, 2016). It is also essential that each party seeks legal advice to make sure they obtain the best alternatives for themselves, and are protected from possible legal risks. Overall, the legal aspects of securitization are important, and they can have significant influence on the price of structured finance issues (Lupica 1998; Schwarcz, 2005).

2.2 | Importance of legal advisors in ABS transactions

Views on legal advisors are contradictory in the literature. On the one hand, it is argued that in structured financial transactions, legal opinions are predominantly "third party legal opinions" (Schwarcz, 2005), i.e. although an originator or an issuer is the client of an outside legal advisor, the opinions provided to the clients are often to the benefit of third parties such as investors or rating agencies. These opinions effectively reduce information asymmetry among the parties involved in a transaction (Schwarcz, 2005). On the other hand, it is also argued that legal opinions in securitization cannot be relied upon by ultimate beneficiaries, such as the investors, as these opinions are addressed towards a client (i.e. the originator or the issuer) and thus should not be relied upon by the third parties (Carabellese, 2018).

It is argued that in securitization it is historically uncommon to see downgrades as a result of legal matters (Fabozzi & Vink, 2012b). Schwarcz (2005, p.6) further supports the view that legal opinions provided on the bankruptcy remoteness of an entity are not 'inherently deceptive or illegal', nor is there any proof that lawyers had intention to mislead market participants (Schwarcz, 2003). It is also emphasized that legal advisors, in evaluating ABS transactions, do not assess the 'business wisdom'. Yet their involvement in structured finance helps third parties (i.e. investors) to understand the externalities[8] and reduce information asymmetry among different parties engaged in the transaction (Schwarcz, 2005).

These positive notions in securitization concerning the legal aspects and the involved legal opinion providers may be perceived as an assurance by investors that SPVs are immune from insolvency and, therefore, can be valued by them when this is the case. For example, Ayotte and Gaon (2011) confirms how valuable insolvency protection can be for investors. They investigate the case of US company LTV Steel that was on the verge of bankruptcy filing, in which a bankruptcy court ruled that the securitised assets of the company could be used by the company for its ongoing operations, invalidating the true sale of the underlying assets. The authors assessed the implications of the decision on the price of other ABS products issued by non-depository institutions that can be similarly challenged by bankruptcy courts[9]. They observe a significant increase in the initial spread of ABS instruments issued by non-depository issuers after the court's decision as it increased the risks of structured bonds and weakened creditor protection.

Overall, the literature seems to suggest it is highly unlikely that legal opinions are deceptive towards any parties, and thus, the legal advisors are highly unlikely to be affected by moral hazard. Nevertheless, as far as we know, research

that negates the existence of collusion between legal advisors and issuers and/or any other parties in securitization is non-existent. Legal advisors engaged in a securitization deal are often hired by issuers, but there are many cases when managers also hire their own legal advisors. One of the essential aspects of their involvement in securitization is that they contribute to reduce information asymmetry by providing legal opinion. Although hired by issuers and/or managers, legal opinion rendered by legal advisors serve for the benefit of potential buyers of structured bonds as they intend to draft the detailed legal elements of the underlying asset pool (Wood, 2019). Therefore, the more detailed and clear the prospectus they develop the lower the information asymmetry between opposite sides of the transaction. Legal opinion also contributes to the ratings assigned to structured bonds as it is utilised as part of credit rating agencies assessment prior to issuing ratings (S&P, 2013; Fabozzi & Vink, 2012b). A note of caution, however, is expressed by Carabellese (2018) to ultimate beneficiaries of legal opinion, reminding potential buyers of ABS securities that legal opinions are issued by the request of the issuers.

Moreover, given that ABS markets are often profitable, legal advisors were also active and willing to participate in securitization processes. Interestingly, due to the complex nature of structuring ABS deals, legal advisors preferred to be involved with familiar programs (Lupica, 1998). For instance, the consultants of legal and financial advisory firms often guide their clients towards securitization programs which they are most familiar with. The author claims that after completing one transaction, advisory firms are likely to engage in similar financial programs as they would have established the knowledge and the skills. Yet, the author highlights the possibility that these legal advisors might have engaged with similar deals due to their lucrative nature. If such a profit-oriented motivation exists, then this may impact on the structural quality of the ABS.

2.3 | Factors impacting on ABS pricing beyond credit ratings

The initial yield spread (or the launch price in the primary market) of ABS reflects the risk premium that investors demand (Fabozzi & Vink, 2012b). Considering investors overwhelmingly relied on ratings agencies' assessments in pricing securities[10], the price of ABS products reflects mainly the risks evaluated by credit rating agencies. Generally, these are risks related to the collateral, cashflow and credit enhancement by third parties (Fabozzi & Vink, 2012a; 2012b). Due to the complex nature of structured financial products, the credit ratings assigned by rating agencies are more important in determining price than they are for standard corporate bonds, where risks are often tied into a single company's performance and investors can look at the financial stability of the issuing entity (He et al., 2012). This makes it easier to obtain the various filings reported by public companies in consistence with governing regulations. In the case of ABS securities, however, it is not as straightforward as the securitization process requires the pooling of credit sensitive assets (such as bank loans). These are then tranched into securities of different risk levels that are legally separated from the parent company and sold to an independent entity, i.e. the SPV. The SPV then sells the securities to investors. In contrast to corporate bonds, the structuring of a securitization program for many investors is not just a complex process, but one in which there is increased asymmetric information and moral hazard (Coval et al., 2009a; Ashcraft & Schuermann, 2009; Keys et al., 2010).

Although the complexity has made investors heavily reliant on credit ratings, the literature suggests ratings were not sufficient, and investors incorporated several other factors when pricing structured securities at issue (Adelino, 2009; Skreta & Veldkamp, 2009; Ashcraft et al., 2010). Cuchra (2005) argues that there is systematic difference in how rating agencies and investors assess certain aspects of securitization transactions. He provides empirical evidence that investors consider factors that are not included in rating agencies' assessments such as market placement and factors partly examined by rating agencies such as creditors' rights. Cuchra (2005) concludes that market liquidity, the number of underwriters involved in a transaction, the legal regime and the jurisdiction of a country were all considered by investors and reflected in ABS spreads at launch. Similarly, Fabozzi & Vink, 2012a, 2012b) also argue that although the collateral and credit enhancement aspects of an ABS transaction are assessed by the CRAs, investors went beyond these factors in assessing the risks of the bonds. He et al. (2012, 2016) argue that investors were aware of the

possibility that a conflict of interest could exist in ABS transactions and, thus, demanded a higher spread on the bonds. Their findings suggest that bonds issued by 'big issuers'[11] were granted inflated ratings (He et al., 2012), whereas the number of ratings assigned to a bond was seen as a sign for rating shopping[12] (He et al., 2016). Reputation of the trustees (Deku et al., 2019b) and issuers (Deku et al., 2019a) are also found to be influential factors beyond the credit ratings when investors price ABS. These studies conclude that investors value trustee and issuer reputation especially when risk assessment is challenging.

2.4 | Hypotheses tested

We posit that legal advisors' involvement can also impact on ABS initial yield spreads, reflecting investors sentiments about the legal risks of the deal due to the complex nature of securitized assets and legal advisors' interactions with issuers. Investors could be suspicious of potential conflicts of interest if the issuer and manager hire the same advisor to complete a deal. A single advisory firm hired by two parties at different ends of a transaction could be more susceptible to representing one party more than the other, or let go certain legal weaknesses, or at the worst, might collude with both parties in structuring a transaction. Such an arrangement may signal moral hazard risk to investors, in a similar way that a close relationship between issuers and credit ratings agencies was observed in the pre-GFC period (He et al., 2012), which witnessed increased risk appetite among the parties involved in structuring complex bonds and created opportunities for conflict of interest. Hence, a transaction involving two different legal advisory teams may concern investors less as both will work for the benefit of their clients, reducing the possibility of collusion. Investors may demand compensation for potential collusion between issuers and legal advisors, reflecting the higher legal risk. Alternatively, if investors do not see this as a potential risk, then the spread should not be affected. Therefore, we propose two alternative hypotheses:

H1a *- Initial yield spread is positively related to an issuer and a manager having the same legal advisor*
H1b *- Initial yield spread is not affected when an issuer and a manager have the same legal advisor*

Another aspect we consider is the past relationship between legal advisors and issuers. Investors may be cautious about the past links between legal advisors and issuers which could signal a negative message on their potential collaboration, as longer partnerships can make parties more susceptible to conflict of interests. On the other hand, if investors may view past cooperation between legal advisors and issuers as a positive sign, since previous experience is likely to be highly valued when structuring complex ABS programs (Lupica, 1998). Accordingly, we test the following hypotheses:

H2a *- Initial yield spread is positively related to the past relationships between an issuer and the legal advisors*
H2b *- Initial yield spread is negatively related to the past relationships between an issuer and the legal advisors*

3 | DATA AND METHODOLOGY

3.1 | Data sources

The data is obtained from Bloomberg, which provides detailed information on deal and tranche characteristics. However, for around 80% of the transactions the data for the identity of the legal advisors are not reported. In order to fill in the missing information, we went through the prospectus for each deal and manually collected the legal advisor firms' identity. Similarly, other missing characteristics such as issuer identity as well as maturity dates have all been singly filled in through deal prospectuses that are available in Bloomberg. We are primarily interested in major securitization

markets in Europe[13]. Our sample includes ABS and MBS deals issued France, Germany, Italy, Ireland, Netherlands, Spain and the UK between 1998 and 2018. These countries are responsible for over 81% of all the issued ABS securities in the continent (Bloomberg, 2018). The key deal characteristics are type of collateral, asset origin, pricing date, issue year, value of a deal, issuer nation, type of a deal, issuer's identity, issuer's legal advisor identity, manager's legal advisor identity. Furthermore, for each tranche of a deal we collect the assigned credit ratings, the value of the tranche and the maturity date. Initially, we collected information on 18,399 tranches; however, some data were eliminated due to missing key variables. As a result, the final sample in our study includes 6,624 tranches.

3.2 | Empirical model

Following the literature on measuring initial yield spread of structured finance securities (Cuchra, 2005; Fabozzi & Vink, 2012a;b; He et al., 2012; Deku et al., 2018), we specify the baseline model applied to describe the initial spread yield for a given tranche *i* as follows:

$$Spread_i = \beta_0 + \beta_1 L_i + \gamma' X_i + \varepsilon_i \quad (1)$$

Spread is the fixed premium set in basis points over the relevant benchmark rate. The offer price and the market demand on risk premiums at the issuance are represented by the primary spread as reliable indicator (Cuchra, 2005; He et al., 2012; Fabozzi and Vink, 2012; 2015; Deku et al., 2018). *L* is a set of four variables (*Same Advisor*, *Past Collaboration*, and *Collaboration Magnitude*) that we utilise interchangeably to capture the legal advisor related factors. *Same Advisor* equals to 1 if in a given deal a legal advisor of an issuer and a legal advisor of a manager are the same entity, and 0 otherwise. *Past Collaboration* is the variable used to describe previous cooperation. It is a dummy variable that equals to 1 if an issuer and either of the two legal advisors (issuer or manager legal advisors) have cooperated in previous ABS deals, and 0 otherwise. *Collaboration Magnitude* indicates the number of past cooperation between an issuer and the legal advisors. We count the number of all previous deals where the issuer worked with the same legal advisors. This variable aims to capture how investors perceived the magnitude of familiarity between issuer and legal advisor.

We use a set of variables (X_i) to control for various deal, tranche, issuer and macro characteristics. *Number of ratings* indicates the number of ratings reported for each tranche and utilised to control for rating shopping by issuers (He et al., 2012).[14] *Size* is the natural logarithm of each tranche value and controls for liquidity (Whetten and Adelson, 2004; He et al., 2012; Efing & Hau, 2015; Deku et al., 2018). *Weighted Average Life* is the tranche maturity in its logarithmic form (Cuchra, 2005; Adelino, 2009; Mahlmann, 2012; Efing & Hau, 2015; Deku et al., 2018). *Issue Type* equals to 1 if a deal is MBS, and 0 if it is non-MBS ABS (Cuchra, 2005; Deku & Kara, 2017). *Market Area* captures the market where the issues is traded and indicates Domestic, Global or International in the dummy variable form. *Issuer Nation* are important in pricing of the securities (Cuchra, 2005; He et al., 2012; Fabozzi & Vink, 2012b) and indicates the country where the securitization programs are structured. Macroeconomic conditions as well as legal systems in the country of origination can have a considerable impact on the performance of the ABS. *Guarantor* is a dummy variable and indicates whether external credit enhancement applies for a given ABS deal. Similarly, *Private Placement* is a binary variable and shows if sales of ABS tranches are conducted in public or private offering. *Credit Rating* is utilised to control for the credit quality of the ABS tranches by assigned credit ratings. Structural and asset risks can be captured by ratings and ratings are the biggest explanatory factor in yield spread (Fabozzi & Vink, 2012a; b; Cuchra, 2005). Our data includes ratings reported by the three big rating agencies: S&P, Fitch and Moody's. We convert the ratings into factor variables by using numerical point scale of 1 denoting (3A – the highest notch) down to 21 (C – the lowest notch) and we control for all rating categories. All the notches have been changed into numbers and arithmetic mean of all the available ratings per security has been calculated. We classify AAA rated securities as *prime* and others as *non-prime*. *Issuer Market Share* is a dummy taking the value of 1 if, for a given year, an issuer has been involved with at least 5% of all the issuance in the market in previous year, and 0 otherwise (Deku et al., 2018). Market volume for a

given firm is estimated as the ratio of the number of deals completed by an issuer to the number of all the deals in one-year period. Dummy variables for each issuer (*Issuers*) allows us to control for issuer specific omitted variables effect. *Collateral Nation* controls the country of origination for the assets underlying ABS. We control for time effects (*time*) using dummy variables indicating each quarter. One of the benefits of pooled cross-sectional data is that the sample size can be improved which in turn can lead to more accurate estimators as long as the relationships in estimation are stable over time. In order to relax this notion and allow temporal variation we employ time dummies (Wooldridge, 2013). Also, the introduction of *time* is important as the impact of macroeconomic factors across time are captured (Peterson, 2009). Following the literature, we estimate the models via OLS (Cuchra, 2005; Fabozzi & Vink, 2012a;b; He et al., 2012; Deku and Kara, 2018). In order to mitigate correlation of errors we cluster standard errors at deal level (Cuchra, 2005; Deku et al., 2018) as it is argued that tranches of a given deal may not be independent from each other (Deku et al., 2018).[15]

3.3 | Descriptive statistics

We present descriptive statistics for all variables in Table 1 Panel A. The percentage of the deals where the issuer and the manager have the *Same Advisors* are 21%. In 55% of the deals, issuer, issuer's legal advisor and manager's legal advisor cooperated together in the past (*Past Collaboration*). Average number of previous cooperation between an issuer and its legal advisor is 2.3 deals (*Collaboration Magnitude*). The mean of the initial yield spread is 129 basis points for the entire sample. On average, the deals are over €1.6bn while the mean value for each tranche is at around €280 m. The average rating for the securities is between AA- and A+, whereas the median is AA. Securities in the sample are issued by 740 different issuing entities, while 127 (Issuer) and 84 (Manager) legal advisors have been responsible for legally structuring the deals. In Panel B we present the distribution of tranches for the full sample by the assigned credit ratings. Overall, 8,443 tranches have been rated by at least one of the three CRAs. The securities rated as AAA (prime securities) constitutes the largest number of tranches in per notch terms, followed by AA, A and BBB rated tranches, respectively.

4 | REGRESSION RESULTS

The regression models we employ are estimated progressively. Initially, the results of the aggregate ABS sample are provided. We then present the estimations for the prime and non-prime tranches of the same sample. Further, we split the full sample into MBS and ABS and estimate the models separately for each sample. Lastly, we investigate the effects of legal advisors over the pre- and post- global financial crisis periods.

4.1 | Full sample

The results for the full sample are presented in Table 2. We employ the key variables, i.e. *Same Advisor*, *Past Collaboration*, and *Collaboration Magnitude* separately and estimation results are displayed in Columns 1 to 3, respectively. We find that the coefficient of *Same Advisor* is insignificant, suggesting that investors are indifferent as to whether or not the legal advisor is the same entity for both the manager and issuer. The possibility of collusion between parties does not seem to be a concern for investors, confirming *H1b*. This result can also be interpreted that investors do not see legal advisors acting unlawfully in case they work for both parties of the securitization deal. This result also confirms Schwarcz (2005) arguments that lawyers do not intentionally deceive or provide deceptive legal opinions, whilst investors do not see legal advisory teams to engage in conflicts of interest.

TABLE 1 Descriptive Statistics

Panel A					
Variable	*Mean*	*Median*	*Std.Dev.*	*Min.*	*Max.*
Same Advisor	0.21	0	0.41	0	1
Past Collaboration	0.55	1	0.50	0	1
Collaboration Magnitude	0.23	0	0.42	0	1
Spread (basis points)	129	68	161	−100	2,700
Weighted Average Life (Years)	33	30	27	1	100
Credit Rating	5	3	4	1	21
Number of Ratings	2	2	1	1	3
Number of Tranches	6.42	6	4.81	1	40
Tranche value (million EUR)	281	52	704	0.6	16,610
Deal Value (million EUR)	1,655	670	3,008	1.3	31,936

Panel B			
Rating	*% of sample*	*Rating*	*% of sample*
AAA	38.5	BB	4.4
AA+	1.8	BB-	1.2
AA	13.8	B+	0.3
AA-	2.8	B	0.6
A+	2.9	B-	1.1
A	12.9	CCC+	0.0
A-	2.0	CCC	0.0
BBB+	1.4	CCC-	0.1
BBB	11.5	CC	0.2
BBB-	3.5	C	0.0
BB+	0.9	Total	100.0

*We identify 740, 127 and 84 issuers, issuer legal advisors and manager legal advisors, respectively.

TABLE 2 The effect of legal advisors on initial market spread of ABS tranches

	(1)		(2)		(3)	
Same Advisor	2.3119	(5.4934)				
Past Collaboration			−11.7638***	(3.2221)		
Collaboration Magnitude					−6.3967***	(2.0135)
Number of Ratings	−14.8354***	(2.8628)	−13.3403***	(2.9668)	−12.7289***	(3.0786)
Size	−0.0041**	(0.0018)	−0.0041**	(0.0019)	−0.0044**	(0.0018)
Weighted Average Life	−0.0325	(0.0599)	−0.0271	(0.0612)	−0.0265	(0.0612)
Mortgage-backed	−27.2893***	(3.7274)	−26.1592***	(3.7336)	−26.1190***	(3.7585)
Domestic	−50.4851	(31.8344)	−53.6933*	(30.8549)	−55.9202*	(33.2949)
Global	−30.3466***	(6.7271)	−26.8785***	(7.3310)	−23.8621***	(7.7868)
International	6.1047	(6.5551)	15.8289**	(6.6602)	18.8373**	(7.4680)
France	−48.5576***	(9.4177)	−55.9063***	(10.1115)	−53.3653***	(9.2164)
Germany	−29.1114*	(15.6607)	−29.9095*	(15.6994)	−30.9508**	(15.5179)
Italy	−29.5355*	(17.3356)	−29.6281	(18.3267)	−32.1944*	(17.6630)
Netherlands	−8.5805	(8.1971)	−12.8180	(8.3295)	−11.9187	(8.2288)
Republic of Ireland	−2.5532	(10.6849)	−2.7267	(11.2052)	−3.4690	(11.0799)
Spain	−43.4801**	(16.9943)	−30.6244*	(17.8676)	−32.0257*	(17.2784)
Guarantor	−3.8748	(8.5781)	−4.6447	(8.6566)	−5.9937	(8.4151)
Private Placement	−6.9474*	(3.5987)	−7.5119**	(3.6296)	−7.6170**	(3.6197)
Credit Rating	Yes		Yes		Yes	
Issuer Market Share	Yes		Yes		Yes	
Issuer	Yes		Yes		Yes	
Collateral Nation	Yes		Yes		Yes	

(Continues)

TABLE 2 (Continued)

	(1)	(2)	(3)
Time	Yes	Yes	Yes
Obs.	6,624	6,368	6,368
R^2	0.748	0.748	0.748

This table presents OLS regressions of initial market spread of European issued ABS tranches on legal advisor, deal and tranche-level as well as collateral characteristics. Same Advisor is a dummy variable that takes the value of 1 if manager and issuer legal advisors are the Same Advisors, otherwise 0. Past Collaboration is a dummy variable that takes the value of 1 if both legal advisors and issuer have all cooperated in the past, otherwise 0. Collaboration Magnitude is the number of previous cooperation between issuer legal advisor and the issuer. Past Link2 is the number of past cooperation between both legal advisors and issuer. Number of ratings assigned for a given tranche is used to control for possible rating shopping. Size of each tranche (in $ millions) is employed to control for liquidity. Weighted Average Life is tranche's maturity conditional upon the prepayment expectations. Issue Type classifies the type of issuance i.e. the underlying assets for a tranche within a deal. Market Area where tranches of a deal is targeted for. Issuer Nation is the country where a tranche is issued. Guarantor indicates whether external credit enhancement applies for a given ABS deal. Tranche Credit Rating is the initial rating assigned for a tranche. Issuer Market Share is a dummy that takes the value of 1 is the issuer accounts for at least 5% of the market for previous year. Issuer of each deal has been controlled for. Collateral nation is where the collateral originates. Time is factor variable indicates issuing period quarterly. ***, ** and * indicate significance levels at 1%, 5% and 10%respectively. Robust standard errors are presented in parentheses.

The coefficient of *Past Collaboration* is negative and significant at 1% level. This result shows that investors ask for lower yields if the issuer and the legal advisors have had an experience of working together in the past, confirming *H2b*. For such deals initial yield spreads are, on average, 12 bps lower in comparison to deals where there is no previous working relationship between the issuer and legal advisors. Hence, investors value a previous working relationship and expect that such relationships will produce less risky securities. Liu (2015), examining the effect of past relationship between the issuer and underwriter on pricing of municipal bonds, report similar results. They conclude that investors' valuation of such deals as less risky could be due to the accumulation of soft information between parties, experience, comfort and trust that has been built through previous collaboration.

Our findings show that similar dynamics are present in securitization issuance. In particular, a previous relationship between issuer and legal advisor may aid the accumulation of knowledge and build trust. There is now an extensive literature emphasising the importance of trust between organisations, with a general agreement that trust becomes particularly important in situations characterised by risk and uncertainty (Dasgupta, 1988; Kramer, 1999; Gulati & Sytch, 2008). Higher levels of trust are associated with many benefits including reduced transaction costs, superior information sharing and higher organisational performance (Dyer & Chu, 2003). A key finding from this literature is that trust stems most of all from a past history of working together[16] (Gulati & Sytch, 2008). Since the securitisation process is a knowledge-intensive industry with significant information asymmetry, a previous relationship between issuers and legal advisors that builds trust is likely to involve lower costs.

The magnitude of the past relationship is captured with *Collaboration Magnitude* in Column 3. We find that *Collaboration Magnitude* has negative relationship with *Spread* at 1% significance level. This result shows that investors deemed ABS bonds less risky if the issuer and its legal advisor have a longer experience of working together in the past. The spread of deals where the issuer and legal advisors were working together for the first time is, on average, 6 bps higher than deals where the two actors have a past working relationship. Lower yields could be explained by the fact that investors possibly saw a longer term past cooperation as a positive sign as it can help build knowledge, expertise and trust between the two parties (Liu, 2015). The magnitude of the relationship here also implies that the more the two have worked together in the past, the lower the price.

Number of ratings, is negative and statistically significant. This shows that investors value a security that is rated by more than one rating agencies. This finding is in line with the rating shopping argument (He et al., 2012; 2016; Deku et al., 2018; 2019), where issuers chose to submit only highest ratings they receive, and they conceal the lower rates. The coefficient of *Issue Type* indicates that mortgage backed securities are seen as less risky by the market comparing to the rest of the ABS products. Negative significant values in all four models show that at issuance, MBS securities offer about 27 bps lower yield spread to buyers than other non-MBS ABSs. We also find that privately placed deals carry lower spreads.

4.2 | Prime versus non-prime tranches

By separating prime and non-prime securities we aim to examine whether investors' perception of legal advisors, and their interaction with issuer and managers, is related to the risk they are exposed to. Empirical evidence shows that AAA bonds can yield different results when compared to non-prime ones (Adelino, 2009; Mahlmann, 2012). The least risky prime tranches of ABS bonds for investors are the AAA rated. In Table 3, we present estimations where the sample is split as *prime*, or AAA rated (Panel A), and *non-prime*, or non-AAA rated (Panel B). Similar to the results for the full sample, we find that *Same Advisor* is not significant regardless of the riskiness of the bonds. *Past Collaboration* is negative in both categories; however, the statistical significance drops for the prime sample and remain at 1% for the non-prime sample. In addition, the size of the coefficient is much larger for the non-prime bonds (-18 bps) in comparison to the prime bonds (-4 bps). This suggest that investors attach more value to previous cooperation between the issuers and legal advisors as the risk increases. For both samples *Collaboration Magnitude* is negative and statistically

TABLE 3 The effect of legal advisors on initial market spread of prime and non-prime ABS tranches

Panel A: Prime (AAA)						
	(1)		(2)		(3)	
Same Advisor	−3.2189	(2.9447)				
Past Collaboration			−4.4242*	(2.5684)		
Collaboration Magnitude					−6.5245***	(1.5806)
Number of Ratings	−10.7500***	(2.0806)	−9.6834***	(2.1947)	−8.3391***	(2.2241)
Size	−0.0031***	(0.0012)	−0.0030**	(0.0012)	−0.0032***	(0.0012)
Weighted Average Life	0.0067	(0.0514)	0.0007	(0.0528)	−0.0032	(0.0519)
Mortgage-backed	−3.2277	(2.7763)	−2.8543	(2.9328)	−2.2902	(2.8187)
Guarantor	−10.4492*	(5.5561)	−12.1406**	(5.6601)	−13.6485**	(5.5635)
Private Placement	−5.3961**	(2.6954)	−5.8073**	(2.6993)	−6.3900**	(2.7161)
Obs.	2,533		2,437		2,437	
R^2	0.556		0.554		0.561	
Panel B: Non-Prime (non-AAA)						
	(1)		(2)		(3)	
Same Advisor	3.0219	(7.9543)				
Past Collaboration			−17.7515***	(4.3147)		
Collaboration Magnitude					−5.1463*	(2.7760)
Number of Ratings	−17.6613***	(3.7176)	−14.8872***	(3.8556)	−15.3261***	(4.0517)
Size	−0.0325***	(0.0085)	−0.0347***	(0.0090)	−0.0350***	(0.0089)
Weighted Average Life	−0.0164	(0.0767)	−0.0064	(0.0782)	−0.0075	(0.0785)
Mortgage-backed	−41.4976***	(5.0852)	−39.8416***	(5.0880)	−40.5754***	(5.2040)
Guarantor	−11.9577	(15.8347)	−10.8885	(15.6701)	−13.2997	(15.3017)
Private Placement	−10.7934**	(4.9478)	−11.3235**	(4.9621)	−11.1424**	(4.9648)

(Continues)

TABLE 3 (Continued)

Panel B: Non-Prime (non-AAA)			
	(1)	**(2)**	**(3)**
Obs.	4,091	3,931	3,931
R^2	0.763	0.764	0.762
All regressions in Panels A and B controlled for			
Credit Rating	Yes	Yes	Yes
Issuer/Issuer Market Share	Yes/Yes	Yes/Yes	Yes/Yes
Collateral/Issuer Nation	Yes/Yes	Yes/Yes	Yes/Yes
Market area/Time	Yes/Yes	Yes/Yes	Yes/Yes

This table presents OLS regressions of initial market spread of European issued prime and non-prime ABS tranches on legal advisor, deal and tranche-level as well as collateral characteristics. Same Advisor is a dummy variable that takes the value of 1 if manager and issuer legal advisors are the Same Advisors, otherwise 0. Past Collaboration is a dummy variable that takes the value of 1 if both legal advisors and issuer have all cooperated in the past, otherwise 0. Collaboration Magnitude is the number of previous cooperation between issuer legal advisor and the issuer. Number of ratings assigned for a given tranche is used to control for possible rating shopping. Size of each tranche (in $ millions) is employed to control for liquidity. Weighted Average Life is tranche's maturity conditional upon the prepayment expectations. Issue Type classifies the type of issuance i.e. the underlying assets for a tranche within a deal. Market Area where tranches of a deal is targeted for. Issuer Nation is the country where a tranche is issued. Guarantor indicates whether external credit enhancement applies for a given ABS deal. Tranche Credit Rating is the initial rating assigned for a tranche. Issuer Market Share is a dummy that takes the value of 1 is the issuer accounts for at least 5% of the market for previous year. Issuer of each deal has been controlled for. Collateral nation is where the collateral originates. Time is factor variable indicates issuing period quarterly. ***, ** and * indicate significance levels at 1%, 5% and 10%respectively. Robust standard errors are presented in parentheses.

significant. Investors seem to value previous cooperation between the issuers and legal advisors regardless the risk level of the bonds.

Other factors, such as *Number of ratings* and the *Size* of tranches are negative and significant in all specifications. It should be noted that markets have attached higher values for both variables when there is an increased risk. Negative coefficients for both are higher (in absolute value) for non-prime ABS. *Issue Type* is non-significant for AAA bonds, while in non-AAA rated instruments, investors demand about 41 bps less spread for MBS in comparison to non-MBS. These results further confirm that when the risk is higher investors assess all possible information when pricing an ABS issuance.

4.3 | MBS versus non-MBS tranches

Although MBS is a sub-category of ABS, their risk level is considered to be lower, mainly due to the quality of the underlying collateral (Deku et al., 2017). For this reason, we divide our sample into two groups as MBS and non-MBS and examine the relationship between our key variables and the spread separately for each sample. We present the results for non-MBS in Panel A of Table 4 and MBS in Panel B. Similar to previous results, the variable *Same Advisor* is insignificant for both non-MBS and MBS bonds, indicating that even if the risk levels of the tranches may be different, investors do not expect that having the Same Advisor will increase or mitigate risk levels. We find that the coefficient of *Past Collaboration* for the non-MBS sample is negative and statistically significant at 5% level (Column 2). However, for MBS this variable is not significant. These results indicate that when the risk is higher and difficult to assess, such as in the case of non-MBS, familiarity between issuers and legal advisors seems to reduce the potential risks envisaged by the investors. We find that *Collaboration Magnitude* is only significant in the non-MBS sample and insignificant in MBS sample. This result provide some evidence that as risk increases, past cooperation between the issuers and legal advisors becomes more important. We note that the coefficients of *Number of ratings* is about twice the size in the ABS sample, in comparison to the MBS sample, indicating the number of ratings matter more for investors when the risk is higher.

4.4 | Pre- and post-crisis periods

It is argued that during the boom period (between 2004 and 2007) leading up to the GFC, issuers engaged in riskier lending practices, reducing the quality of ABS issued. There is also evidence showing increase in wide-spread moral hazard in creation of ABS securities. To examine whether investors have changed their perception regarding the riskiness of these securities in the light of the catastrophic losses they faced after the GFC, we estimate our models by splitting the sample into two periods, before and after the financial crisis of 2007–2009. We present our results in Table 5 for pre-GFC period (1998 – June 2007) in Panel A and post-GFC period (2010 – 2018) in Panel B[17]. We find that the results are not different from the results we reported for the baseline model and also between these pre- and post-GFC periods. Particularly, the coefficients for the variable *Same Advisor* are not statistically significant for both periods. *Past Collaboration* and *Collaboration Magnitude* are all statistically significant and have negative relationships with the initial yield spreads. However, one difference we observe between the two periods is the larger coefficients, roughly doubling, in the post-GFC period for *Past Collaboration* and *Collaboration Magnitude.* These results show that investors started to attach even more value to close working partnership between the issuers, managers and legal advisors.

Table 6 compares prime and non-prime securities pre- and post-GFC periods. Note that for brevity in we do not report the full regressions, but only the relevant coefficient from each regression.[18] We find that *Same Advisor* does not yield significant coefficients in any of the sub-groups and periods. In the pre-GFC period *Past Collaboration* is significant for prime securities (Column 1), whereas, for riskier non-prime tranches (Column 2) it has a negative and

TABLE 4 The effect of legal advisors on initial market spread of ABS and MBS tranches

Panel A: Non-MBS						
	(1)		(2)		(3)	
Same Advisor	−0.2639	(7.5690)				
Past Collaboration			−8.3520**	(4.2295)		
Collaboration Magnitude					−10.6463***	(2.7822)
Number of Ratings	−21.7712***	(4.3514)	−20.3698***	(4.6171)	−20.0641***	(4.5851)
Size	0.0026	(0.0041)	0.0022	(0.0040)	0.0024	(0.0040)
Weighted Average Life	0.0047	(0.0788)	−0.0220	(0.0819)	−0.0228	(0.0796)
Guarantor	18.9982*	(10.5892)	16.5560	(10.7207)	13.6088	(10.5599)
Private Placement	−6.8362	(5.0447)	−7.6252	(5.0399)	−7.6171	(4.9662)
Obs.	2,859		2,746		2,746	
R^2	0.835		0.836		0.867	
Panel B: MBS						
	(1)		(2)		(3)	
Same Advisor	−3.6293	(6.1876)				
Past Collaboration			−4.6779	(3.7130)		
Collaboration Magnitude					−0.3808	(2.4677)
Residential dummy	−10.2764***	(3.9410)	−9.9550**	(3.9502)	−10.4354**	(4.1144)
Number of Ratings	−11.4798***	(3.4296)	−11.3257***	(3.3832)	−11.6196***	(3.5354)
Size	−0.0052**	(0.0021)	−0.0053**	(0.0022)	−0.0053**	(0.0021)
Weighted Average Life	0.0222	(0.0884)	0.0375	(0.0895)	0.0299	(0.0887)
Guarantor	−19.1759	(27.8259)	−19.5128	(27.6960)	−19.7974	(27.6700)

(Continues)

TABLE 4 (Continued)

Panel B: MBS						
	(1)		**(2)**		**(3)**	
Private Placement	−8.1685*	(4.4488)	−9.3226**	(4.4924)	−9.0060**	(4.4910)
Obs.	3,765		3,622		3,622	
R^2	0.674		0.672		0.672	
All regressions in Panels A and B controlled for						
Credit Rating	Yes		Yes		Yes	
Issuer/Issuer Market Share	Yes/Yes		Yes/Yes		Yes/Yes	
Collateral/Issuer Nation	Yes/Yes		Yes/Yes		Yes/Yes	
Market area/Time	Yes/Yes		Yes/Yes		Yes/Yes	

This table presents OLS regressions of initial market spread of European issued ABS and MBS tranches on legal advisor, deal and tranche-level as well as collateral characteristics. Same Advisor is a dummy variable that takes the value of 1 if manager and issuer legal advisors are the Same Advisors, otherwise 0. Past Collaboration is a dummy variable that takes the value of 1 if both legal advisors and issuer have all cooperated in the past, otherwise 0. Collaboration Magnitude is the number of previous cooperation between issuer legal advisor and the issuer. Number of ratings assigned for a given tranche is used to control for possible rating shopping. Size of each tranche (in $ millions) is employed to control for liquidity. Weighted Average Life is tranche's maturity conditional upon the prepayment expectations. Issue Type classifies the type of issuance i.e. the underlying assets for a tranche within a deal. Market Area where tranches of a deal is targeted for. Issuer Nation is the country where a tranche is issued. Guarantor indicates whether external credit enhancement applies for a given ABS deal. Tranche Credit Rating is the initial rating assigned for a tranche. Issuer Market Share is a dummy that takes the value of 1 is the issuer accounts for at least 5% of the market for previous year. Issuer of each deal has been controlled for. Collateral nation is where the collateral originates. Time is factor variable indicates issuing period quarterly. ***, ** and * indicate significance levels at 1%, 5% and 10%respectively. Robust standard errors are presented in parentheses.

TABLE 5 The effect of legal advisors on initial market spread of ABS tranches issued before and after the Great Financial Crisis (GFC)

Panel A: Before GFC						
	(1)		(2)		(3)	
Same Advisor	−0.4322	(5.1299)				
Past Collaboration			−10.4180***	(2.4738)		
Collaboration Magnitude					−5.4355***	(1.2948)
Number of Ratings	−18.4396***	(2.5648)	−16.9333***	(2.6206)	−16.1153***	(2.6481)
Size	0.0008	(0.0017)	0.0016	(0.0018)	0.0012	(0.0017)
Weighted Average Life	0.0248	(0.0533)	0.0269	(0.0559)	0.0326	(0.0562)
Mortgage-backed	−23.6538***	(3.5057)	−21.3672***	(3.4404)	−21.7934***	(3.4554)
Guarantor	−16.5604*	(9.5553)	−16.9377*	(9.1759)	−17.5473*	(8.9543)
Private Placement	0.9197	(3.4143)	0.7545	(3.2892)	0.7650	(3.3043)
Obs.	4,335		4,117		4,117	
R^2	0.751		0.756		0.756	
Panel B: Post GFC						
	(1)		(2)		(3)	
Same Advisor	−16.8619	(10.6852)				
Past Collaboration			−21.4243***	(6.4396)		
Collaboration Magnitude					−14.3899***	(4.1607)
Number of Ratings	7.8080	(8.7842)	11.6273	(8.6439)	12.8971	(8.6308)
Size	−0.0039	(0.0054)	−0.0048	(0.0058)	−0.0055	(0.0055)
Weighted Average Life	0.0368	(0.1230)	0.0634	(0.1270)	0.0398	(0.1251)
Mortgage-backed	−13.9376*	(7.3733)	−14.5466*	(7.5897)	−13.2718*	(7.4077)
Guarantor	−2.8300	(19.6577)	8.8202	(24.6722)	−0.1446	(22.0894)

(Continues)

TABLE 5 (Continued)

Panel B: Post GFC						
	(1)		**(2)**		**(3)**	
Private Placement	−9.8892	(6.7595)	−11.7836*	(6.8138)	−11.3037*	(6.7089)
Obs.	1,721		1,684		1,684	
R^2	0.801		0.801		0.802	
All regressions in Panels A and B controlled for						
Credit Rating	Yes		Yes		Yes	
Issuer/Issuer Market Share	Yes/Yes		Yes/Yes		Yes/Yes	
Collateral/Issuer Nation	Yes/Yes		Yes/Yes		Yes/Yes	
Market area/Time	Yes/Yes		Yes/Yes		Yes/Yes	

This table presents OLS regressions of initial market spread of European ABS tranches issued before and after the financial crisis on legal advisor, deal and tranche-level as well as collateral characteristics. Same Advisor is a dummy variable that takes the value of 1 if manager and issuer legal advisors are the Same Advisors, otherwise 0. Past Collaboration is a dummy variable that takes the value of 1 if both legal advisors and issuer have all cooperated in the past, otherwise 0. Collaboration Magnitude is the number of previous cooperation between issuer legal advisor and the issuer. Number of ratings assigned for a given tranche is used to control for possible rating shopping. Size of each tranche (in $ millions) is employed to control for liquidity. Weighted Average Life is tranche's maturity conditional upon the prepayment expectations. Issue Type classifies the type of issuance i.e. the underlying assets for a tranche within a deal. Market Area where tranches of a deal is targeted for. Issuer Nation is the country where a tranche is issued. Guarantor indicates whether external credit enhancement applies for a given ABS deal. Tranche Credit Rating is the initial rating assigned for a tranche. Issuer Market Share is a dummy that takes the value of 1 is the issuer accounts for at least 5% of the market for previous year. Issuer of each deal has been controlled for. Collateral nation is where the collateral originates. Time is factor variable indicates issuing period quarterly. ***, ** and * indicate significance levels at 1%, 5% and 10%respectively. Robust standard errors are presented in parentheses.

TABLE 6 The effect of legal advisors on initial market spread of ABS tranches issued before and after the Global Financial Crisis (GFC) for prime and non-prime bonds

	Before GFC		*Post GFC*	
	Prime (AAA)	**Non-Prime**	**Prime (AAA)**	**Non-Prime**
Same Advisor	0.4629	−1.7954	−9.3338	−10.8396
	(2.3627)	(7.3573)	(8.3262)	(17.7954)
Past Collaboration	−1.84	−14.1821***	−16.9288**	−23.2386***
	(1.3854)	(3.4399)	(7.2883)	(7.5492)
Collaboration Magnitude	−1.4637**	−7.2226***	−14.8437***	−9.1590*
	(0.6931)	(1.8512)	(3.4319)	(5.1061)

This table presents OLS regressions of initial market spread of European ABS on legal advisor, deal and tranche-level as well as collateral characteristics. For brevity we only report the coefficients of the key variables from 16 regressions, and full regressions are not reported. ***, ** and * indicate significance levels at 1%, 5% and 10%respectively. Robust standard errors are presented in parentheses. .

significant coefficient. This shows that having an issuer and legal advisor team that has worked together previously was valuable for investors when the securities are of high risks in the pre-GFC period. In contrast, for AAA prime securities, they perhaps relied on the credit ratings as these bonds were seen less risky. Looking at the post-GFC period, we find that *Past Collaboration* becomes more significant both for prime (Column 3) and non-prime (Column 4) securities, with larger coefficients. This result is plausible as investors' confidence on ABS bonds fell significantly in the post-GFC period due to experiences of substantial losses even for the triple-A rated bonds during the GFC, making investors more vary of the quality of these securities. Hence, investors started to put more trust on experience teams, requiring lower spreads, in securitization issuance. We find *Collaboration Magnitude* to be significant (albeit with different significance levels) in all of the specifications regardless of the risk. It is worth to note that the size of the coefficients increased in the post-GFC period, once again indicating the importance of experience issuance teams in securitization for investors.

4.5 | Robustness check with a uniform sample

We check robustness of our results by utilising a more uniform sample of the UK securitization market only. This is because, even though we control for country specific factors in various ways, there is still a possibility that our results could be affected by the legal environment in a way that is not captured in our analysis. The UK the largest ABS issuer in the EU, and in our sample it represents around 50% of the observations. Results are presented in Table 7. For the full sample (Column 1), we find that *Past Collaboration* and *Collaboration Magnitude* have negative coefficients and significant coefficients. We observe that both variables are also significant for prime and non-prime samples (Columns 2 and 3, respectively) with varying degrees of impact on price. We also observe that these variables impact on initial yield spreads became more important for investors in reducing perceived risks of ABS in the *Post GFC* period (Column 5). Overall, our results are robust and findings are similar to the ones reported for the full sample.

4.6 | Robustness check for predetermined legal advisor-issuer matching

In this section we address a potential source of bias in our estimates due to the possibility that legal advisors and issuers matches may be predetermined. In particular, it may be the case that legal advisors and issuers that have more presence in the securitization market are more likely to work together. In other words, as larger issuers (in terms of their share in the securitization issuance market) and larger legal advisors (in terms of their share of business activity in the securitization market) are more likely to be present in the market, they may be more likely to partner with each other, resulting in an endogenous legal advisor–issuer matching. In short, there may be fundamental differences between past collaborators versus non-collaborators, creating a bias in the impact of our *Past Collaboration* variable and yield spreads.

Following the literature (Kara et al., 2019), we use an instrumental variable approach to account for this possible bias using the market share of the legal advisor as an instrument. Accordingly, we create *Legal Advisor Market Share*, a dummy variable that takes the value of 1 for a given year if a legal advisor accounts for at least 10% of the total market volume in previous year, and 0 otherwise. In measuring market share, we follow the same intuition as in Deku et al., (2018; 2019) and He et al. (2012). Market volume for a given legal advisor is estimated as the ratio of the number of deals completed by the firm to the number of all the deals in one-year period. We are confident that the instrument we choose influences legal advisor–issuer matching without directly affecting the yield spreads of securitized bonds. To test whether *Legal Advisor Market Share* is a determinant of yield spreads, we estimate our baseline regression by including this variable. Results, presented in Appendix 2, shows that the coefficient of *Legal Advisor Market Share* is not statistically significant.

TABLE 7 The effect of legal advisors on initial market spread of ABS tranches – UK sample only

	Full sample	Prime (AAA)	Non-Prime	*Before GFC*	*Post GFC*
Same Advisor	18.6230	0.4194	19.7018	9.7803	6.3401
	(13.1362)	(4.4059)	(14.1537)	(10.8605)	(14.3610)
Past Collaboration	−11.2246***	−7.7985**	−15.4820***	−4.1719	−14.1294*
	(4.0447)	(3.4378)	(5.3051)	(3.3147)	(7.3237)
Collaboration Magnitude	−8.6796***	−9.7119***	−5.2462*	−3.2722*	−21.8586***
	(2.1489)	(1.9246)	(2.7819)	(1.7010)	(4.6062)

This table presents OLS regressions of initial market spread of European ABS on legal advisor, deal and tranche-level as well as collateral characteristics. Reported are the coefficients of main variables of interest for prime, non-prime, ABS and MBS tranches before and after the financial crisis. ***, ** and * indicate significance levels at 1%, 5% and 10%respectively. Robust standard errors are presented in parentheses. .

TABLE 8 2SLS Regressions

Panel A: Instrumented Past Collaboration						
	Whole sample		**Prime (AAA)**		**Non-Prime**	
	(1)		**(2)**		**(3)**	
Instrumented Past Collaboration	−59.2257***	(21.9784)	−82.0168***	(27.7250)	−66.1209**	(27.4807)
Number of Ratings	−13.6638***	(2.0086)	−9.4189***	(1.7805)	−15.7155***	(2.8764)
Size	−0.0025	(0.0017)	−0.0012	(0.0011)	−0.0321***	(0.0071)
Weighted Average Life	−0.0370	(0.0421)	−0.0023	(0.0381)	−0.0241	(0.0593)
Mortgage-backed	−27.2406***	(2.3955)	−3.4521	(2.1767)	−41.3452***	(3.3589)
Guarantor	−3.3550	(11.3944)	−11.4487	(8.7244)	−10.5591	(18.1720)
Private Placement	−7.0222***	(2.3004)	−5.5991***	(2.0471)	−10.8956***	(3.2582)
Obs.	6,368		2,437		3,931	
R^2	0.7473		0.5550		0.7619	
Panel B: Instrumented Collaboration Magnitude						
	Whole sample		**Prime (AAA)**		**Non-Prime**	
	(1)		**(2)**		**(3)**	
Instrumented Collaboration Magnitude	−25.6524***	(9.5195)	−31.0361***	(10.4915)	−30.49231**	(12.6730)
Number of Ratings	−13.6638***	(2.0086)	−9.4189***	(1.7805)	−15.7155***	(2.8764)
Size	−0.0021	(0.0017)	−0.0015	(0.0011)	−0.0304***	(0.0073)
Weighted Average Life	−0.0370	(0.0421)	−0.0023	(0.0381)	−0.0241	(0.0593)
Mortgage-backed	−27.2406***	(2.3955)	−3.4521	(2.1767)	−41.3452***	(3.3589)
Guarantor	−3.3550	(11.3944)	−11.4487	(8.7244)	−10.5591	(18.1720)

(Continues)

TABLE 8 (Continued)

Panel B: Instrumented Collaboration Magnitude						
	Whole sample		**Prime (AAA)**		**Non-Prime**	
	(1)		**(2)**		**(3)**	
Private Placement	−7.0222***	(2.3004)	−5.5991***	(2.0471)	−10.8956***	(3.2582)
Obs.	6,368		2,437		3,931	
R^2	0.7473		0.5550		0.7619	
All regressions in Panels A and B controlled for						
Credit Rating	Yes		Yes		Yes	
Issuer/Issuer Market Share	Yes/Yes		Yes/Yes		Yes/Yes	
Collateral/Issuer Nation	Yes/Yes		Yes/Yes		Yes/Yes	
Market area/Time	Yes/Yes		Yes/Yes		Yes/Yes	

This table shows the results of the two-stage least squares estimations of European issued ABS initial yield spread on Instrumented Past Collaboration, Instrumented Collaboration Magnitude, ratings, size, weighted average life, issuer reputation and other deal and tranche level characteristics. Past Collaboration is a dummy variable that takes the value of 1 if both legal advisors and issuer have all cooperated in the past, otherwise 0. Instrumented Past Collaboration is the predicted value of Past Collaboration that is obtained in the first stage of the estimation. Collaboration Magnitude is the number of previous cooperation between issuer legal advisor and the issuer. Instrumented Collaboration Magnitude is the predicted value of Collaboration Magnitude that is obtained in the first stage of the estimation. Legal Advisor Market Size is utilised as the instrument. Legal Advisor Market Size is a dummy variable that takes the value of 1 for a given year if the legal advisor accounts for at least 10% of the market share for previous year, otherwise 0. Issuer Market Size is a dummy that takes the value of 1 is the issuer accounts for at least 5% of the market for previous year. Number of ratings assigned for a given tranche is used to control for possible rating shopping. Size of each tranche (in $ millions) is employed to control for liquidity. Weighted Average Life is tranche's maturity conditional upon the prepayment expectations. Issue Type classifies the type of issuance i.e. the underlying assets for a tranche within a deal. Market Area where tranches of a deal is targeted for. Issuer Nation is the country where a tranche is issued. Guarantor indicates whether external credit enhancement applies for a given ABS deal. Tranche Credit Rating is the initial rating assigned for a tranche. Issuer Market Share is a dummy that takes the value of 1 is the issuer accounts for at least 5% of the market for previous year. Issuer of each deal has been controlled for. Collateral nation is where the collateral originates. Time is factor variable indicates issuing period quarterly. ***, ** and * indicate significance levels at 1%, 5% and 10%respectively. Robust standard errors are presented in parentheses.

We utilize a 2SLS estimator to implement the instrumental variable estimation. In the first stage, we regress the *Past Collaboration* and *Collaboration Magnitude* on *Legal Advisor Market Share*, *Issuer Market Share*, *Size* of the deal, and country where the deal is issued (*Issuer Nation*). We choose these set of variables as the main determinants of past collaboration between issuers and legal advisors as such interaction is more likely to be the result of institutions volume of activity in the securitization market, size of the securitization deal and the country of issuance. In the second stage we use the *Instrumented Past Collaboration* and *Instrumented Collaboration Magnitude* variable to run our main models. We present results in Table 8 (Panel A for *Instrumented Past Collaboration* and Panel B for *Instrumented Collaboration Magnitude*) for the whole sample and prime versus non-prime sub-samples. In all models we still find positive and significant coefficients for *Past Collaboration* and *Collaboration Magnitude*.

5 | CONCLUSION

Legal advisors play a crucial role in structuring ABS by providing information on the legal process, assisting in structuring the deal and selling the securities to investors, developing contracts for the portfolio, and offering legal advice on the 'bankruptcy remoteness' of the transaction. In this paper, we investigate the influence of legal advisors on the securitization process. In particular, we examine how the structure of the legal advisory team and their previous working relationships with issuers are perceived by investors buying these securities. Our sample includes more than 10,219 ABS issued in seven European countries between 1998 to 2018.

We find that investors value previous cooperation between issuers and legal advisors. The results suggest that past collaboration between issuer and legal advisors is perceived as a positive sign by the market and thus reflected in the prices of the securities. Moreover, as the risk increases, the importance of the relationship is seen to have strengthened. This is especially noticeable when prime tranches of a deal are compared to non-prime securities of the same deal. In terms of the overall securitization market before and after the crisis, like previous literature, due to plunging confidence, the relationship in our model becomes weaker after 2009.

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NOTES

[1] Since the GFC a growing literature has provided extensive empirical evidence on the negative effects of securitization on bank risk taking and financial stability (see Deku et al., 2019c for an extensive survey).

[2] These include poor quality ABS due to relaxed bank lending standards of underlying loans (Keys et al., 2010; Dell'Ariccia et al., 2012; Nadauld and Sherlund, 2013), inadequate bank monitoring of loans post-ABS issuance (Petersen and Rajan, 2002; Kara et al., 2018), misreporting of assets in the securitization pools (Piskorski et al., 2015; Griffin and Maturana, 2016) and falsified declarations by borrowers whose loans are securitized (Jiang et al., 2013; Griffin and Maturana, 2016).

[3] These include poor quality ABS due to relaxed bank lending standards of underlying loans (Keys et al., 2010; Dell'Ariccia et al., 2012; Nadauld and Sherlund, 2013), inadequate bank monitoring of loans post-ABS issuance (Petersen and Rajan, 2002; Kara et al., 2018), misreporting of assets in the securitization pools (Piskorski et al., 2015; Griffin and Maturana, 2016) and falsified declarations by borrowers whose loans are securitized (Jiang et al., 2013; Griffin and Maturana, 2016).

[4] SPVs should be the sole legal owner of underlying assets of the ABS and be immune if the originator goes bankrupt (Ayotte and Gaon, 2011; Schwarcz, 2013). Any legal weaknesses in the structure of the ABS in case of originator's bankruptcy, can be used to reverse the transferred assets back to the bankrupt owner (Lupica, 1998).

[5] Accordingly, issuers set a provisional price based on the sentiment as investors indicate the price they are willing to pay, as well as the corresponding volume. To ensure that the issue is well subscribed to, issuers are diligent to avoid overpricing (Choudhry, 2011).

[6] France, Germany, Italy, Ireland, Netherlands, Spain and the UK. ABS issued in these markets constitute over 80% of all ABS volume in the European market during this period.

[7] Similarly, credit rating agencies, before issuing their ratings, consider various possible legal risks in a deal, different scenarios on the existence of the assets, legal issues regarding asset isolation, SPV and so on (S&P, 2013; Fabozzi and Vink, 2012b). For instance, legal risks could include the possibility that underlying assets cease to exist due to documentary defect, or assets become unenforceable due to minor fouls in mandatory legislative requirements (S&P, 2013).

[8] Possible costs incurred by investors due to misleading legal opinion by legal advisors e.g. weakly drafted legal opinion on the true sale.

[9] Issuances by insured depository institutions cannot be judged by bankruptcy courts as they were governed by FDIC which guarantees insolvency protection of ABS issuances (Ayotte and Gaon, 2011).

[10] Evidenced by a number of studies including Cuchra (2005), Adelino (2009), Coval et al. (2009b), Skreta and Veldkamp (2009), Partnoy (2009), Kisgen and Strahan (2010), and Mahlmann (2012).

[11] "Big issuer" refers to the market size of the issuer i.e. the issuer is among the top 10% of the market share distribution for a given year (He et al., 2012).

[12] Authors concluded that below AAA single-rated tranches compared to ones with multi ratings were seen as riskier bonds, as investors perceived it as a sign for rating shopping. That is, issuers shopped for better ratings and undesirable ratings were never published.

[13] The European securitization market is the second biggest in the world and although the damage caused by financial crisis was not as severe as it was in the US, the recovery of the market has been sluggish (EPRS, 2015). Therefore, in order to exploit its potential benefits, there has been a growing sentiment in recent years by EU policymakers to revive the 'well-functioning' securitization markets. Creating healthy securitization market requires regulatory bodies to introduce stricter rules to avoid increased information asymmetry and conflict of interest between parties while protecting investors and creating more transparent environment.

[14] Rating shopping occurs when an issuer decides to publish only the highest ratings received and ignore lower rates thus it influences rating agencies to issue inflated ratings (Skreta and Veldkamp, 2009; He et al., 2012). This phenomenon increases the risk of securities thus the price of securities demanded by investors (He et al., 2012; 2016). Reporting all the ratings are not a requirement, but the availability of all the three CRAs' ratings makes investors more comfortable who might otherwise suspect the issuers of supressing negative ratings.

[15] CRAs adopt different techniques and yardsticks in assessing the ABS securities. While the risk evaluation can be carried out at deal and/or tranche levels, any deal specific assessment revisions leads to deal-wide rating changes. According to Adelino (2009), ratings revisions on multiple tranches are often carried out about same time.

[16] Parties to an exchange develop a greater trust in each other by learning about each other's competence and reliability to carry out the task at hand (Child and Mollering 2003). A joint history of interaction enables partners to create a more effective system of rewards and penalties, whilst developing a stronger identification with their partners and greater confidence in their integrity (Gulati and Sytch 2008).

[17] We exclude the period of July 2007- December 2009 as the European securitization market came to a halt during this period and most issues were not bought by the investors.

[18] Full results are available upon request.

DATA AVAILABILITY STATEMENT

Data is available on request from the authors.

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APPENDIX 1: VARIABLES LIST

Variables	Description	Source
Spread	Fixed premium set in basis points over the relevant benchmark rate. The offer price and the market demand on risk premiums at the issuance are better represented by the primary spread as it is a more reliable indicator	Bloomberg
Same Advisor	This is a binary variable that takes the value of 1 if single legal advisory team is employed by issuer and manager.	Authors' calculation
Past Collaboration	Equals 1 if issuer and issuer's legal advisor and manager's legal advisor have had cooperated together in the past.	Authors' calculation
Collaboration Magnitude	This variable shows the number of previous cooperation between issuer and its legal advisor	Authors' calculation
Tranche Credit Rating	Ratings issued by the Big Three CRAs converted into factor variables, using numerical point scale of 1 (denoting 3A) down to 21 (C). Arithmetic mean of all the available ratings per security has been calculated. We classify 1 (AAA) rated securities as prime class securities while the rest as non-prime class.	Bloomberg
Number of Ratings	This variable shows the number of ratings reported for a securitised bond. We use this variable to capture the potential effects of rating shopping by issuers that might impact the initial spread of tranches demanded by investors.	Bloomberg
Size	Possible effects of liquidity are addressed by this variable. The variable tranche size is the value (in € millions) of each security within a structured deal.	Bloomberg
Time	The deal issuances are reported quarterly over a two-decade period. We assume that the quality thus the price of securities change as time changes. The variable can help capture the effects of time and potential macroeconomic factors that might impact the price of structured instruments.	Bloomberg
Weighted Average Life	This variable is tranche's maturity conditional upon the prepayment expectations. It can control for the possible risks that might arise due to maturity and prepayment effects.	Bloomberg
Issue Type	This variable classifies the type of issuance i.e. the underlying assets for tranches within a deal. The variable can help capture risks that can arise due to varying assets that underlie securitised bonds.	Bloomberg
Issuer	Issuer effects are used to capture the specific attributes of the issuer indicator. The introduction of dummy variables for each issuer allows us to control for issuer specific omitted variables effect.	Bloomberg
Issuer Market Share	Dummy that takes the value of 1 if, for a given year, an issuer has been involved with at least 5% of all the issuance in the market in previous year, and 0 otherwise. Market volume for a given firm is estimated as the ratio of the number of deals completed by an issuer to the number of all the deals in one-year period.	Authors' calculation
Legal Advisor Market Share	Dummy variable takes the value of 1 for a given year if a law firm accounts for at least 10% of the total market volume in previous year. Market volume for a given firm is estimated as the ratio of the number of deals completed by the legal firm to the number of all the deals in one-year period. The same method has been used for both issuer's and manager's legal advisors.	Authors' calculation

Variables	Description	Source
Issuer Nation	The country where securitisation pograms are structured and used to control for country specific macroeconomic and legal conditions that might effect the price of ABS.	Bloomberg
Collateral Nation	Variable shows the country of origination for the assets underlying securitised bonds. The variable can help addressing country specific attributes that might impact ABS spread.	Bloomberg
Guarantor	This variable controls for the possible effects of external credit enhancements. The dummy indicates whether external credit enhancement applies for a given ABS deal.	Bloomberg
Private Placement	Binary variable that shows if sales of ABS tranches are conducted in public or private offering	Bloomberg
Market Area	Market area is where tranches of a deal is targeted to be traded at. It helps in addressing possible country specific characteristics that might impact the spread of tranches.	Bloomberg

APPENDIX 2: : THE IMPACT OF LEGAL ADVISOR MARKET SHARE ON YIELD SPREAD

Legal Advisor Market Share	**−6.1668**	**(3.6051)**
Number of Ratings	−15.3274***	(2.8706)
Size	−0.0041**	(0.0018)
Weighted Average Life	−0.0283	(0.0595)
Mortgage-backed	−27.3061***	(3.7190)
Domestic	−46.6917	(33.0336)
Global	−30.7871***	(6.7824)
International	5.4831	(6.6121)
France	−47.7337***	(9.5827)
Germany	−27.6966*	(15.7940)
Italy	−28.5107	(17.6052)
Netherlands	−7.9109	(7.9844)
Republic of Ireland	−1.7817	(10.8583)
Spain	−40.6544**	(17.1266)
Guarantor	−3.6005	(8.5565)
Private Placement	−6.7855*	(3.5144)
Credit Rating	Yes	
Issuer Reputation	Yes	
Issuer	Yes	
Collateral Nation	Yes	

Legal Advisor Market Share	**−6.1668**	**(3.6051)**
Time	Yes	
Obs.	6,624	
R^2	0.748	

This table presents OLS regressions of initial market spread of European issued ABS tranches on legal advisor, deal and tranche-level as well as collateral characteristics. Same Advisor is a dummy variable that takes the value of 1 if manager and issuer legal advisors are the Same Advisors, otherwise 0. Past Collaboration is a dummy variable that takes the value of 1 if both legal advisors and issuer have all cooperated in the past, otherwise 0. Collaboration Magnitude is the number of previous cooperation between issuer legal advisor and the issuer. Past Link2 is the number of past cooperation between both legal advisors and issuer. Legal Advisor Size is a dummy variable that takes the value of 1 for a given year if the legal advisor accounts for at least 5% of the market share for previous year, otherwise 0. Number of ratings assigned for a given tranche is used to control for possible rating shopping. Size of each tranche (in $ millions) is employed to control for liquidity. Weighted Average Life is tranche's maturity conditional upon the prepayment expectations. Issue Type classifies the type of issuance i.e. the underlying assets for a tranche within a deal. Market Area where tranches of a deal is targeted for. Issuer Nation is the country where a tranche is issued. Guarantor indicates whether external credit enhancement applies for a given ABS deal. Tranche Credit Rating is the initial rating assigned for a tranche. Issuer Reputation is a dummy that takes the value of 1 is the issuer accounts for at least 5% of the market for previous year. Issuer of each deal has been controlled for. Collateral nation is where the collateral originates. Time is factor variable indicates issuing period quarterly. ***, ** and * indicate significance levels at 1%, 5% and 10%respectively. Robust standard errors are presented in parentheses.