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The International Comparative Legal Guide to:

Lending & Secured Finance 2018

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A practical cross-border insight into lending and secured finance

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EDITORIAL

Welcome to the sixth edition of *The International Comparative Legal Guide to: Lending & Secured Finance*.

This guide provides corporate counsel and international practitioners with a comprehensive worldwide legal analysis of the laws and regulations of lending and secured finance.

It is divided into three main sections:

Three editorial chapters. These are overview chapters and have been contributed by the LSTA, the LMA and the APLMA.

Twenty one general chapters. These chapters are designed to provide readers with an overview of key issues affecting lending and secured finance, particularly from the perspective of a multi-jurisdictional transaction.

Country question and answer chapters. These provide a broad overview of common issues in lending and secured finance laws and regulations in 54 jurisdictions.

All chapters are written by leading lending and secured finance lawyers and industry specialists and we are extremely grateful for their excellent contributions.

Special thanks are reserved for the contributing editor Thomas Mellor of Morgan, Lewis & Bockius LLP for his invaluable assistance.

Global Legal Group hopes that you find this guide practical and interesting.

The *International Comparative Legal Guide* series is also available online at www.iclg.com.

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Loan Syndications and Trading: An Overview of the Syndicated Loan Market

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In the past 30 years, the art of corporate loan syndications, trading, and investing has changed dramatically. There was a time when banks lent to their corporate borrowers and simply kept those loans on their books, never contemplating that loans would be traded and managed by investors like stocks and bonds in a portfolio. In time, however, investors became drawn to the attractive features of loans. Unlike bonds, loans were senior secured debt obligations with a floating rate of return, and, over the years, an institutional asset class emerged. Today, such loans are not only held by banks but are also typically sold to other banks, mutual funds, insurance companies, structured vehicles, pension funds, and hedge funds. This broader investor base has brought a remarkable growth in the volume of loans being originated in the primary market and subsequently traded in the secondary market. The syndicated loan market represents one of today's most innovative capital markets.

In 2017, total corporate lending in the United States surpassed $2.5 trillion.[1] This figure encompasses all three subsectors of the syndicated loan market – the investment grade market, the leveraged loan market, and the middle market. In the investment grade market, total lending stood at approximately $820 billion in 2017. Most lending in the investment grade market consists of revolving credit facilities to larger, more established companies. The leveraged loan market, where loans are made to companies with non-investment grade ratings (or with high levels of outstanding debt), represented approximately $1.4 trillion.[2] Leveraged loans are typically made to companies seeking to refinance existing debt, to finance acquisitions or leveraged buy-outs, or to fund projects and other corporate endeavours such as dividend recapitalisations. Leveraged loans comprise the overwhelming majority of loans that are traded in the secondary market. Then there is the middle market. As traditionally defined, middle market lending includes loans of up to $500 million that are made to companies with annual revenues of under $500 million.[3] For these companies, the loan market is a primary source of funding. In 2017, middle market lending totalled approximately $280 billion.[4]

Of these three market segments, it is the leveraged loan market that has evolved most dramatically over the past 30 years. Attracted by the higher returns of the loan asset class, the investor base expanded significantly starting from the mid 1990s and has grown increasingly more diverse. This, in turn, fuelled demand for loans, leading to a commensurate rise in loan origination volumes in the primary market. For the loan market to grow successfully, for the loan asset class to mature, and to ease the process of trading and settlement, the new entrants to the market in the 1990s needed uniform market practices and standardised trading documentation. In response to these needs, the Loan Syndications and Trading Association ("LSTA" or "Association") was formed in 1995, and its mission since inception has included the development of best practices, market standards, and trading documentation. The LSTA has thus successfully spearheaded efforts to increase the transparency, liquidity, and efficiency of the loan market; in turn, this more standardised loan asset class has directly contributed to the growth of a robust, liquid secondary market.

The LSTA's role has expanded since the Global Financial Crisis to meet new market challenges, assuming more prominence in the loan market generally and regularly engaging with the U.S. government and its regulatory bodies on legislative and regulatory initiatives. Policymaking in the wake of the financial crisis had included sweeping changes to the financial industry, including to the loan market, even though the regulatory impact on the loan market was sometimes an unintended byproduct of reform legislation aimed somewhere else. The LSTA has, therefore, dedicated substantial time and energy over the past decade to building awareness amongst regulators about the loan market and how it functions, seeking to distinguish it from other markets and, at times, persuading policymakers to exempt the loan market from particular legislative measures.

Now in the second phase of its regulatory outreach programme, the LSTA is maintaining a dialogue about the loan market with regulators and promoting the many benefits of a vibrant leveraged loan market for U.S. companies.

This chapter examines: (i) the history of the leveraged loan market, focusing on the growth and maturation of the secondary trading market for leveraged loans; (ii) the role played by the LSTA in fostering that growth through its efforts to standardise the practices of, and documentation used by participants active in, the secondary loan market to bring greater transparency to the loan asset class; and (iii) the regulatory challenges faced by the loan market.

Growth of the Secondary Market for Leveraged Loans

The story of the leveraged loan market starts about 30 years ago in the United States, with the first wave of loan market growth being driven by the corporate M&A activity of the late 1980s. Although a form of loan market had existed prior to that time, a more robust syndicated loan market did not emerge until the M&A deals of the 1980s and, in particular, those involving leveraged buy-outs (LBOs), which required larger loans with higher interest rates. This had two significant consequences for the loan market. First, because banks found it difficult to underwrite very large loans on their own, they formed groups of lenders – syndicates – responsible for sharing the funding of such large corporate loans. Syndication enabled the banks to satisfy market demand while limiting their own risk exposure to any single borrower. Second, the higher interest rates associated with these large loans attracted non-bank lenders to the loan market, including traditional bond and equity investors, thus creating a new demand stream for syndicated loans. Retail mutual funds also entered the market at this time and began to structure their funds for the sole purpose of investing in bank loans. These loans generally were senior secured obligations with a floating interest rate. The resultant asset class had a favourable risk-adjusted return profile. Indeed, a non-bank appetite for syndicated leveraged loans would be the primary driver of demand that helped propel the loan market's growth.[5]

Although banks continued to dominate both the primary market (where loans are originated) and the secondary market (where loans are traded), the influx of the new lender groups in the mid-1990s saw an inevitable change in market dynamics within the syndicated loan market. In response to the demands of this new investor class, the banks, which arranged syndicated loans, began modifying traditional deal structures, and, in particular, the features of the institutional tranche or term loan B, that portion of the deal which would typically be acquired by the institutional or non-bank lenders. The size of these tranches was increased to meet (or create) demand, their maturity dates were extended to suit the lenders' investment goals, and their amortisation schedules tailored to provide for only small or nominal instalments to be made until the final year when a large bullet payment was scheduled to be made by the borrower. In return, term loan B lenders were paid a higher rate of interest. All these structural changes contributed to a more aggressive risk-return profile, which was necessary in order to still attract more liquidity to the asset class.

A true secondary market for leveraged loans in the United States emerged in the 1990s. During the recession of the early 1990s, default rates rose sharply, which severely limited the availability of financing, particularly in transactions involving financing from regional and foreign banks. Interest rates to non-investment grade borrowers thus increased dramatically. Previously, banks had carried performing loans at par or face value on their balance sheets, while valuations below par (expected sale prices) were only generally assigned to loans that were in or near default. During the credit cycle of the early 1990s, however, a new practice developed in the banking industry. As banks in the U.S. sought to reduce their risk and strengthen their balance sheets, they chose to sell those leveraged loans which had declined in value since their syndication, rather than hold the loans until their maturity date as they had in the past. In so doing, a new distressed secondary market for leveraged loans emerged, consisting of both traditional (bank) and non-traditional (non-bank) buyers. Banks were not simply originators of these loans but now were also loan traders, and thus, in their role as market makers, began to provide liquidity for the market.

Although leveraged lending volume in the primary market had reached approximately $100 billion by 1995, trading activity was still relatively low, standing at approximately $40 billion.[6] The early bank loan trading desks at this time initially acted more as brokers than traders, simply brokering or matching up buyers and sellers of loans. As liquidity improved and the lender base expanded, investors began to look to the secondary market as a more effective platform from which to manage their risk exposure to loans, and eventually active portfolio management through secondary loan trading was born. With the advent of this new and vibrant secondary loan market, there naturally was a greater need for standard trading documents and market practices which could service a fair, efficient, liquid, and professional trading market for commercial loans – a need reflected in the LSTA's creation in 1995. (The LSTA and its role in the development of a more standardised loan market are discussed more fully below, under "The Standardisation of a Market".)

Around the same time, the loan market acquired investment tools similar to those used by participants in other mature markets, for example, a pricing service, bank loan ratings, and other supporting vendor services. In 1996, the LSTA established a monthly dealer quote-based secondary mark-to-market process to value loans at a price indicative of where those loans would most likely trade. This enabled auditors and comptrollers of financial institutions that participated in secondary trading to validate the prices used by traders to mark their loan positions to "market". Within a few years, however, as leveraged lending topped $300 billion and secondary trading volume reached $80 billion, there was a need to "mark-to-market" loan positions on a more frequent basis.[7] In 1999, this led to the LSTA and Thomson Reuters Loan Pricing Corporation jointly forming the first secondary mark-to-market pricing service run by an independent third party to provide daily U.S. secondary market prices for loan market participants. Shortly thereafter, two other important milestones were reached, both of which facilitated greater liquidity and transparency. First, the rating agencies began to make bank loan ratings widely available to market participants. Second, the LSTA and Standard & Poor's together created the first loan index, the S&P/LSTA Leveraged Loan Index (LLI), which has become the standard benchmarking tool in the industry. Just as the market's viability was on the rise, so was its visibility. In 2000, the Wall Street Journal began weekly coverage of the syndicated loan market and published the pricing service's secondary market prices for the most widely quoted loans. All these tools – the pricing service, the bank loan ratings, the loan index, and the coverage of secondary loan prices by a major financial publication – were important building blocks for the loan market, positioning it for further successful growth.

At about this time, the scales tipped, and the leveraged loan market shifted from a bank-led market to an institutional investor-led market comprised of finance and insurance companies, hedge, high-yield and distressed funds, loan mutual funds, and structured vehicles such as collateralised loan obligations or "CLOs". Between 1995–2000, the number of loan investor groups managing bank loans grew by approximately 130 per cent and accounted for more than 50 per cent of new deal allocations in leveraged lending. By the turn of the millennium, leveraged lending volume was approximately $310 billion and annual secondary loan trading volume exceeded $100 billion as illustrated in the chart below. With these new institutional investors participating in the market, the syndicated loan market experienced a period of rapid development that allowed for impressive growth in both primary lending and secondary trading.

US Secondary Trade Volume Hits Record $635B in 2017

Source: LSTA

Unfortunately, as the credit cycle turned and default rates increased sharply in the early 2000s, there was a temporary lull in the market's growth, with secondary loan trading stalled for a number of years. By 2003, however, leveraged lending (and trading) volumes quickly rebounded as investor confidence was restored.

Even the most bullish of loan market participants could not have predicted the rate of expansion that would take place over the next four years. Once again, this growth was driven by M&A activity and large LBOs. Increasing by nearly 200 per cent from 2003–2007, leveraged loan outstandings were more than half a trillion dollars and secondary trading volumes reached $520 billion. Although hedge funds, loan mutual funds, insurance companies, and other investor groups played a large part in this phase of the loan market's expansion, the growth had only been possible because of the emergence of CLOs. This structured finance vehicle changed the face of the leveraged loan market and was also responsible for its revival after the Global Financial Crisis.

The 2008 Global Financial Crisis led to a recession in the United States, a contraction of global supply and demand, and record levels of default rates. Several years passed before leveraged lending issuance was restored to pre-crisis levels, finally reaching $665 billion in 2012. Although secondary trading activity had been in steady decline from 2008 through 2012, the asset classes' investment thesis (senior secured, floating rate, high risk-adjusted return) coupled with the investment tools put in place years earlier and the standardisation of legal and market practices helped the market to expand further during its next phase which began in 2013. Since 2013 annual secondary loan trade volumes have grown almost without interruption. 2014 saw an all-time high of $628 billion – a record just broken again in 2017 with $635 billion in annual loan trade volume. This large volume of loan trading together with the record loan issuance of $1.4 trillion seen in 2017 ushered in 2018 on a positive note.

The Standardisation of a Market

No regulatory authority directly oversees or sets standards for the trading of loans in the United States, although, of course, loan market participants themselves are likely to be subject to other governmental and regulatory oversight. Instead, the LSTA leads the loan market by developing policies, guidelines, and standard documentation and promoting just and equitable market practices. The LSTA's focus is attuned to the distinctive structural features of the loan market which stem from the fact that corporate loans are privately negotiated debt obligations that are issued and traded subject to voluntary industry standards. Because the LSTA represents the interests of both the sellers and buyers of leveraged loans in the market, it serves as a central forum for the analysis and discussion of market issues by these different market constituents and thus is uniquely placed to balance their needs and drive consensus.

Loan market participants have generally adopted the standardised documents and best practices promulgated by the LSTA. The LSTA is active in the primary market, where agent banks originate syndicated loans, and in the secondary market, where loan traders buy and sell syndicated loans. The LSTA has an ever growing library of documents for use in the primary market, including a new form of a complete credit agreement published in 2017, all of which are generally used by market participants. Over the years, the Association has published a suite of standard trading documents: forms or "trade confirmations" are available to evidence oral loan trades made by parties and form agreements are available to document the terms and conditions upon which the parties can settle those trades. The universal adoption of the LSTA's standard trading documents by the market has directly contributed to the growth of a robust, liquid secondary market.

It is customary for leveraged loans to be traded in an over-the-counter market, and, in most instances, a trade becomes legally binding at the point the traders orally agree the material terms of the trade. Those key terms are generally accepted as including the borrower's name, the name, facility type, and amount of the loan to be sold, and the price to be paid for the loan. For commercial reasons, most U.S. borrowers choose New York law as the law governing their credit agreements, and for similar reasons, the LSTA has chosen New York as the governing law in their trading documentation. Since 2002, loan trades agreed over the telephone, like agreements relating to derivatives contracts and certain other financial instruments, have benefited from an exemption from a New York law which would otherwise require them to be set forth in a signed writing to be enforceable. Because of the LSTA's lobbying efforts, the applicable New York law was changed in 2002 to facilitate telephone trading. Thus, provided both parties have traded together previously on LSTA standard documentation, even if one party fails to sign a confirmation evidencing the terms of the trade, the loan trade will be legally binding and enforceable, if it can be shown that the parties orally agreed the material trade terms. This was a critical legislative reform that contributed to legal certainty in the loan market and harmonised its status with that of other asset classes.

After agreeing the essential trade terms, loan market practice requires that parties then execute a form of LSTA trade confirmation (the legislative change discussed above merely makes it possible legally to enforce an oral trade even if a confirmation has not been signed). Loans can be traded on what is referred to as par documentation or on distressed documentation. Two forms of trade confirmations are available for this purpose and the choice of which one to use is a business decision made at the time of trade. Performing loans, where the borrower is expected to pay in full and on a timely basis, are typically traded on par documentation which means that the parties evidence their binding oral trade by executing an LSTA Par Confirmation and then settling the trade by completing the form of Assignment Agreement provided in the relevant credit agreement (the term par is used because performing loans historically traded at or near par). Alternatively, where a borrower is in, or is perceived to be in, financial distress or the market is concerned about its ability to make all interest payments and repay the loan in full and on a timely basis, parties may opt to trade the borrower's loans on distressed documentation. In this case, the trade is documented on an LSTA Distressed Confirmation, and the parties settle the transaction by executing the relevant assignment agreement and a supplemental purchase and sale agreement. The LSTA has published a form agreement for this purpose which has been refined over the years and is generally used by the market. This agreement includes, amongst other provisions, representations and warranties, covenants, and indemnities given by seller and buyer. The adoption of standard documents in this regard, particularly for distressed debt trading, significantly contributed to a more liquid loan market, for market participants, knowing that an asset is being traded repeatedly on standard documents, can then uniformly price the loan and more efficiently settle the trade.

When a loan is traded, the existing lender of record agrees to sell and assign all of its rights and obligations under the credit agreement to the buyer.[8] In turn, the buyer agrees to purchase and assume all of the lender's rights and obligations under the credit agreement. The parties must then submit their executed assignment agreement to the administrative agent which has been appointed by the lenders under the credit agreement. The borrower's and agent's consent is typically required before the assignment can become effective. Once those consents are obtained, the agent updates the register of lenders, and the buyer becomes a new lender of record under the credit agreement and a member of the syndicate of lenders.[9]

If, for some reason, the borrower does not consent to the loan transfer to the buyer, the parties' trade is still legally binding under the terms of the LSTA's Confirmation and must be settled as a participation.[10]

The LSTA has published standardised par participation agreements and distressed participation agreements which may be used to settle par and distressed trades, respectively, where loan assignments are not permissible. Under this structure, the seller sells a 100 per cent participation interest in the loan to the buyer and retains bare legal title of the loan. Although the seller remains a lender of record under the credit agreement and the borrower will not typically be aware that a participation interest in the loan has been sold, the seller must pass all interest and principal payments to the buyer for so long as the participation is in place. The transfer of a participation interest on LSTA standard documents is typically afforded sale accounting treatment under New York law. Thus, if the seller of the participation becomes a bankrupt entity, the participation is not part of the seller's estate, and the seller's estate will have no claim to the participation or the interest and principal payments related thereto.

The LSTA continues to expand its suite of trading documents and has increasingly played a more active role in the primary market. Building on the recent publication of the *LSTA's Complete Credit Agreement Guide*, in 2017, the LSTA released its first form of a complete credit agreement, an unsecured revolving credit facility designed to be used by investment grade borrowers, and plans to produce a complete credit agreement for leveraged finance transactions (this will be based on its existing Model Credit Agreement Provisions) in 2018. Finally, the LSTA is also expanding its suite of documents for making, trading, and settling loans to borrowers domiciled in certain jurisdictions in Latin America.

Leveraged Lending Guidance: Is Regulatory Headwind Easing?

The Leveraged Lending Guidance ("LLG") has had a significant effect on banks that underwrite loans and on the loan market generally. The LLG was not styled by the U.S. banking regulators – the OCC, the Federal Reserve and the FDIC – as a "rule" but many observed that it has been largely applied as such since its implementation in 2013. In addition to rigorous reporting and monitoring requirements, the LLG identifies certain criteria to be considered in developing an institution's "leveraged lending" definition, including whether a loan's leverage exceeds 3X senior debt or 4X total debt to EBITDA. It further restricts banks from originating – defined broadly to include amendments and refinancings – a "non-pass" credit. While noting in the LLG that loans with a leverage ratio of greater than 6X raise concerns, the regulators' focus has been on whether a company can show the ability to pay back half their debt from free cash flow in five to seven years. In the years following the LLG's release, the banks have endeavoured to comply with the LLG and as conformance has taken hold, the loan market has seen banks retreat from deals for which there was market demand, but which would not pass regulatory muster. This bank retrenchment has created opportunities for unregulated lenders and direct lenders have been writing bigger cheques and playing in the large cap space. The LLG has certainly changed bank behaviour in the U.S. and we will see if those changes are observed in Europe now that the European Central Bank's guidance on leveraged lending transactions went effective in November 2017.

Europe's recent step toward increased regulation is in contrast to the shifting regulatory sentiment in Washington, D.C. under the new administration and newly-appointed heads of the banking agencies. In a remarkable development, the U.S. Government Accountability Office ("GAO"), in response to a request by U.S. Senator Pat Toomey last spring, determined in October 2017 that the LLG actually was a "rule" in guidance's clothing subject to Congressional review (and possible disapproval) under the Congressional Review Act ("CRA"). Through the CRA, Congress is then given 60 legislative days to invalidate the LLG, if it wishes to do so, by passing a resolution disapproving the LLG and sending that resolution to the president for his signature. While the likelihood that Congress will pass such a resolution is uncertain, the process itself has seemingly opened the door for improvements to the LLG. Last December, the three U.S. banking agencies sent letters to Congressman Luetkemeyer, Chairman of the U.S. House Financial Services Subcommittee on Financial Institutions and Consumer Credit, stating that they are considering soliciting public comment on the LLG in the near term to improve clarity of the LLG and reduce undue burden. This decision was perhaps informed by the U.S. Treasury Department's report recommending that the agencies re-issue the LLG for public comment and refine it. If Congress does not act to invalidate the LLG, it seems likely the *status quo* remains intact. But even then, the new guard at the banking agencies may well take a lighter touch toward enforcement in applying the LLG. As market participants wait for the agencies to reopen the LLG for public comment, some observe that, with looser terms and instances of aggressive leverage levels seen in 2017, some players in the market may now be anticipating that the LLG will be loosened. Whether this is in response to a perceived change in regulatory tone or merely in response to extreme competitive pressures in the market is difficult to ascertain. We hope to see clarity on the LLG – one way or another – in 2018.

Aside from the regulatory uncertainty surrounding the LLG, the market is grappling with the uncertainty that LIBOR will continue to be the prevailing benchmark of the corporate loan market (and broader financial markets). Although the UK's Financial Conduct Authority, the regulator of ICE LIBOR, has announced that panel banks have agreed to submit quotes through 2021, many believe that LIBOR will be phased out in the coming years. When, and if, the financial markets transition to a new benchmark, there are many conversion issues to consider with respect to legacy deals. In addition to including the flexibility to transition to a new rate in credit agreements being signed today, the loan market is beginning to work on answering the larger questions around how to ensure the new benchmark is equivalent to LIBOR. To help the loan market in this process, the LSTA has joined the business loans and CLO working group organised by the Fed-sponsored Alternative Reference Rates Committee tasked with spearheading the transition away from LIBOR. There is much work to be done and that work is only just beginning, but certainly this topic will continue to be at the forefront of many market participants' minds in 2018.

Conclusion

Today's loan market certainly looks very different from that before the financial crisis. We are experiencing a new and more challenging period, not only for investors but also for the LSTA. Loan prices are now said to be closely correlated to, and no longer shielded from, the daily price fluctuations of other asset classes. Although that is true, the risk-adjusted returns of leveraged loans are still advantageous. In this environment, the LSTA remains committed to promoting a fair, efficient and liquid market for loans and maintaining its position as the market's principal advocate.

Endnotes

1. Thomson Reuters Loan Pricing Corporation.
2. Thomson Reuters Loan Pricing Corporation. "Leveraged" is normally defined by a bank loan rating by Standard & Poor's of BB+ and below (by Moody's Investor Service, Ba1 and below) or, for non-rated companies, typically an interest rate spread of LIBOR +125 basis points.
3. For a more detailed description on the loan market sectors, see Peter C. Vaky, Introduction to the Syndicated Loan Market, in *The Handbook Of Loan Syndications & Trading*, 39 (Allison Taylor and Alicia Sansone, eds., 2007); Steve Miller, Players in the Market, in *The Handbook Of Loan Syndications & Trading*, *supra*, 47.
4. Thomson Reuters Loan Pricing Corporation.
5. For a more detailed description of the history of the loan market, see Allison A. Taylor and Ruth Yang, Evolution of the Primary and Secondary Leveraged Loan Markets, in *The Handbook Of Loan Syndications & Trading*, *supra*, 21.
6. Thomson Reuters Loan Pricing Corporation.
7. Thomson Reuters Loan Pricing Corporation.
8. For a detailed comparison of assignments and participations, see Michael Bellucci and Jerome McCluskey, *The LSTA's Complete Credit Agreement Guide*, 2nd ed., 541–542 (McGraw-Hill 2016).
9. For further information on the structure of assignments, see *id*. at 543–561.
10. For further information on the structure of participations, see *id*. at 561–567.

Acknowledgment

The authors would like to acknowledge the invaluable assistance of their colleague Tess Virmani in the preparation of this chapter.

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Mr. Basta received an M.B.A. from the Zicklin School of Business at Baruch College and a B.A. in Accounting from Long Island University.

LSTA

Since 1995, the Loan Syndications and Trading Association has been dedicated to improving liquidity and transparency in the floating rate corporate loan market. As the principal advocate for this asset class, we aim to foster fair and consistent market practices to advance the interest of the marketplace as a whole and promote the highest degree of confidence for investors in floating rate corporate loans. The LSTA undertakes a variety of activities to foster the development of policies and market practices designed to promote just and equitable marketplace principles and to encourage coordination with firms facilitating transactions in loans and related claims. For more information, please visit www.lsta.org.

Loan Market Association – An Overview

Loan Market Association

Nigel Houghton

Loan Market Association

Founded in late 1996, the Loan Market Association ("LMA") is the trade body for the syndicated loan market in Europe, the Middle East and Africa (EMEA).

The LMA's principal objective is to foster liquidity in the primary and secondary loan markets, a goal which it seeks to achieve by promoting efficiency and transparency, by the establishment of widely accepted market practice and by the development of documentation standards. As the authoritative voice of the syndicated loan market in EMEA, the LMA works with lenders, law firms, borrowers and regulators to educate the market about the benefits of the syndicated loan product, and to remove barriers to entry for new participants.

The purpose of this chapter is to give the reader insight into the background and development of the LMA, the scope of its work, and recent and current initiatives.

Background to the LMA

Banks have bought and sold loans for decades but standard market practice is still relatively recent.

Growth in borrowing requirements in the 1970s had seen loan facilities traditionally provided on a bilateral basis, increasingly replaced by larger credit lines from a club of lenders, and then by loan facilities syndicated to the wider market. In the US in the 1980s, a more formal secondary market evolved in parallel with demand on banks' balance sheets and into the 1990s also with the proliferation of non-bank lenders hungry for assets. Proprietary loan trading began to increase and crossed the Atlantic into Europe initially via London-based units of US banks.

By the mid-90s, the secondary market in Europe had itself evolved to become of increasing importance to banks looking to manage their loan book more proactively, be it for single client exposure reasons, return on equity or otherwise. Proprietary trading added to its growing relevance. Despite this, it was evident to practitioners that the market, as it was at the time, lacked any standard codes of practice, and was inefficient and opaque. In response, a group of banks agreed to form a market association tasked with promoting transparency, efficiency and liquidity and, in late 1996, the LMA was formed.

Initial Focus and Development

Within a few years of inception, the LMA had introduced standard form secondary trade documentation for performing loan assets and distressed debt, proposed standard settlement parameters and built out a contributor-based trading volume survey. Based on the success of the Association's secondary market initiatives, its remit was then broadened to cover primary, as well as secondary, loan market issues.

Just two years after it was founded, LMA membership had grown from an initial seven founding bank practitioners to over 100 institutions. Steady growth since then has seen the membership base expand to 674 in 2017, including banks, non-bank institutional investors, law firms, ratings agencies and service providers from 62 countries.

The evolution of the market from the mid 90s to today and the requirements of its increasingly diverse membership have seen the LMA's work become broadly subdivided into the following categories:

- Documentation.
- Market practice and guidelines.
- Advocacy and lobbying.
- Education and events.
- Loan operations.

An overview of each category, a brief market overview and outlook summary are given below.

Documentation

From secondary to primary

Following widespread adoption of the LMA's secondary trade documentation as the European market standard, focus was turned to primary documentation. A recommended form of primary documentation was developed by a working party which included LMA representatives and those of the UK-based Association of Corporate Treasurers (ACT), the British Bankers' Association (BBA), as well as major City law firms, with documents first launched in 1999. Involvement of the ACT and BBA from the outset played a major role in achieving broad acceptance of the LMA recommended forms among borrowers and lenders alike. This success was complemented by the subsequent addition of other forms of primary documentation, including a mandate letter and term sheet.

Following the English law recommended forms in terms of format and style, French law (2002) and German law (2007) versions of investment grade primary documentation were later developed, further broadening general acceptance of LMA standards.

From corporate to leveraged and beyond

The increasing importance of the European leveraged loan market in the early 2000s saw the Association also focus on the development of standardised leveraged loan documentation, with recommended forms agreed in early 2004.

All proposed forms of documentation produced by the LMA are to be regarded as a starting point for negotiations, with the expectation that the more complex the transaction, the more tailoring will be required. This notwithstanding, the fact that all documents have been developed after extensive consultation with market practitioners has led to the recommended documents being viewed as a robust framework upon which to base subsequent individual negotiations. This is particularly true of the leveraged document, where significant input was also sought from non-bank investors within the membership via an institutional investor committee.

As the financial crisis of 2007 began to bite, work commenced on a recommended form of intercreditor agreement, a document generally bespoke to the structure of each transaction. Launched in 2009, the document met with market-wide acclaim again as a robust framework and as the product of comprehensive discussion by market practitioners. As the leveraged market evolved post-crisis, so did the suite of LMA template documents. 2013 saw the launch of an intercreditor agreement and super senior revolving credit facility for use in conjunction with a high yield bond. These were complemented in 2014 with a second super senior intercreditor agreement, for use alongside a super senior RCF, senior secured note and high yield note structure.

Historically, the LMA's principal focus has been on documentation relating to corporate investment grade and leveraged loans, alongside a full suite of secondary loan trading documentation. However, in recent years, and in response to member demand, the association has significantly expanded its coverage, both from a product and geographical perspective, the latter particularly with developing markets in mind.

In 2012, a commercial real estate finance document for multi-property investment was launched, as well as a facility agreement for developing markets and a pre-export finance facility agreement. 2013 saw the launch of a single property development finance facility agreement and four further facility agreements intended for use in developing markets transactions. The LMA continued to expand its suite of documentation in these areas in 2014, with the publication of a real estate finance intercreditor agreement, also facility agreements for use in South Africa, Kenya, Tanzania, Uganda and Nigeria.

In early 2014, the association published a guide to *Schuldschein* loans, the result of extensive collaborative work by a working party based in Germany. Appropriately, the guide was published in German with an English translation. An updated version was published in August 2016.

Following positive feedback from members on the Schuldschein project and in response to member demand, work commenced on the production of a standard form private placement document, with documents in both loan and note format launched in January 2015. The project benefitted from the involvement of the International Capital Market Association (ICMA) and the ACT. This provided valuable input particularly on the note format (developed in coordination with ICMA) and on borrower/issuer concerns (in the case of the ACT).

The LMA initiative is a significant contribution to the development of a European private placement market particularly when seen in the context of the current work of the Pan-European Private Placement Working Group coordinated by ICMA, which also includes the Euro PP Working Group (composed of all relevant professional organisations and participants in the French market). The Euro PP Working Group has also produced French law private placement documents to complement the French Charter for Euro Private Placements released in 2014.

2015 saw the publication of a term sheet for use in pre-export finance transactions, a secured single currency term facility agreement governed by South African law and a real estate finance German law facility agreement. Later that year, the LMA published a recommended form of clause for inclusion in non-EU law governed facility agreements to the extent required by Article 55 of EU Directive 2014/59, the Bank Recovery and Resolution Directive.

2016 releases included a new security agreement and contractually subordinated intercreditor agreement for use in real estate finance, a German language German law facility agreement and term sheet for multi-property real estate transactions and an insurance broker letter also for use in real estate finance.

In 2017, the LMA further expanded its suite of documentation with the publication of fronted agreements for leveraged acquisition finance transactions, a mezzanine facility drafting guide for leveraged finance transactions, template Italian law private placement documentation and a confidentiality agreement governed by South African law.

Looking ahead to 2018, documentation projects once again reflect the breadth of the LMA's remit across EMEA. Work will commence on a security agreement for use across common law jurisdictions in Africa and a South African law mandate letter. Work will continue on the production of an ECA buyer credit facility agreement, a new confidentiality letter to address disclosure to credit risk insurers (along with a confidentiality agreement user guide) an intercreditor agreement for use alongside combined institutional unitranche and bank lending transactions and a mezzanine facility drafting guide for real estate finance transactions. Following renewed discussions with an expanded working group, work will also be undertaken on a recommended form of Schuldscheindarlehen document, alongside an amended product guide.

Brexit: while the UK referendum vote in June 2016 to leave the EU will have a major impact on the future financial landscape in the UK and Europe, in the vast majority of cases it does not bring about any immediate legal or contractual change. It is too early to speculate on the implications for the syndicated loan market of the UK's withdrawal from the EU and much will depend on the form of negotiated exit. Needless to say, the LMA is closely following developments and will, in due course, address any documentary changes. In the meantime, however, a note has been published addressing a number of considerations for LMA facility documentation.

LIBOR: in July 2017, the Chief Executive of the UK Financial Conduct Authority gave a speech about the future of LIBOR, noting that market participants should not rely on LIBOR being available after 2021 (see Advocacy and Lobbying below). Clearly the adoption of a replacement benchmark rate would have wide ranging implications across the loan market and would impact the technical workings of LMA documentation. Study and discussion are ongoing and at the time of writing there is no obvious alternative to LIBOR for the syndicated loan market. Until a suitable alternative benchmark rate is identified and accepted by market participants, LMA recommended form documentation cannot be updated to reflect a new benchmark rate. However, we are reviewing our documentation to assess what can helpfully be done to facilitate transition to a new rate once identified.

Review and development

In response to member feedback, market developments, legislation and regulation, the LMA's document library is constantly reviewed and updated. Primary and secondary recommended forms have undergone several revisions and seen some significant amendments, a notable example being the combination of secondary par and distressed trading documents in 2010, updated once again in 2012. Continuing the theme, terms & conditions for secondary loan trading were subject to a full "Plain English" review in 2013 with the goal of making these more navigable, particularly for those whose native language is not English. Further revisions to secondary terms & conditions were subsequently agreed including, *inter alia*, clarification of treatment of notary fees and to reflect, amongst other things, recent changes to ERISA.

In late 2014, revised primary facility agreements were published, *inter alia*, to facilitate the use of non-LIBOR interest rate benchmarks following the discontinuance of certain tenors and currencies. In 2015, anti-trust amendments were incorporated into mandate letters and the confidentiality and front running letter for primary syndication. French, German and South African law investment grade templates have all been updated and general updates were published to the suite of documents to reflect legal and market issues, such as changes in the accounting treatment of leases (IFRS 16) and the new ICE LIBOR submission methodology. Leveraged documentation was also recently revised to include, among other things, an optional incremental facility. In 2018, the LMA also intends to publish amendments to its developing markets suite of facility agreements (to include, amongst other things, a letter of credit option) and private placement documents (to include a US investor rider).

Market Practice and Guidelines

LMA guidelines are widely regarded as defining good market practice and typically address those aspects of loan market business not specifically documented between parties. Guidelines produced include those covering the use of confidential information, a guide to waivers and amendments and transparency guidelines.

The first in a series of market guides, Regulation and the Loan Market, published late 2012, met with considerable interest from the membership. This publication has subsequently been updated on several occasions to reflect ongoing regulatory developments. Other guides in the series include Insolvency in the Loan Market, Using English Law in Developing Markets, Guide to Syndicated Loans and Leveraged Finance Transactions, Glossary of Terms for Transfers of Interests in Loans, a Guide to Agency Protections, a Guide to Secondary Market Transactions and a Guide to Secondary Market Liquidity. A Comparison of Private Placement Debt Products was published in July 2016. In 2017, a Guide to Dealing with Request for Amendments was released, also an Introduction to Position Reconciliation and a paper on Why We Need Identifiers. Most recently in early 2018, after significant input from members of the Loan Operations Committee, the LMA published An Agent's Guide to Handling Ancillary Facilities.

The LMA has recently established a Green Lending Committee, with a view to producing a set of green lending principles. This will consist of a high level framework, setting out a series of market standards and guidelines, which will aim to create a consistent methodology to apply in every "green" lending transaction. The overarching aim of the principles is to allow the loan product to retain its flexibility, whilst ensuring the integrity of the development of a green lending market. The principles will aim to closely follow the four core components of ICMA's Green Bond Principles.

Advocacy and Lobbying

The LMA seeks to maintain a dialogue with regulators and government bodies wherever new or revised regulatory proposals may impact the loan market, whilst also proactively promoting the market as a core funding source in the corporate economy. Since the financial crisis of 2007, this area of the Association's work has grown in importance as the number of regulatory proposals has dramatically increased. Policy decisions underlying the new proposals are largely to be supported, the overarching aim being a more robust financial system better able to shoulder economic shock and withstand periods of stress. The LMA's lobbying focus has been on the potentially negative implications of these proposals for the loan market, both intentional and unintended, and the effects on its members. Responses to regulatory bodies across the globe are too numerous to list.

Notable dialogue over recent years includes submissions re the impact of the EU Capital Requirements Directive (CRD IV) on bank financing, to the OECD consultation re Base Erosion and Profit Shifting (BEPS), the EC consultation on European Capital Markets Union and submissions to the EC, PRA and FCA re the Article 55 bail-in directive. Also to highlight are responses to the Financial Stability Board, EC and EBA consultations on strengthening oversight and regulation of both banking and shadow banking, a response to the HMRC consultation re tax deductability of loan interest payments and lobbying the EU on its framework for simple, transparent and standardised securitisations. The LMA had previously successfully lobbied for lower risk retention requirements for new CLOs in the post-crisis era.

Anti-money laundering and counter-terrorist financing measures have been the subject of several recent submissions to the ESA and HM Treasury and the LMA has most recently drafted a proposed revision to the Joint Money Laundering Steering Group's guidelines. A submission was made to the FCA in September 2016 on the potential impact of Brexit on the loan market and in January 2017 to the ECB on its leveraged lending guidelines.

On the subject of the potential replacement of LIBOR from 2021, the LMA is in active dialogue with the Bank of England and the FCA to ensure that the interests of the loan market are represented. The LMA has submitted a response to the Bank of England's SONIA White Paper, outlining the issues posed by using the Sterling Overnight Index Average in the syndicated loan market. We are also a member of the term rate working group which has been established to consider the production of a SONIA term rate. We have also responded to the Federal Reserve Bank's Request for Information on SOFR (Secured Overnight Funding Rate), given the importance of U.S. dollar LIBOR in the EMEA loan market. Given the importance of a consistent approach being adopted across the financial markets, the LMA has also brought together relevant trade associations in the financial markets to discuss a coordinated way forward. We are working in particular with the other loan trade associations (namely the LSTA and APLMA), as well as ICMA, ISDA, AFME and others. The ACT is also involved in this group to ensure borrower input.

Significant progress has been made by the LMA in reducing the impact of regulation on the loan market and its participants; however, undoubtedly changes in the regulatory and fiscal landscape will continue to present challenges into 2018 and beyond. The LMA remains committed to play a pivotal role in tracking these changes and their potential impact on the loan product.

Education and Events

As a core objective, the LMA seeks to educate members and others regarding documentation and legislative, regulatory, legal, accounting, tax and operational issues affecting the syndicated loan market in EMEA. As the industry's official trade body, the LMA is the ideal education and training resource for what has become an increasingly technical market. Relationships with the key players in the market afford the LMA access to some of the leading experts in their field and as such the credentials of contributors can be guaranteed.

Evening seminars and documentation training days are regular calendar events in the UK. Also, to reflect the multi-jurisdictional membership base, seminars, training days and conferences are held in many other financial centres, including Frankfurt, Paris, Amsterdam, Brussels, Milan, Madrid, Vienna, Zurich, Stockholm, Istanbul, Moscow, Dubai, Nairobi, Lagos, Johannesburg and New York.

In September 2017, over 900 delegates attended the LMA's 10th annual Syndicated Loans Conference in London, the largest loan market event in EMEA. Additionally, the LMA now also runs a joint LMA/LSTA Conference in London, an annual Developing Markets Conference in London, an annual Real Estate Conference in London and Frankfurt/Munich, and conferences in East and South Africa. In total, over 17,000 delegates have attended LMA events in the last three years.

In 2005, the inaugural LMA Certificate Course was held in London. Consistently oversubscribed, the course is now entering its 12th year and will be run three times in 2018. Held over five days, the course covers the syndication process through to secondary trading, including agency, portfolio management, pricing and mathematical conventions, terms sheets and an introduction to documentation.

The Syndicated Loans Course for Lawyers is a two-day programme, designed specifically for those working in the legal profession, providing detailed tuition on all aspects of the primary and secondary loan markets.

A Loan Documentation Certificate Course was launched in 2016, affording professionals a more in-depth understanding of LMA primary documentation. A Real Estate Finance Certificate Course was also launched, aimed at junior professionals in that sector.

In 2011, the LMA published The Loan Book, a comprehensive study of the loan market through the financial crisis, with contributions from 43 individual market practitioners. Over 10,000 copies of The Loan Book have been distributed to date since publication. In 2013, the association published Developing Loan Markets, a volume dedicated to the analysis of various regional developing markets, both from an economic and loan product perspective. Adding to the series, the Real Estate Loan Book was published in May 2015. In recognition of the 20th anniversary of the LMA, the latest book – 20 Years in the Loan Market – was published in November 2016. Again the result of contributions from leading practitioners from across the market, the publication looks back at the last two decades of the syndicated loan market, analysing its evolution over that period.

In August 2015, the LMA launched a webinar programme, offering members across the globe access to training on demand, with concise and comprehensive tutorials across a range of topics presented by senior industry professionals. The programme expanded in terms of coverage in 2016 to include sessions in French, German and Spanish. At the time of writing there were 26 webinars available to view.

Working in close collaboration with the LMA Operations Committee (see below), in October 2016 the LMA launched its first e-learning programme, Understanding the Loan Market. Aimed at practitioners across the market, be it from a legal, financial or operations background, the course seeks to create a knowledge benchmark for the asset class. The course consists of 10 modules in total and is free of charge for LMA members. To date over 4,000 delegates from 60 jurisdictions have registered on the dedicated e-learning portal.

Loan Operations

Operational issues have long been raised by LMA members as an area of concern, particularly around administrative agency and the potential for significant settlement delays in the secondary market. Syndicate size alone can lead to process overload when waivers and amendments are combined with transfer requests. The LMA has a dedicated Loan Operations Committee focused on identifying roadblocks, communicating issues and promoting best practice solutions. Several administrative "quick-wins" have been implemented across top agency houses since 2014 as a direct result of the Committee's work. Since Q4 2014, the LMA has consolidated and published secondary trade settlement statistics from major European trading desks in order to help benchmark efficiency gains going forward.

In June 2017, the LMA held its 3rd Loan Operations Conference to showcase the work of the committee and highlight issues faced by operations teams across the market.

Financial technology ("fintech") is high on the agenda at most major financial institutions and the LMA is engaged with banks, lawyers and vendors alike to understand the potential implications of innovative technology such as Blockchain, in particular as it may impact operational processes in the medium term. Fintech discussions are now regular features at LMA seminars and a dedicated extended seminar is planned for 2018.

Maintaining the spotlight on secondary settlement and operations in general is a core strategic aim for the LMA into 2018 and beyond.

Market Overview

A detailed study of the development of the syndicated loan market in EMEA, particularly post the financial crisis of 2007–2009, is beyond the scope of this chapter. The Loan Book, as mentioned above, gives a practitioner's overview and detailed reference guide, as does the LMA's latest publication 20 Years in the Loan Market. It goes without saying, however, that the crisis sparked by the US sub-prime mortgage market had a significant impact. Fuelled by an abundance of liquidity, particularly from institutional investors in the leveraged market, primary volumes in EMEA soared in the years building up to the crisis. The liquidity crunch saw primary issuance fall dramatically by 2009 to barely one-third of the record $1,800BN seen in 2007. Volumes recovered some ground through to 2011 but dipped again in 2012 against the backdrop of the Eurozone sovereign debt crisis and the US "fiscal cliff." In contrast, 2013 saw markets rebound and loan issuance increase substantially. Policy intervention and specifically the Outright Monetary Transactions programme announced by the ECB in the 2nd half of 2012 was a significant driver of confidence. In 2015, EMEA total loan market volumes reached $1,400BN for the first time since the crisis. EMEA volumes have dipped slightly since then and stood at $1,125BN in 2017. Reduced volume overall is no measure of lending appetite, however. Most recently, in 2018, a reported $100BN in loan commitments has been raised for the proposed Broadcomm acquisition of Qualcomm, a new global record (US-led) and underlining the liquidity available in the loan market 10 years after the crisis.

Demand for the leveraged loan product in particular has spread across a broader investor base than seen prior to 2007. Credit funds and managed accounts now have a much larger foothold than previously. A significant driver of demand within leveraged finance pre-crisis, the CLO returned to European markets in 2013 with new vehicle issuance volume of €7.4BN, compared with virtually zero since 2008. European CLO issuance reached a post-crisis high of €20.9BN in 2017.

Institutional investors have also become more visible in other loan asset classes, such as real estate and infrastructure finance. A multitude of funds have also been set up to lend directly to small and medium companies, particularly in the UK. Retrenchment by banks immediately post crisis opened the door to alternative sources of finance across the loan market and many larger institutions are now established participants. Many more managers have raised dedicated loan funds over the last few years and competition for assets is becoming intense, especially as several banks have actively looked to expand activity in the sector.

The Way Forward

Results from a survey of LMA members at the end of 2017 suggest that market participants are cautiously optimistic about prospects into 2018. Some 39% of respondents expect loan market volumes across EMEA to grow at least 10%, versus only 14% predicting lower volumes. Global economic and/or geopolitical risks (including Brexit) were cited as the biggest potential influence on the market in 2018 with 35% of respondents, with competitive pressure very closely behind at 34%. Respondents saw refinancing activity as the main volume driver at 37% of the vote, with new money requirements in corporate M&A at 24%. Asked how much financial regulatory change has impacted their business over the last five years, some 70% have seen a significant or material impact.

Indeed, regulatory issues remain high on the agenda and the LMA's focus on lobbying and advocacy will continue unabated. Other trends will also determine the focus of the LMA's work into 2018 and beyond. The institutional investor base has continued to grow and non-bank finance has increased in importance across loan asset classes, be it in parallel with banks in syndicated lending, in a bespoke bank/fund partnership, via unitranche or other forms of direct lending. More borrowers from developing markets will require funding from beyond domestic boundaries; the LMA will continue and expand its work in these markets to promote the acceptance of regional standards. We expect the focus on operational efficiency to continue to grow and the LMA is fully engaged with partners and practitioners across the market to identify issues, find solutions and broker change. Fintech will undoubtedly evolve to reshape the financial services industry and it will be increasingly important to trade ideas and knowledge in this area.

The LMA's principal objective some 20 years ago was to promote greater liquidity and efficiency in the loan market, an objective which remains as, if not more, relevant today.

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Nigel is Managing Director at the LMA. He has over 20 years' experience in loan markets, from origination and structuring through to sales, trading and workout. Prior to joining the LMA in 2012, Nigel was at GE Capital in London for seven years where he was head of secondary sales & trading for the European leveraged finance business. In 10 years at Commerzbank, Nigel ran the London-based distressed portfolio and was a founding member of the bank's London structured finance & loan syndications team. He served as an LMA Board Member for several years during this time. Nigel began his City career via a graduate programme at Deutsche Bank following training at Coopers & Lybrand Deloitte. Nigel has a BA (Hons) from the University of Durham.

Loan Market Association

the authoritative voice of the EMEA market

The Loan Market Association (LMA) has as its key objective improving liquidity, efficiency and transparency in the primary and secondary syndicated loan markets in Europe, the Middle East and Africa (EMEA). By establishing sound, widely accepted market practice, the LMA seeks to promote the syndicated loan as one of the key debt products available to borrowers across the region.

As the authoritative voice of the syndicated loan market in EMEA, the LMA works with lenders, law firms, borrowers and regulators to educate the market about the benefits of the syndicated loan product, and to remove barriers to entry for new participants.

Since the establishment of the LMA in 1996, the Association's membership has grown steadily and now stands at 640 organisations covering 60 nationalities, comprising commercial and investment banks, institutional investors, law firms, service providers and rating agencies.

Asia Pacific Loan Market Association – An Overview

Asia Pacific Loan Market Association (APLMA)

Katy Chan

About the APLMA

Founded in 1998, the APLMA is a pan-Asian trade association that represents the common interests of the many different institutions active in the syndicated loan markets of the Asia-Pacific region. The APLMA's primary objective is to promote growth and liquidity in the primary and secondary loan markets and works in tandem with its sister associations in Europe and North America to advocate common market standards and practices with a view towards improving global loan market liquidity.

Standard Documentation

One of the core objectives of the APLMA is to produce standard primary documentation for syndicated loan transactions in the Asia Pacific markets. These documents, covering English law, Hong Kong law, Australian law and Singapore law, have become the market standard for Asia. The documents are reviewed and updated continuously to reflect market and regulatory changes.

The APLMA has also developed a number of templates to provide alternative wording for use by members. These include a sample Asia arbitration clause with a litigation option for a hybrid dispute resolution process and a full suite of standard term sheets, mandate letters and confidentiality letters including templates for primary syndication and for sale/sub-participation under both English and Hong Kong law.

New APAC Regulatory Guide

In light of ongoing regulatory changes, the APLMA launched a new Asia Pacific Regulatory Guide in June 2017 which summarises some of the key regulatory changes over the past few years including sections on FATCA, Brexit, Competition Law, Basel III, sanctions, etc. as well as an analysis of how these impact on the syndicated loan market in Asia. This guide is available to all members via the APLMA website.

Documentation Updates

In 1H2017, the Hong Kong Documentation Committee focused on the updates of the following APLMA templates in order to be consistent with the updated English law and Hong Kong law Facility Agreements published in 4Q2016:

- Facility Agreement for Secured Transactions.
- Facility Agreement for Offshore RMB transactions.
- Mandate Letters (updated version completed in 2Q2017).
- Term Sheets (updated version completed in 2Q2017).
- Confidentiality Agreements (updated version completed in 2Q2017).

In 2H2017, the committee also updated the primary suite of Facility Agreements to take into account:

- Recent LMA template updates – the LMA updated its investment grade documentation templates in July 2017 mainly to bring them into line with the leveraged documentation templates of November 2016. The updates include revisions to the representations and undertakings, tax provisions, replacement lenders (increased lender), alternate reference bank rates, etc.
- Regulatory changes – the LMA has produced wording related to "Designated Entity" provisions in respect of Brexit. A footnote will be added to the APLMA templates so that banks can take into consideration such provisions.

The Facility Agreement for Secured Transactions and the Facility Agreement for Offshore RMB transactions will be updated once these revisions are complete.

The Singapore Branch Documentation Committee has revised the Singapore law document based on the revisions to the Hong Kong law facility agreement published in 4Q2016. These will be further updated once the current round of amendments to the Hong Kong law facility agreement are finalised.

The Australian Branch Documentation Committee also published a number of updates to the following Australian law syndicated and bilateral investment grade facility agreements:

- Term and Multicurrency Revolving Syndicated Facility Agreement for multiple borrowers and guarantors.
- Multicurrency Revolving Facility for multiple borrowers.
- Term and Multicurrency Revolving Syndicated Facility Agreement incorporating a letter of credit.
- A$ Revolving Facility for Multiple borrowers and guarantors.
- A$ Term and Revolving Facilities for multiple borrowers and guarantors.
- Term and Multicurrency Revolving Bilateral Facility Agreement.
- Term and Multicurrency Revolving Bilateral Agreement with a letter of credit.

The 2017 updates bring the suite of Australian law facility agreements into line with the Secured Term and Multicurrency Revolving Syndicated Facility Agreement incorporating a letter of credit that was published in December 2016.

The APLMA also published for the first time a Secured Term and Multicurrency Revolving Bilateral Facility Agreement with letter of credit based on the unsecured Term and Multicurrency Revolving Bilateral Facility Agreement incorporating a letter of credit and the secured provisions in the Secured Term and Multicurrency Revolving Syndicated Facility Agreement incorporating a letter of credit.

Agency Issues

In 1Q2017, the Agency Committee hosted two new half-day Introductory and Intermediate Documentation Training workshops in Hong Kong and Singapore tailored specifically for agent banks. The introductory session focused on the role and protection of Agents in the context of syndicated facilities. The intermediate session looked at significant events that may arise during the life of a loan transaction that give rise to special considerations for an agent.

In June 2017, the Agency Committee also formed a new Agency Best Practices Working Group and agreed in principle on the work scope, focusing initially on two new Agency Notes:

i) **KYC Note**: to provide clarity on the Agent's role in respect of KYC and the related provisions in the APLMA documents; and

ii) **Best Practice Note on Borrowers' reporting obligations**: in respect of providing documents such as financial statements, certificates of compliance etc and to clarify the responsibilities of the Agent *vis-à-vis* the Borrower.

The Committee will also review the wording of the e-communications and use of deal site provisions to take into consideration the language adopted in the APLMA Australian law templates.

Education and Training

The APLMA hosted over 100 seminars, conferences, training courses and networking events in 2017 as part of its commitment to enhancing industry education and providing a vibrant pan-Asian professional network. The APLMA hosts events in all the major financial centres in the region, the majority of which are free of charge for Members.

In 2017, inaugural seminars were held in Myanmar, Qingdao and Macau (Documentation Training Seminar and first seminar focused specifically on the Macau market). The event programme will continue to expand in terms of coverage for 2018 to include seminars and conferences in South East Asia and fast-growing cities in China.

The APLMA also continued its commitment to building on its series of events to promote diversity through its Women in the Loan Market Asia (WILMA) events and its training for younger members through the Young Leader's series, both of which saw expanded programmes in 2017.

New Teach-Ins & Webinars

The APLMA broadened the scope of its event programme with the introduction of Teach-Ins in 2017. Covering a wide range of sectors from oil and gas to commodity finance, APLMA Teach-Ins focus on specific industry sectors with a view to expanding market knowledge in a particular field with a spotlight on key issues in relation to the different requirements and structures in order to put together sound transactions. We also hosted a series of Teach-Ins on changes to the regulatory environment.

Another teaching tool the APLMA has developed is the webinar series which is now available on the APLMA website. The webinars are similar to the Teach-In series in that they aim to provide a set of teaching tools for members, but they can be accessed remotely.

The following webinars are now available on the APLMA website (aplma.com):

- Fintech and what it means for the loan market.
- Commodity finance.

APLMA China

The APLMA held its inaugural Loan Market Conference in Qingdao in March 2017. Shandong province has long been an economic powerhouse in China, while Qingdao is the largest city in Shandong by GDP. A major industrial centre, it is also home to some of the leading corporates in China. Recognising the economic importance of the city, the conference helped to foster the relationship between Chinese banks, international banks and the local community.

The conference featured high level speakers from the finance department of the Qingdao Government, local borrowers, bankers and lawyers. The event was well attended with representatives from local and international banks, lawyers, and delegates from government agencies and banking regulatory bodies including representatives from the China Banking Regulatory Commission (CBRC), the Peoples Bank of China (PBOC), the National Development and Reform Commission (NDRC) and the Qingdao Banking Association. The attendees came from various cities including Beijing, Shanghai, other parts of Shandong and Hong Kong.

Sustainable Finance

The APLMA Green Loan Committee conducted a members survey in early 2017 and, based on the results of this survey, concluded that it would be conducive to market development to have a standard definition of what constitutes a green loan, as well as a set of green loan principles for market players in view of the difference in green standards under each jurisdiction in Asia.

The committee reviewed the ICMA Green Bond Principles (GBP) to assess the applicability and practicability of adopting similar guidelines for the loan market. ICMA was invited to join the committee to provide an overview of the development of the green bond market as well as the development and evolution of ICMA's GBP.

The APLMA subsequently joined forces with the LMA and ICMA to form a new Global Green Loan Working Group together with a number of other trade associations. Several members of the APLMA Green Loan Committee participated in the inaugural meeting in June. The aim of the working group is to adapt the ICMA GBP for the loan market in order to establish parameters to facilitate growth in the green loan market. It was agreed that the new green loan market principles should follow the four pillars set out in the GBP, namely:

i) use of proceeds;

ii) process for project evaluation and selection;

iii) management of proceeds; and

iv) reporting.

The GBP also recommend that issuers appoint an external reviewer to confirm that the issuer's own assessment of the alignment of its green bond with the GBP. Members of the new working group were tasked with reviewing the GBP and providing feedback on how these might be adapted for the loan market.

In September, the group met to discuss the drafting of potential Green Lending Principles (GLP). During the meeting a number of key themes were discussed at length which align closely with the four core pillars of the GBP. The group inclined towards producing a high level framework setting market standards and guidelines so as to allow the loan product to retain its flexibility whilst ensuring the integrity of the development of a green lending market.

A further meeting was held in November to discuss and clarify a number of issues around green terms. It was agreed that the definition of green should be consistent between the GBP and GLP to allow free movement between markets and to maintain integrity of the green product. A second draft was then produced and the intention is to publish the first version of the GLP by 1Q2018.

To ensure that the views of all the APLMA Green Loan Committee members were taken into consideration, the APLMA conducted a further survey to solicit feedback on the proposed new GLP.

In Hong Kong, the APLMA also met with the HKMA in September to give an update on its recent green loan initiatives and to look at ways of promoting green finance in the region.

LIBOR Transition

In July 2017, the Financial Conduct Authority (FCA) in the UK announced that it would cease to compel LIBOR panel banks to continue providing quotes beyond 2021. As such, market participants need to prepare themselves for the likelihood that LIBOR will cease to exist by end 2021.

The APLMA documentation contains a number of fallbacks in the event of the unavailability of a "Screen Rate" benchmark. In particular, there is an "optional" provision on "Replacement of Screen Rate" which provides for the replacement of an unavailable screen rate with borrower and majority lender consent. The fallback provisions, however, would have practical limitations in the absence of agreed alternatives to LIBOR.

The APLMA has engaged with a number of parties on this issue and hosted LIBOR reform briefing sessions in Hong Kong and Singapore for members. The APLMA has also joined forces with the LMA and a number of other trade associations to monitor LIBOR fall backs and potential consequences for the syndicated loan market. A new local APLMA LIBOR working group comprising EU and Asian bank members has also been established to review issues and potential practical difficulties encountered by market participants in the region which may arise in the absence of LIBOR.

The new APLMA LIBOR Working Group held its first meeting in October to discuss the initiatives of banks in Asia in respect of tackling the potential discontinuation of LIBOR. While there is no consensus on a suitable alternative rate from the market at present, it was suggested that the APLMA templates could include a possible amendment as a placeholder for a new benchmark rate in the future. The suggestion was brought to the attention of the APLMA Documentation Committee for further discussion.

In 4Q, the APLMA continued its dialogue with the global LIBOR Trade Association Group and finalised a global issues list to be jointly presented in a letter to the Financial Stability Board in Europe with other global trade associations. A copy of the letter will be posted on the APLMA website in due course.

Major Projects 2018

The newly formed APLMA Agency Best Practices Working Group will continue its works in 1Q2018 on drafting new guidance notes for members on the Agents' role in respect of KYC and Borrowers' reporting obligations under APLMA templates to clarify the responsibilities of the Agent *vis-à-vis* the Borrower.

The APLMA Taiwan Documentation Sub-committee is working on the draft of a new APLMA Taiwan Law template to promote the use of standardised documentation in Taiwan. The new template will be synchronised with the standard APLMA forms and will be produced in dual language.

The global Green Loans Working Group comprising the APLMA, LMA, ICMA and other trade associations in the international debt capital markets are actively working to finalise the GLP with the first version expected to be published in early 2018.

Looking Ahead

2018 marks the 20th Anniversary of the founding of the APLMA. To celebrate this important milestone, a 20th Anniversary Party will be held in September in Hong Kong.

With the regulatory landscape constantly changing, the APLMA will continue to monitor fiscal and regulatory developments in the region and publish market guidance notes to assist members in assessing the extent of the potential impact on the loan market. The APLMA has also sought to engage more actively with regulators in the region to monitor fiscal and regulatory developments.

As part of its commitment to enhance industry skills and education and provide members with a vibrant pan-Asian professional network, the APLMA will continue to host regular seminars and conferences in major cities and financial centres across Asia Pacific, including inaugural conferences in Japan, Dubai and Hangzhou in China whilst at the same time expanding the APLMA's presence in frontier markets in the region.

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Katy is a Director at the APLMA, responsible for developing the APLMA's presence in China and Taiwan and building up the APLMA's presence in new markets in Asia. She is also focusing on membership and working with the APLMA committees.

Before joining the APLMA in 2014, Katy was with Standard Chartered Bank in Hong Kong where she managed a portfolio of large international and local corporates. She also worked in project and structured finance at ANZ from 2008 to 2011 and prior to that she was a Director at HSBC where she worked from 2000 to 2008 in various roles including project finance, government advisory and principal investments.

Founded in 1998, the APLMA is a pan-Asian not-for-profit industry association dedicated to promoting growth and liquidity and advocating best practices in the primary and secondary loan markets of the Asia-Pacific region. Its primary objectives include:

- providing standard loan documentation templates;
- formulating guidelines on market practices;
- organising seminars, training and networking events;
- monitoring legislative, regulatory and market changes for impact on the syndicated loan market; and
- serving as a liaison between major loan market players and regional regulators.

The APLMA is headquartered in Hong Kong with a branch in Australia and a management committee in Singapore, as well as offshore committees in China, India, Malaysia, New Zealand and Taiwan. Currently the APLMA has over 300 institutional members from Asia Pacific, Europe, North America and the Middle East. Membership comprises commercial and investment banks, non-bank financial institutions, law firms, rating agencies and financial information service providers.

An Introduction to Legal Risk and Structuring Cross-Border Lending Transactions

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1 Introduction: The Rise of Cross-Border Lending

Increase in Cross-Border Lending. For lenders and lawyers who practise in the cross-border lending area, whether in the developed economies or the emerging markets, this is a dynamic and exciting time. Cross-border lending has increased dramatically over the last couple of decades in terms of volume of loans, number of transactions and number of market participants. According to the Bank for International Settlements, the amount of outstanding cross-border loans held by banks worldwide has increased from approximately $1.7 trillion in 1995 to over $7 trillion today. There are many reasons for this increase: the globalisation of business and development of information technology; the rise of emerging economies that have a thirst for capital; and the development of global lending markets, especially in the US, which has led to a dramatic rise in the number of market participants searching for the right mix of yield and risk in the loan markets, a search that often leads to cross-border lending opportunities.

Challenges of Cross-Border Lending. In addition to understanding the creditworthiness of a potential borrower, the overlay of exposure of a lender to a foreign jurisdiction entails analysis of a myriad of additional factors, the weighting of which will vary from country to country. This mix of political, economic and legal risks, bundled together, is referred to collectively as *country risk*. Understanding country risk is imperative for lenders and investors to be able to compare debt instruments of similarly-situated companies located in different countries.

Examination of Legal Risk. This first overview chapter of the *Guide* provides some observations on an element of country risk that is closest to the hearts of lawyers: *legal risk*. Together with tax considerations, understanding legal risk is important for structuring cross-border loan transactions. But what exactly is legal risk? Can legal risk be measured? What tools do lenders traditionally use to mitigate legal risk? Do these tools work? Finally, we complete this chapter with some observations on how conventional notions of legal risk are being challenged.

2 Legal Risk in the Cross-Border Lending Context

What is Legal Risk? Young lending lawyers are taught that when a loan transaction closes, "the borrower walks away with a pile of the lender's money and the lender walks away with a pile of paper *and the legal risk*". If the borrower refuses to pay the money back, then the lender must rely on the *pile of paper and the legal process*, in order for the money to be returned. This notion helps drive the point home that legal risk is primarily something that keeps lenders (rather than borrowers) awake at night. While there is no settled description of legal risk, it can be thought of as having a number of components, starting with *documentation risk*, which is mitigated by having competent counsel ensure that legal documentation correctly reflects the business arrangement and is in the proper form. In a cross-border lending context it is useful to think of legal risk as having two additional related and sometimes overlapping components: (1) *enforcement risk*; and (2) *the risk of law reform*.

Enforcement Risk. Lenders prefer to enter a lending transaction knowing that a number of "enforcement components" are in place to allow for enforcement of loan documentation (that *pile of paper*) and to resolve disputes and insolvency in a predictable way. These components include a well-developed body of commercial law, an independent judiciary and an expedient legal process. In a cross-border lending context, especially if a borrower's primary assets are located in a foreign jurisdiction, there is typically some reliance by a lender on the laws, legal institutions and legal process of that foreign jurisdiction.

For example, a US lender seeking to enforce a loan agreement against a foreign borrower could do so in one of two ways. Assuming the borrower has submitted to the jurisdiction of New York courts, the lender could file suit in New York against the borrower, obtain a judgment from a New York court, and then seek to have that judgment enforced against the assets of the borrower in the borrower's home country. In the alternative, the lender could seek to enforce the loan agreement directly in the courts of the foreign jurisdiction. In either case, there is reliance on the laws, institutions and legal process in the borrower's home jurisdiction.

If the foreign jurisdiction's local law is not consistent with international norms, or its legal institutions are weak, corrupt or subject to undue political influence, then *enforcement risk* may be considered high. It should be noted that enforcement risk may be high even in a jurisdiction that has modernised its commercial laws if legal institutions have not also matured (the latter taking more time to achieve).

Law Reform Risk. Lenders also want to know that the laws they are exposed to in connection with a loan to a borrower will not arbitrarily change to the lender's detriment. This aspect of legal risk is closely associated with political risk. Law reform risk detrimental to lenders is at its highest when a country is undergoing some sort of systemic crisis. For example, in 2002, during Argentina's financial crises, the government of Argentina passed a law that converted all obligations of Argentine banks in US dollars to Argentine pesos. Given that pesos were only exchangeable at a fixed rate that did not accurately reflect a true market rate, this change in law had the effect of immediately reducing the value of the lenders' loans.

Why Legal Risk Matters. If enforcement risk is high, this weakens a lender's negotiating position in the case of a workout of a loan (as compared to a similarly situated borrower in a country where enforcement risk is low). If law reform risk is high, lenders risk a multitude of unsettling possibilities, some examples of which are described below. In each case, this increased risk should be reflected in increased pricing. In cases where the risk and/or pricing of a loan is considered too high, then a loan transaction may be structured in order to attempt to mitigate the legal risk and/or reduce pricing. Lenders have a number of tools at their disposal in order to mitigate legal risk. In this way, loan transactions that might otherwise not get done, do get done.

3 Can Legal Risk be Measured?

Before examining ways to mitigate legal risk, it is interesting to examine the extent to which legal risk can be measured. Measuring legal risk is not an exact science, though it nevertheless can be a useful exercise to consider yardsticks that might provide a sense of one country's legal risk relative to another's. A threshold challenge is that while there are many tools available to measure *country risk*, *legal risk* is only one component of country risk. Nevertheless, there are some tools that may be helpful. In terms of measuring legal risk, the conventional wisdom is that developed economies have stronger legal institutions and less legal risk when compared to emerging market jurisdictions.

The Usefulness and Limitations of Sovereign Ratings. Sovereign ratings measure the risk of default on a sovereign's debt. These ratings are useful to get a "systemic" view of how a country is doing economically. A country that has a high sovereign debt rating is likely to be financially stable. A country that is financially stable is less likely to undergo systemic stress, at least in the short term, and therefore less likely to undergo *law reform* adverse to lenders (remember the link between systemic stress and law reform noted above).

But does it follow that there is a correlation between a sovereign's rating and *enforcement risk* against private borrowers in the sovereign's jurisdiction? A sovereign's risk of default on its debt instruments may be low because the country has extensive state-owned oil production that fills the country's coffers. This would not necessarily indicate that a country's legal institutions would fairly and efficiently enforce a pile of loan documents against a borrower in that jurisdiction – the legal institutions in such a country might be corrupt and/or inefficient. While a quick review of sovereign ratings suggests that there is at least some correlation between ratings and enforcement risk, there are also some outliers (for example, at the time of writing, Bermuda and China have similar long-term sovereign ratings from Standard & Poor's, though international lenders probably consider enforcement risk to be more significant in China than in Bermuda).

Sovereign Rate Spreads and Sovereign Credit Default Swap Prices. One of the simplest and most widely used methods to measure *country risk* is to examine the yields on bonds issued by the country in question compared to a "risk free" bond yield (still usually considered the US). A comparison of sovereign debt credit default swap prices provides a similar measure. As with sovereign ratings, this tool is useful to obtain a measure of potential systemic stress and *law reform risk* but seems less useful in terms of measuring *enforcement risk* of a borrower in that jurisdiction for the same reasons provided above.

Recovery after Default Analysis. A type of analysis performed by ratings agencies that might be considered useful for measuring legal risk from country to country is corporate default and recovery analysis. A reasonable hypothesis might be that the average recovery for creditors after a borrower default would be higher countries with low legal risk: stronger institutions means higher recoveries for creditors. But a review of the data suggests there is little or no such correlation. Why is this? There are a few possible explanations: recovery rates depend on a variety of factors other than legal risk, including the severity of default and the makeup of the individual borrowers subject to the analysis. It also is probable that lenders in a country with strong legal institutions (and low risk) may be more willing to make "riskier" loans (based on a portfolio theory of investment) given they have confidence in the jurisdiction's strong legal institutions to resolve defaults and insolvency in a predictable manner.

World Bank "Doing Business" Rankings. The World Bank publishes an interesting study each year titled the *Ease of Doing Business Rankings*. These rankings rate all economies in the world from 1 to 190 on the "ease of doing business" in that country, with 1st being the best score and 190th the worst (see http://doingbusiness.org/rankings). Each country is rated across 11 categories, including an "enforcing contracts", "resolving insolvency" and "protecting investors" category. The rankings provide a helpful tool for comparing one country to one another. While there is not space to detail the methodologies of the rankings in this chapter, the methodologies can produce some strange results. For instance, in the 2017 rankings, each of China, Belarus and the Russian Federation have a better "enforcing contracts" score than the United Kingdom. Nevertheless, these rankings can be a useful benchmark and are worth mentioning.

Subjectivity. Ultimately, in addition to the data described above, a lender's perception of the legal risk of lending into a particular country will be driven by a number of geographic, historical, political, cultural and commercial factors peculiar to the lender and the country in question. For example, as a general matter, French lenders seem more comfortable than US lenders when lending to borrowers in Africa, while US lenders seem generally more comfortable than French lenders lending to borrowers in Latin America. (English lenders seem comfortable lending anywhere!) Lenders will measure legal risk differently based on their institution's experience and tools at hand to work out a loan should it go bad.

4 Tools Used to Mitigate Legal Risk

The fact that a borrower is located in a jurisdiction with a high level of legal risk does not mean that a loan transaction cannot be closed. Lenders have been closing deals with borrowers in far-off lands since the Venetians. Today, lenders use a number of tools to help mitigate legal risk, both in terms of structuring a transaction and otherwise. These concepts are used in all sorts of financings, from simple bilateral unsecured corporate loans to large, complicated syndicated project financings with a variety of financing parties. Which of these tools will be available to a lender will depend on a variety of factors, especially the relative negotiating positions of the borrower and lender for a particular type of transaction.

Governing Law. As a starting point, the choice of governing law of a loan agreement is important because it will determine whether a contract is valid and how to interpret the words of the contract should a dispute arise. The governing law of most loan agreements in international transactions has historically been either New York or English law. This is primarily because these laws are considered sophisticated, stable and predictable, which lenders like. Also, lenders generally prefer not to have a contract governed by the law of a foreign borrower's jurisdiction, since lawmakers friendly to the borrower could change the law in a way detrimental to the lender (law reform risk). As part of any cross-border transaction, lending lawyers spend time ensuring that the choice of governing law will be enforceable in the borrower's jurisdiction, often obtaining coverage of this in a legal opinion delivered at closing.

It should be noted that that while a loan agreement may be governed by New York or English law, the collateral documentation (the documentation whereby the borrower pledges assets as collateral to secure the obligations under the loan agreement) is almost always governed by the law where the assets are located – often that of the borrower's home jurisdiction. As a general matter, courts generally have the power to adjudicate issues relating to property located in their jurisdiction. Sometimes local laws require that the collateral documentation be under local law, though in any event local courts are more efficient interpreting and enforcing collateral agreements that are governed by their own law.

Recourse to Guarantors in a Risk-Free Jurisdiction. A lender to a borrower in a jurisdiction with high legal risk may require a parent, subsidiary or other affiliate of the borrower in a "risk-free" jurisdiction to guarantee the loan. In this type of situation, the lender would want to ensure that the guaranty is one of "payment" and not of "collection", since the latter requires a lender to exhaust all remedies against a borrower before obligating the guarantor to pay. In a cross-border context, this could result in a lender being stuck for years in the quagmire of costly enforcement activity in a foreign and hostile court. While almost all New York and English law guarantees are stated to be guarantees of payment, it is nevertheless always wise to confirm this is the case, and especially important if the guarantee happens to be governed by the laws of another jurisdiction.

Collateral in a Risk-Free Jurisdiction. With secured loans, if the legal risk of a borrower's home country is high, lenders will often structure an "exit strategy" that can be enforced without reliance on the legal institutions of the borrower's jurisdiction. This has been a classic tool of project finance lenders for decades and has contributed to the financing of projects in a variety of countries that have high legal risk.

a. *Offshore Share Pledge*. For example, a lender often requires a share pledge of a holding company that ultimately owns the borrower. This type of share pledge may be structured to allow for an entity organised in a risk-free jurisdiction to pledge the shares of the holding company, also organised in a risk-free jurisdiction, under a pledge document governed by the laws of a risk-free jurisdiction. Such a pledge, properly structured and vetted with local counsel, is a powerful tool for a lender, allowing a lender to enforce the pledge and either sell the borrower as a going concern to repay the loan or to force a replacement of management. In the case of such a pledge, it is important to ensure that the borrower's jurisdiction will recognise the change in ownership resulting from enforcement of such a pledge under its foreign ownership rules. When preparing such a pledge, it is important to carefully examine the enforcement procedures to ensure that the pledge can, to the maximum extent possible, be enforced without reliance on any cooperation or activity on the part of the borrower, its shareholders or directors.

b. *Offshore Collateral Account*. Another classic tool is to require a borrower to maintain an "offshore collateral account" in a risk-free jurisdiction into which the borrower's revenues are paid by its customers. In project finance structures, lenders will often enter into agreements with the borrower's primary customers requiring that revenues be paid into such an account so long as the loans are outstanding. It is important to point out that these accounts will only be as valuable as the willingness of customers to pay revenues into them. Creditworthy, offshore customers from jurisdictions where the rule of law is respected are likely to provide more valuable credit enhancement than customers affiliated with the borrower and located in the same jurisdiction.

c. *Playing Defence and Offence*. It should be noted that, in the case of a secured transaction, offshore collateral should not be viewed as a substitute for the pledge of the borrower's local assets. In such a case, a pledge of local assets is also vitally important since, at least theoretically, it preserves the value of the lender's claim against those assets against third-party creditors. To use a football analogy, collateral can be thought of as having an "offensive" component and a "defensive" component: the pledge of local assets to the lender is a "defensive" move because this keeps other creditors from obtaining prior liens in these assets, while an equity pledge might be considered an "offensive" tool, allowing the lender to foreclose and sell a borrower quickly and efficiently in order to repay a loan with the proceeds.

Partnering with Multilateral Lenders or Export Credit Agencies. A multilateral development bank is an institution (like the World Bank) created by a group of countries that provides financing and advisory services for the purpose of development. An export credit agency (ECA) is usually a quasi-governmental institution that acts as an intermediary between national governments and exporters to provide export financing. Private lenders to borrowers in risky jurisdictions are often comforted when these government lenders provide loans or other financing alongside the private lenders to the same borrower, the theory being that the "governmental" nature of these institutions provides additional leverage to the lenders as a whole, given these entities are considered to be more shielded from possible capriciousness of a host country's legal and political institutions.

Reputation in the Capital Markets. A borrower or its shareholders may be concerned with their *reputations* in the capital markets in connection with a long and contentious loan restructuring exercise. This may be particularly true in the case of family-owned conglomerates in emerging markets, especially if other parts of the business need to access international financing. If access to the capital markets is not considered to be important, they may be willing to weather the storm. *See* T. DeSieno & H. Pereira, *Emerging Market Debt Restructurings: Lessons for the Future*, 230 N.Y.L.J. 39 (2003). In sovereign or quasi-sovereign situations, a government *seeking foreign investment* or striving to *maintain good relations with the international capital markets* may be less likely to be heavy-handed in a dispute with international investors.

Personal Relationships. The value of personal relationships should not be overlooked in mitigating legal risk. While personal relationships are important in both the developed and emerging markets, personal relationships play a particularly special role in those countries that do not have well-developed institutions and processes to resolve disputes. Some institutions, when working out problem loans in emerging markets, often turn the loan over to different personnel than those who originated the loan. In certain cases, it may be helpful to keep those with the key personal relationships with the borrower involved in these negotiations.

Political Risk Insurance and Credit Default Swaps. A lender may purchase "insurance" on a risky loan, in the form of political risk insurance or a credit default swap. Rather than mitigating risk, this instead shifts the risk to another party. In any event, this is a good tool to have in the lender's toolbox.

Why Good Local Counsel is Important. Finally, the value of high-quality local counsel in a cross-border loan in a high-risk jurisdiction cannot be overstated. This value comes in three forms: knowledge of local law and which legal instruments provide the most leverage to lenders in an enforcement situation; providing local intelligence on where other "leverage points" may be; and finally, by being well-connected to the local corridors of power and thereby being able to predict or "deflect" law reform in a manner helpful to clients. When choosing local counsel in a high-risk jurisdiction, spending more for the best counsel is usually worth the investment.

5 Recent Developments and Anecdotes that Both Support and Challenge the "Conventional Wisdom"

Legal Reform Risk in Developed Economies? As mentioned above, the conventional wisdom suggests that legal risk is higher in the emerging markets compared to the developed economies. But consider what happened to creditors in Ireland and Greece a few years ago. In both cases, lawmakers in these countries *changed the law* in a manner that materially and adversely impacted the rights of creditors. In Ireland, Irish lawmakers changed the bank resolution rules *to favour equity over debt*. In Greece, lawmakers changed Greek law in a way that allowed for collective active mechanics in a form that did not exist previously, effectively forcing minority shareholders to be bound by a majority vote. *See* T. DeSieno & K. Dobson, *Necessity Trumps Law: Lessons from Emerging Markets for Stressed Developed Markets?* (Int'l Ass'n of Restructuring, Insolvency and Bankruptcy Professionals, International Technical Series Issue No. 25, 2013). These and other examples make clear that even in the so-called developed economies, law reform can be a risk to creditors, especially when economies are under systemic stress.

Why New York or English Law is Still a Good Choice. In the Greek situation mentioned above, the majority of Greek bonds were issued under Greek law and some bonds were issued under English law. Bondholders holding English law governed bonds did not suffer the same consequence of the change in Greek law (since Greek lawmakers could not change English law). In this instance at least, the conventional wisdom held true.

Why Local Law May Sometimes be a Better Choice. In a recent transaction in the emerging markets, lenders were provided with a choice to have a guarantee governed by either New York law or local law. Conventional wisdom would suggest the lenders should opt for New York law. However, on the advice of a top local law firm, the lenders opted for the guarantee to be governed by local law. Why? Because after considerable weighing of risks and benefits (including the law reform risk associated with the choice of local law), it was determined the local law guarantee would provide considerably more leverage against the guarantor in the event of enforcement. It could be enforced more quickly and efficiently in local courts than a New York law guarantee (used by other creditors under other facilities) thus potentially providing an advantage to its beneficiaries. This notion of local law being better is probably more often going to be the exception rather than the rule.

Are Offshore Share Pledges Really Risk-Free? Even in cases of offshore pledge agreements that are perfectly documented as described above, lenders who have tried to enforce these pledges have sometimes run into difficulties. In jurisdictions with high legal risk, borrowers and their shareholders can prevent lenders from being able to practically realise on the value of their collateral in a number of ways: they may use the local legal system to their advantage by making baseless arguments that the change of ownership should not be legally recognised; they may transfer assets to other affiliated companies in violation of contractual obligations; or engage in countless other activities unimaginable to lenders when the loan was closed. This "hold-up" value effectively gives the borrower and its shareholders leverage not available in risk-free jurisdictions, even when the equity is "out of the money".

Does Teaming Up With Government Lenders Help or Hurt Private Lenders? As mentioned above, private lenders are often comforted when government lenders co-lend to a borrower. Is this comfort warranted? Government lenders may have motivations during a workout that extend beyond debt recovery to other goals. These goals may be maintaining good relationships with the foreign country in question, maintaining employment at home (in the case of ECAs), or instituting environmental, anti-terrorism or other policy goals. Experience with government lenders in restructuring exercises suggests that government lenders may be less willing to engage in difficult negotiations with foreign borrowers and, in the eyes of at least some private investors in certain restructuring exercises, their inclusion in a transaction has led to decreased recoveries. While government lenders can certainly be helpful to a workout process under the right circumstances, private lenders should be clear-sighted on the benefits government lenders provide.

Challenges to New York and English Law? As transaction and insolvency laws in emerging markets are modernised and become more uniform, and as legal and political institutions develop and mature, many local borrowers may push harder for local law to govern their loan agreements. At a recent syndicated lending conference focused on Latin America, local lenders in the region made clear they thought they had a competitive advantage over international lenders because they had an ability to make loans under local law, something local corporate borrowers seemed to value. The extent to which the market would soon see syndicated loans governed by local law was much discussed. While this phenomenon likely may not occur on a significant scale in the near term, it does seem that the choice of governing law may be one consideration that is increasingly in play when lenders are competing for lending mandates.

6 Final Thoughts

With the world becoming smaller, emerging markets developing and lenders searching for yield, more lenders will seek opportunities in cross-border lending. As a result, the question of legal risk will be one of increasing relevance, and local knowledge will be of increasing importance.

Lenders have a number of useful tools available to help mitigate legal risk. Ultimately, it may not be possible to reduce risk to that of a "risk free" jurisdiction. Lenders should be careful not to overestimate the comfort certain structural tools will ultimately provide. A borrower and its shareholders in a jurisdiction where the rule of law is weak typically enjoy a significant advantage over a foreign lender in a debt restructuring exercise.

Focus on structural tools should not overshadow perhaps the most important mitigant of all: the best protection against legal risk is to make a good loan to a responsible borrower with "sound commercial fundamentals". In the case of a cross-border loan to a borrower in a high-risk jurisdiction, "sound commercial fundamentals" goes beyond looking at a borrower's financial statements, projections and understanding its strategies. The most forward-thinking lenders will strive at the outset of a transaction to understand the full array of leverage points it may have against a borrower and its shareholders, including the need for future financing and/or access to the capital markets, and of the consequences of default for a borrower and its shareholders.

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Chapter 5

Global Trends in the Leveraged Loan Market in 2017

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1. 2017 – Record Year Driven By Refinancings/Repricings

2017 was a record year for leveraged loan issuance in both the US and European markets. Thomson Reuters reported that over USD 250bn of leveraged loans were issued in Europe, representing the highest level post credit-crisis. USD 1,400bn of leveraged loans were issued in the US, representing an increase of over 50% compared with 2016. European and US high yield issuance also exceeded issuance in 2016, at USD 89bn and USD 284bn, respectively. Various factors affected the position:

- Continuing low interest rates leading investors to hunt for yield.
- Surplus liquidity and hot competition for financings.
- Borrower-friendly market.
- Improving economic performance.
- Deregulation and tax reform in the US.
- Continuing high valuations for target companies.
- Continuing new CLO issuance as regulatory uncertainty has been resolved and CLOs have adjusted to risk retention rules.
- US Federal Reserve raising its target federal funds rate.

The leveraged loan share of the leveraged market increased to around two thirds of leverage issuance at the expense of high yield bonds. Investors favoured floating rate loans in a rising interest rate environment.

The majority of both loan and bond issuances were refinancings (or repricings). Thomson Reuters reported that the USD 933bn of refinancing activity in 2017 broke 2013's record by 23% as a borrower-friendly market allowed issuers to cut lending costs and get better terms. In Europe, M&A related financings rose, but LBOs fell and were a small part of the market. Most LBOs were secondary buy-outs.

Despite the Brexit vote, the UK led the way in Europe with the biggest volume of issuance, followed by France and then Germany. Large European leveraged loan financings included those for Semyrhamis SA (EUR 8.69bn), Mico Focus (EUR 7.85bn), Fiat Chrysler (EUR 6.25bn) and the sponsor deal, Misys (EUR 5.66bn). As a result of the low interest rates, favourable pricing and similar terms in Europe, the volume of loan issuance by US companies in Europe grew over 10%. Examples included Western Digital (EUR 3.68mm), McNee (EUR 3.59bn) and Fresenius (EUR 3.43mm). In some deals, European loan terms were even more borrower friendly than in the US.

The red hot market competition led to continued tightening of pricing and erosion of covenant protection as described below and an increase in B+ loan financings as credit quality fell. Leverage levels rose. The secondary market remained strong, with Debtwire reporting weighted average pricing for institutional term loans of a little over 99, with many bids over 100.

Although overshadowed by the loan market, the high yield market remained strong in Europe and the US. Large high yield bond issuances included Wind Tre SpA (EUR 7.43bn), Intrum Justitia (EUR 3bn), Ardagh Packaging (EUR 2bn) and Intelsat (EUR 1.3bn).

This is not the whole story though. The beginning of 2017 started off very strong due to increased refinancing activity, some deals having been delayed from 2016. Issuance volumes dropped as the year went on and central banks reduced quantitative easing; there was some investor pushback on pricing and refinancing activity dropped off. A market correction had been expected during 2018. At the time of writing, the bond markets are in sell off and the stock markets are volatile in anticipation of inflation, rising interest rates, potential tariff wars and a drop in central bank stimulus. However, this should be viewed against the possible impact of deregulation and tax reform in the US as referred to below, strengthening economies in Europe and the US as well as high buy-side demand.

If default rates rise, then investors will find that restructurings are only triggered by payment defaults as there are no earlier triggers, such as financial covenant breaches, under the loan terms which have become standard in the market. The options for recovery may be more limited and, despite recent reforms, European bankruptcy laws do not generally protect enterprise value in the same way as Chapter 11.

2. Covlite TLB – The Instrument of Choice

In Europe and the US, leveraged covlite term loans were preferred over high yield bonds due to favourable pricing and very similar covenant flexibility to that applicable under high yield covenants, but allowing the borrower to prepay the loan voluntarily with either a limited or no prepayment premium. High yield bonds are expensive to redeem or buy back in the first two or three years due to the redemption premium. Most term loans are now covlite, save for smaller deals or deals in difficult sectors, such as retail. Revolving credit facilities provided alongside term loans benefit only from a springing net leverage covenant with term lenders only having a remedy if the revolving credit facility lenders accelerate. The net leverage covenant is commonly tested at the end of a quarter, so it is only tested four days in the year. In addition, the covenant is only tested if the facility is drawn over a threshold amount, which has trended upwards this year to be 35% or more, in a number of deals. In some cases, the borrower's cash on balance sheet is netted off the threshold even though a net leverage test is used.

In some deals in the UK market, if the net leverage test is breached, there is no event of default, but the borrower cannot draw further debt under the revolving credit facility (i.e., a "**springing**" covenant which acts as a draw stop only). The net leverage test is a first lien net leverage test or a total net leverage test calculated by netting off cash on balance sheet and is often set with headroom to allow full drawing under the revolving credit facility and no deleveraging. The EBITDA headroom is usually 30–40%.

The net leverage test remains easy to satisfy:

- cash drawings to fund upfront fees or OID may be excluded in calculating the covenant;
- in European deals, the covenant clause wording or construction clause may provide that a breach of financial covenant (or other undertaking) is deemed cured if the lenders do not take action before the covenant is next tested and passed (or the breach is remedied) (a "**mulligan**");
- the borrower can pay down the revolving credit facility or hoard cash just before the quarter end;
- add-backs to EBITDA may apply; and
- letters of credit may be excluded from the threshold so a borrower can borrow against letters of credit.

The EBITDA cure is now standard in European deals. In Europe, unlike the US, overcures are permitted, cures may be deemed cured and a sponsor may have a pre-cure right to designate equity injected earlier as a cure. However, cures in consecutive financial quarters are generally not permitted. In both the US and Europe, cures may usually be exercised up to five times over the life of the facility.

3. Erosion of Pricing Protections

The borrower of a first lien term loan usually has to pay a soft call prepayment premium of about 1% of the amount prepaid but only if the primary purpose of the deal is repricing. A lender may also be able to extend its loan without consent of other lenders.

Exceptions to call protection

- Borrower doing a transformative transaction, Change of Control or IPO.
- Prepayment with subordinated or second lien debt.
- Prepayment made more than six months after closing.

The margin ratchet protection has weakened in that:

(i) the margin may ratchet down from closing rather than only after 12 months;

(ii) the margin may only ratchet up to the highest level if there is a non-payment or insolvency event of default; and

(iii) the number of stepdowns has trended down to two for TLBs.

Most favoured nation ("**MFN**") protection limits the amount by which the yield on an incremental facility exceeds the yield on the original loan. The yield limit may turn off following a stated period after closing (a "**sunset**"). There has also been an increase in the circumstances in which the MFN does not apply.

MFN ON INCREMENTAL DEBT

EUROPE	US
1% cap on all-in-yield or (sometimes) the margin.	0.5–0.75% cap on all-in-yield.
6–12 months sunset (flex to remove or extend).	6–18 month sunset (flex to remove or extend).
Sometimes no MFN for incremental facilities: ■ other than under leverage ratio test and/or the leverage ratio test may treat RCF commitments as undrawn; ■ in a different currency to the original loan; ■ within a threshold up to a turn of EBITDA; ■ which mature more than around two years after the original debt; and ■ which are not term loans/syndicated debt.	Similar (flex to modify or remove exclusions).

4. Future Proofing Loans/Change of Control

Change of control provisions have been softened, and portability (allowing a change of control without any prepayment requirement) has been a feature of a few deals, generally where a change of control is on the horizon. Portability is more common in Europe than the US, but it is still unusual. In Europe, fall away provisions have become more common. Such provisions suspend covenants on satisfaction of a leverage covenant (and possibly also listing) or reaching an investment grade rating.

Change of Control

EUROPE	US
An individual lender can demand repayment (put right) but sometimes only after 30 days consultation.	An Event of Default.
All Lenders or sometimes Majority Lenders can change definition of Change of Control.	Majority Lenders can waiver.
HY bond style definition sometimes included. Change of Control if a non-sponsor party acquires control.	Similar.
Portability allowing change of control without prepayment sometimes seen, subject to criteria, e.g.: ■ leverage not greater than leverage on closing, satisfaction of rating test or implied equity to enterprise value test; ■ no Event of Default; ■ Change of Control within 12–24 months of Closing and only once during life of facility; and ■ a new owner on a white list.	Portability rare.

5. Increasing Capacity to Incur Incremental Debt or Incremental Equivalent Debt and Leverage Up/Prime

The flexibility to incur incremental and incremental equivalent debt (including priming debts) has increased, allowing borrowers to leverage up. The restrictions applicable to side car debt (e.g. bonds), assumed acquisition debt and debt incurred under debt baskets may be much looser than those applicable to incremental debt.

In Europe, borrowers may be able to incur incremental debt which is structurally senior or capped debt without such debt being subject to the intercreditor agreement. Sponsors are also asking to make shareholder loans to (or receive payments from) subsidiaries rather than having to downstream them on an unsecured basis through a topco. The result is that such shareholder loans to subsidiaries may not be regulated by an intercreditor agreement. Both these developments may complicate European restructurings and potentially affect recoveries.

The borrower may also be able to use baskets available for making restricted payments to incur debt by "reclassifying" them.

Conditions for incurrence of Incremental Facilities ranking *pari passu* and sharing collateral

US/EUROPE
■ Cash capped freebie basket (may be a turn of EBITDA) which grows with EBITDA/total assets.
■ Leverage ratio debt basket (set at senior secured net leverage ratio or total net leverage ratio on closing date so no deleveraging required).
■ Basket equal to amounts voluntarily prepaid or bought back or permanent RCF reductions.
■ No Event of Default.
■ Debt must mature after maturity of original term loan (may have exception for debt which can mature/amortise earlier).
■ Same borrower as original loan.

Conditions for Incurrence of Additional Debt

■ Fixed charge coverage ratio for unsecured or subordinated debt with senior secured leverage ratio for other debt.
■ Incurrence of debt, dollar-for-dollar with new equity, or acquired when an acquisition or investment is made (assumed debt) but, (contribution debt) if secured, may need to satisfy senior leverage test or not make fixed charge coverage ratio worse than before.
■ Borrowing by an Obligor.
■ Borrowing by non-Obligor and secured on assets outside the collateral package.
■ No Event of Default.
■ Refinancing facilities refinancing existing facilities.
■ (In Europe) lenders acceded to intercreditor agreement if debt over a threshold.

6. Expansion of EBITDA Add-Backs

EBITDA add backs are common for synergies and cost savings from acquisitions, group initiatives and restructurings, to the extent these are achievable within the good faith determination of senior management within 12 to 24 months of the acquisition or cost saving measure. EBITDA add backs have a significant impact on financial covenants, incremental debt capacity, grower baskets, margin ratchets, restricted payment capacity and the cash sweep. In Europe, EBITDA add backs were usually subject to caps and independent verification requirements. In 2017, uncapped EBITDA add backs subject to officers' certifications have become more common in Europe, similar to the position in the US. EBITDA add backs attracted attention from US and European regulators, and both the US and European Leveraged Lending Guidances require that add backs be justified. Add backs not reflected in the financial model materially inconsistent with peer credits or which allow for artificial boosts to EBITDA (e.g., accelerated revenue recognition) will need careful review and may attract investor pushback or regulator scrutiny.

7. Restricted Payment Capacity Increases – Impact on Debt Service?

Restrictions on distributions to prevent cash leakage and weakening of debt service capacity are regarded as basic credit protections for highly leveraged companies but 2017 has seen erosion to both such protections. In Europe, capacity to make restricted payments, including investments, distributions and payments of junior debt has significantly increased in 2017. As borrowers are often permitted to reclassify baskets, the increased capacity to make restricted payments may result in the borrower having other flexibility, such as to incur debt.

Unlimited distributions are commonly permitted subject to meeting a total leverage ratio test set around 1.5× to 2× lower than the total leverage at closing. Increasingly, distributions may also be made from a builder basket based on 50% of cumulative net income plus various additions, such as a starter basket with an EBITDA based grower component. Access to the builder basket (and the starter amount) is usually subject to meeting a leverage ratio test which can be satisfied with minimal deleveraging. If no leverage ratio test applies to use of the builder basket (and the starter amount), the borrower may be able to sell material assets on day one.

In Europe, the builder basket may be based on retained excess cashflow. Repayment of junior debt is subject to the same restrictions as the payment of distributions, save that the leverage test may be set at a higher level. If a net leverage test applies instead of a total leverage test, a sponsor may be able to inject equity, net the cash off to meet the net leverage test and, subject to meeting the ratio test, round trip the cash, although sponsors usually cannot round trip the proceeds of an equity contribution used for an equity cure.

As borrowers are often permitted to reclassify baskets, the increased capacity to make restricted payments may result in the borrower having other flexibility, such as to incur debt.

8. Flex Rights and Fee Pay Aways

European lenders now often have broad flex rights similar to those in the US, potentially covering not only pricing and OID but also extension of the soft call protection period to 12 months after closing, extension of the MFN sunset, margin ratchet, increasing the proportion of excess cashflow that must be prepaid, incremental quantum, the leverage tests applicable to restricted payments, and EBITDA add backs.

However, European lenders remain restricted in the exercise of flex rights. European arrangers usually have to pay away OID before flexing and may also need to pay away a minimum amount of their arrangement fees before a pricing flex (or sometimes any flex). The term facility may be upsized on a fee-free basis to fund a flex (flex fund) with a corresponding adjustment to covenant headroom. Arrangers may only have flex rights to sell down to 10–30%, but sponsors may request that the OID and arrangement fee pay away and OID rebate are calculated based on a sell down to zero. Arrangers may also need to show that they cannot achieve a successful syndication without flexing, which may be difficult in a market where they will only achieve a partial sell down anyway.

9. Increasing Limitations on Transferability

There are notable differences between the US and European markets, with European facilities imposing more restrictions on transfers and voting sub-participations without borrower consent.

EUROPE	US
Borrower consent unless: ■ to existing lenders/affiliates/related funds; ■ insolvency/non-payment event of default (possibly other Events of Default); ■ transferee on a white list (borrower may have right to remove names); or ■ rating condition for transfers of the RCF.	Borrower consent unless Event of Default (sometimes specified Events of Default).
No transfer or voting or silent sub-participation to: ■ industrial competitors; ■ distress debt funds; or ■ defaulting lenders.	No transfer to: ■ industrial competitors; or ■ blacklisted lenders.
Borrower consent deemed given after five to 10 business days.	Borrower consent deemed given after five to 10 business days.
Transfers in breach mean transferee is disenfranchised.	Transfer in breach is void.
Borrower may require to see confidentiality agreements with potential lender to be aware of possible transfer and/or have right to object to transferee and find a replacement.	N/A.

"Industrial Competitors" may include affiliates without excluding affiliates and controlling shareholders which are financial institutions and debt funds, who may end up being disenfranchised. Transfers may also be defined widely in a construction clause and may include derivatives, sub-participations and similar matters. A further development in 2017 in European facilities was to restrict transfers to loan to own funds/distressed investors until insolvency or a payment default.

10. Few Restrictions on Acquisitions

Restriction on leveraged borrowers making acquisitions which may weaken the borrower's credit standing has long been viewed as a key credit protection. On the other hand, borrowers want flexibility to buy and build and 2017 saw borrowers prevail with increasing flexibility to make acquisitions, occasionally with no leverage ratio test.

Acquisition conditions

EUROPE	US
Satisfaction of *pro forma* leverage ratio test (sometimes) at time to committing to acquisition.	Similar
No Events of Default.	Similar
No breach of sanctions and sometimes jurisdictional limits.	Similar
Similar or complementary business.	Similar
No restrictions on acquisition if target cannot give security or guarantees for legal, cost or practical reasons (may dilute security/guarantor package and allow leakage to non-Obligors).	Limitation on value if target does not become a Loan Party
Provision of diligence reports if obtained.	N/A

11. J Crew Trap Door Closes but Increased Value Leakage Possible

Borrowers can increasingly shrink the collateral base without prepayment. Uncapped disposals for market value are often permitted so long as 75% of the consideration is in cash, the proceeds are reinvested within 12 to 24 months or applied in prepayment. In Europe, the borrower may then use the disposal proceeds to buy new assets, which do not form part of the collateral as the borrower's obligation to grant collateral is usually subject to carve-outs where the grant of security is subject to legal, cost or practical constraints.

Investors pushed back on the J Crew trap door, which allowed material value leakage out of the group if cash and assets passed through non-obligors. The broad area of investment concern has become the transfer of cash and assets from obligors to restricted non-obligors and, thereafter, from those restricted non-obligors to unrestricted subsidiaries (i.e., entirely outside of the credit structure). This mechanism allows obligors to move collateral into unrestricted subsidiaries and shrink the collateral base without shrinking the debt burden.

12. US Tax Reform

US tax reform has created additional complexity for multi-national companies with a relevant US nexus. Moving somewhat towards a modified territorial system (as opposed to a global system), the US federal government has reduced incentives for maximising the indebtedness of US borrowers within multi-national businesses by, among other things, capping deductions to US federal income for interest on indebtedness. The flip side of this equation is that international corporations should review (or revisit) non-US borrowing structures; for instance, some companies are exchanging US borrower debt for UK borrower debt in light of these tax changes. Equally, when structuring new deals, arrangers are analysing collateral/debt allocation mechanisms to optimise debt structures for multi-jurisdictional borrower corporate groups. Existing debt structures and documentation that have relied on the pre-reform tax code may suffer from unintended consequences due to, among other things, restrictive payment covenants that (now) may be excessively permissive for pass-through entities and controlled foreign corporation (CFC) related provisions that (now) may be over-inclusive due to the expanded definition thereof (e.g., to pick up sister companies under a non-US parent structure). Suffice it to say that US tax reform is a complex, thorny and challenging problem for multi-national corporations, and many (vital) areas require regulations to clarify the legislation to give taxpayers and their creditors a minimum level of certainty. For those tasked with creating financial models and projections for borrowers, US tax reform includes provisions that increase the complexity of modeling taxable income and cash flow (especially as between current and future periods); a boon for accountants but a challenge for investors who believe that cash is king.

13. Revocation of US Leveraged Lending Guidance?

On October 19, 2017, the United States Government Accountability Office (GAO) issued an opinion determining that the 2013 Interagency Guidance on Leveraged Lending (the "**2013 Guidance**"), issued jointly by the Office of the Comptroller of the Currency (OCC), the Board of Governors of the Federal Reserve System

("**Federal Reserve**") and the Federal Deposit Insurance Corporation (FDIC) (collectively the "**Agencies**"), constitutes a "rule" under the Congressional Review Act (CRA). The GAO's determination was issued at the request of Senator Pat Toomey (R-PA), who inquired by letter whether the 2013 Guidance should be subjected to Congressional approval as a rule under the CRA. Before a rule can "take effect", the Federal agency promulgating the rule is required to submit to each of the House of Representatives and the Comptroller General a report containing certain information required by the CRA, including a concise general statement relating to the rule. No such report was submitted in the case of the 2013 Guidance, because the Agencies determined that it did not amount to the promulgation of a rule. In the absence of the required submissions accompanying a new rule, the 2013 Guidance would appear to have the status of an invalidly promulgated rule that has no effect. As a by-product of this development, the Agencies sent letters to Congress indicating that they would be open to revising the 2013 Guidance.

As a general observation, the GAO's determination is beginning to impact the US leveraged debt market as market participants consider the prospects of the 2013 Guidance no longer being enforced, no longer being enforced in a manner consistent with past experience, being revised materially or becoming absorbed into general prudential standards (rather than being a hard-and-fast rule). The market now awaits Congress's next move. In addition, we note that the GAO's determination impact could result in further disparate treatment of leveraged lending between the United States and Europe.

14. ECB Guidance – Limited Impact So Far

The ECB's Leveraged Lending Guidance came into effect in November 2017. The ECB Guidance is similar to the Interagency Leveraged Lending Guidance in various ways, including in guiding that banks should only syndicate loans with leverage levels of 6x on an exceptional basis. The ECB Guidance has had limited effect so far, which may be because the European market is used to the Federal Reserve's Leverage Lending Guidance, and most European deals have a leverage of less than 6x. If the Federal Reserve's Leverage Lending Guidance is withdrawn, this may give a competitive advantage to US banks which have London branches and are not ECB regulated. However, if such banks are required to open a subsidiary in Europe to obtain EU passporting rights to continue to do business in Europe, and the subsidiary is large enough to be ECB regulated, then those banks will need to comply with the ECB Leveraged Lending Guidance. Additionally, even if no leveraged lending guidance applied to limit leverage, there is a limit on the amount of debt that can be incurred on a tax efficient basis in a typical European leveraged structure in light of the limits on deductibility of interest in applicable jurisdictions.

15. Direct Lending

European direct lending deals are reported to have grown by about 15%, with the biggest market being in the UK. Deals included Goldman Sachs's unitranche for Zenith (EUR 525mm), GSO's unitranche for HCS Group and KKR's unitranche for Chassis Brakes (EUR 175mm).

The US market has been a tale of too much money chasing too few deals. Capital has continued to flow into direct lending funds; with nearly $70bn raised in 2017. Pressure on spreads and yields has followed the flood of cash; with borrowers taking advantage of liquid market conditions. Larger club deals have also been a noteworthy trend. Refinancings have taken a toll on portfolios, and the return on cash has forced lenders to be more creative (and flexible) in their financing packages.

16. Investment Grade Syndicated Lending

The investment grade market remained strong in 2017. High grade acquisition financing was a core driver as corporates took advantage of low interest rates and strong liquidity, although syndicated lending fees increased. Thomson Reuters statistics below highlight the overall market trends:

- At $821bn, 2017 investment grade loan issuance finished 5% behind 2016's total.
- Investment grade M&A loan issuance set a new annual record with $203bn in 2017.
- CVS's late year jumbo loan for its Aetna acquisition helped propel bridge issuance to hit a new peak with $145bn in 2017.
- At $79bn, 2017 high grade term loan issuance was 19% lower than 2016's total of $98bn.
- For the year, 2017 refinancing issuance was 9% lower than 2016's total and was the lowest total since 2012.
- The $31.8bn loan for British American Tobacco to buy Reynolds American was the largest EMEA lending in 2017.
- Healthcare, retail and utilities sectors finished 1-2-3 for investment grade issuance in 2017, with retail replacing manufacturing in the top 3.

17. Asset Based Lending

The US ABL market remains a strong source of steady business for major banks, but with severe margin/profit compression. Creativity in asset-based lending now lies with non-traditional asset classes, structured credit solutions and other bespoke structures. Sponsor terms continue to creep into asset-based lending, with fixed charge coverage ratios defined liberally and ratios set at loose, to very loose, levels. Retail has been a source of chronic pain (in the form of workouts, restructuring and bankruptcies) for asset-based lenders, as the retail industry continues to be racked by structural change. The development and expansion of creative structures around whole-business securitisation has also been a noticeable trend.

There has been more interest in cross-border ABL facilities in Europe. At the end of 2017, Ardagh raised cross-border EUR 850mm asset-based loan facilities in the US. The facilities are secured on European and US receivables/inventory. The securitisation market is also picking up, with an end to regulatory undertakings, the draft EU Securities Regulation have now been settled.

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Shearman & Sterling's Leveraged Finance Group is a leader in the high-yield and leveraged loan market. Noted for their in-depth understanding of the business and legal considerations involved in leveraged credits, their lawyers offer a combination of market experience and a broad range of capabilities in the capital markets and the syndicated lending marketplace. They represent commercial banks, investment banks, mezzanine and second-lien providers, private equity sponsors and corporate borrowers. The team includes lawyers from the global Capital Markets and global Finance teams based in New York, London, Paris, Frankfurt, Milan, Singapore, Hong Kong and Abu Dhabi, working in close collaboration with members of the Bankruptcy & Reorganization and Project Development & Finance teams when needed. Shearman & Sterling's Leveraged Finance team delivers sophisticated, market-recognised advice and deal management for acquisition and other leveraged financings across a wide range of industries, financial sectors and jurisdictions.

Avoiding Traps When Documenting Make-Whole Premiums for Term Loans

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As the structure of term loans continues to evolve to include variations on "call protection" – provisions compensating lenders for early prepayments – such features need to be documented with care. One form of such call protection – long a hallmark of high-yield bonds – involves a "non-call period" that, notwithstanding its name, will typically allow borrowers to prepay loans during such period upon payment of a "make-whole premium" to lenders. Attorneys and bankers asked to adapt that feature to the term loan market should be aware of several common mistakes that have appeared in recent loan documentation of make-whole premiums, as well as some uncertainties around the enforceability of these provisions.

What are Make-Whole Premiums?

Debt instruments that allow the borrower or issuer to optionally prepay or redeem all or a portion of the debt prior to stated maturity often contain some form of "call protection" compensating the debtholder for the early prepayment or redemption. In the high-yield bond market, such protection is divided into two parts: (1) a "non-call" period (typically up to one-half of the tenor of the bond) during which the bonds may not be optionally redeemed by the issuer, very often with an exception for redemptions accompanied by a "make-whole premium"; and (2) a period following the end of the non-call period and prior to stated maturity during which the issuer may freely redeem the bonds, subject to payment of a specified redemption premium (typically, starting with one-half to three-quarters of the stated interest rate on the bond, declining ratably to zero one-to-two years prior to maturity).[1] High-yield bonds typically also include an "equity claw" exception during the non-call period allowing redemption of up to 35–40% of the outstanding amount of bonds with a premium equal to one year of interest, so long as such redemption is financed solely with proceeds of an equity offering.[2]

The basis for the non-call period in high-yield bonds is to ensure that bondholders receive a minimum return on their investment in such bonds independent of when the issuer redeems the bonds. Typically, investors will insist on being "made whole": in bondholder terms, paid a premium that provides them the economic equivalent, above a hypothetical conservative investment, of the payments they would have received had the bonds remained outstanding until the end of the non-call period and been redeemed on the first day thereafter (the "first call date"). The make-whole premium is calculated by discounting to present value the remaining scheduled payments on the bond through the first call date (including interest and the specified redemption premium that would be owed if the bonds were redeemed on that date) at a discount rate equal to the yield on a Treasury security plus a specified number of basis points (typically 50). The comparable Treasury rate is determined based on the yield on the U.S. Treasury note having a remaining life to maturity that most closely approximates the period from the redemption date to the first call date.

Documenting Make-Whole Premiums in Term Loans

High yield indentures consistently define the make-whole premium, with respect to any bond on any redemption date, as a dollar amount equal to the greater of:

(a) 1.0% of the principal amount being redeemed; and

(b) the excess, if any, of:

- (i) the present value at such redemption date of the sum of:
  - (A) the redemption price of such bond on the first call date (the "Redemption Price"); plus
  - (B) all remaining scheduled interest payment due on such bond through such first call date (excluding accrued and unpaid interest as of the redemption date),

  computed using a discount rate equal to the comparable treasury rate as of such redemption date plus 50 basis points; over
- (ii) the then outstanding principal amount of such bond being redeemed.

The applicable Redemption Price for the bond on the first call date is likewise expressed as a dollar amount equal to par plus a make-whole premium percentage (that is greater than 100%). The bond indenture will therefore require the issuer, upon such optional redemption, to pay bondholders the sum of the make-whole premium, as calculated above, in addition to the principal amount of the bond being redeemed.

While a non-call period is a standard feature of most high-yield bonds, a term loan will provide for a non-call period only if specifically negotiated by the borrower and lenders as part of the economic package of interest rate and call protection. Most highly leveraged term loans are prepayable at par at any time, with limited "soft call" protection in first-lien secured terms loans (typically a 1.00% premium for certain market-opportunistic refinancings during the first six to 12 months after closing) or "hard call" protection for junior lien secured term loans (typically 1.00–3.00% for the first one to three years).[3] Loan call premiums are most typically documented as a percentage of the principal amount of loans subject to the applicable repricing transaction or prepayment (*e.g.*, "3.00%" of a $100 prepayment (or $3), rather than "103.00%" of a $100 prepayment (or $103), as in bond indentures).

The comparative novelty of non-call periods and make-whole premiums for term loans has meant less standardisation of documentation and, not surprisingly, some common traps for those attempting to document the economic expectations of the parties. Some of these traps will result in ambiguity or imprecision that may be worked out among the relevant parties; others may have more significant consequences. In this chapter we attempt to identify some of these opportunities for error, as well as suggest tools to help practitioners successfully navigate them.

Common Errors in Documenting Make-Whole Premiums in Loan Agreements

One of the most common errors in drafting make-whole premiums in loan agreements arises from the fact that call premiums in term loan agreements are most typically expressed as a <u>percentage</u> of the loan being prepaid, rather than a <u>dollar</u> amount like the Redemption Price in a bond indenture. Thus, mixing terms and technology from a loan agreement and a bond indenture, a number of loan agreements inadvertently require the borrower to pay a premium equal to the <u>product</u> of the make-whole premium and the principal amount of the loan being prepaid, rather than the <u>sum</u> of such make-whole premium and the prepayment amount. For example, one such loan agreement we are aware of provides that in addition to the principal amount of loans subject to prepayment:

> "in the event of any voluntary prepayments of the Term B Loans . . . made prior to the first anniversary of the Closing Date, the applicable Borrower shall pay . . . a prepayment premium equal to the Applicable Premium on such date <u>on</u> the aggregate principal amount of the Term B Loans so prepaid" [emphasis added].

The "Applicable Premium" in this loan agreement is defined in the customary high yield bond-style and results in a <u>dollar</u> amount equal to the present value of the required interest and premium payable on the Term B Loans through the end of the one year non-call period. Taken together and read literally, the <u>product</u> of (i) the loan prepayment amount, and (ii) the present value of such required interest and premium would require the borrower to pay an unrealistically large make-whole premium on any such prepayment, effectively precluding any prepayment during the non-call period.

A second drafting error found in loan agreements is the miscalculation of the make-whole premium itself, resulting from a misunderstanding of the Redemption Price in clause (b)(i)(A) of the standard bond definition above. As noted above, the Redemption Price is the dollar amount equal to the product of the principal amount of bonds being redeemed and the make-whole premium percentage (which is greater than 100%) and represents the aggregate amount of principal and premium that the issuer would be required to pay in order to redeem the bonds on the first call date. The two most common forms of this error that we have seen in loan agreements are as follows (in each case, assuming a one-year non-call period and a prepayment premium on the first call date of 2.00%):

First, certain loan agreements correctly utilise 102% of the prepayment amount as the Redemption Price, but then also include in the discounted amount in clause (b)(i) the principal amount of the loans being prepaid. In these agreements, the "Applicable Premium" calculation would be:

(b) the excess, if any, of:

- (i) the present value at such prepayment date of the sum of:
  - (A) <u>102%</u> on such principal amount being prepaid; plus
  - (B) <u>the principal amount</u> of the Term B Loans being prepaid; plus
  - (C) all remaining required interest to the first anniversary of the Closing Date,

  computed using a discount rate equal to the comparable treasury rate as of such redemption date plus 50 basis points; over
- (ii) the then outstanding principal amount of Term B Loans being prepaid.

The use of a 102% premium rather than a 2.00% premium in clause (b)(i)(A), together with the inclusion of the principal amount of the loan being prepaid in clause (b)(i)(B), effectively double-counts the principal amount of the prepayment and, again, results in an implausibly large make-whole premium.

A second variation of this theme is expressed in agreements that utilise a 2.00% premium on the prepaid amount as the Redemption Price in clause (b)(i)(A) – rather than 102% – while simultaneously failing to include the principal amount of the loans being prepaid in clause (b)(i)(B). In this case, subtracting the principal amount of loans being repaid in clause (b)(ii) from the discounted value of 2% of such amount in clause (b)(i)(A) (plus the discounted value of future interest payments in clause (b)(i)(C)) will unintentionally produce a negative make-whole premium.

A third error found in several loan agreements is to again incorrectly calculate the make-whole premium itself by failing to include the premium payable on the first call date in the equation. For example, one such agreement provides that:

> ". . . any optional or mandatory or other repayment of any Second Lien Term Loan . . (i) prior to October 15, 2012 [i.e. the first call date] shall be accompanied by a prepayment fee equal to the Applicable Prepayment Fee and (ii) prior to October 15, 2013, but on or after October 15, 2012 shall be accompanied by a prepayment fee equal to 75% of the Applicable Rate on the amount so prepaid."

The Applicable Prepayment Fee is, in turn, defined as:

> "the present value at such date, computed using a discount rate equal to the Treasury Rate plus 50 basis points, of all interest that would accrue on the portion of such Second Lien Term Loan being prepaid from such date" to October 15, 2012.

The failure to include the redemption premium of "75% of the Applicable Rate" payable on the first call date in the definition of Applicable Prepayment Fee leads to the incongruous result that the borrower could prepay the loans on the first call date at – assuming for this purpose that the Applicable Rate was 10.0%–107.5% of the principal amount, but prepay the loans at only 100% of the principal amount (plus the net present value of any remaining interest to the first call date) at any time before the first call date.

A final – and more technical – error found in loan agreements involves the specific discount rate used in calculating the make-whole premium. As noted above, all future principal and interest payments and prepayment premium payable on and prior to the first call date are to be discounted based on the yield on the U.S. Treasury note having a remaining life to maturity that most closely approximates the period from the date of prepayment to such first call date.[4] A fair number of loan agreements either (1) fail to define the "comparable treasury rate", or (2) define such term as the rate on a U.S. Treasury note with a tenor most closely approximating the period from prepayment to the <u>maturity date</u> of the loan, rather than the first call date. While this error may not always have a material impact on the make-whole premium calculation, in the case of a long-dated loan (e.g., 10-year maturity or greater) with a short non-call period (e.g., one year), using the yield on a 10-year treasury note (*vs*. one-year note) will, in most interest rate environments, result in a higher discount rate and, consequently, a significantly lower make-whole premium.

Enforcement of Make-Whole Premiums in Bankruptcy

Even where a make-whole premium has been properly drafted in a loan agreement, it may be held unenforceable in a bankruptcy proceeding. Generally, make-whole premiums are enforceable under state law when the debtor is outside of bankruptcy. Although it might be subject to challenge as a "penalty", the fact that the make-whole premium amount is typically owed by a borrower or issuer choosing to prepay or redeem its loans or bonds makes it unlikely as a practical matter and in ordinary circumstances that it would be challenged or that any challenge will be successful unless the make-whole premium is grossly disproportional to the potential loss to creditors. The dynamics of a challenge to a make-whole premium, including those viewed as the real parties-in-interest, change significantly when a borrower or issuer enters bankruptcy and a creditor seeks post-petition payment of the make-whole premium. The enforceability of make-whole premiums against an issuer in a bankruptcy proceeding has been analysed in several decisions in recent years, with certain decisions focusing on whether the contractual language in the indenture or loan agreement expressly provides for payment of the make-whole premium upon acceleration of the debt upon a bankruptcy filing. Most recently, the latest Second Circuit ruling in *Momentive*,[5] analysed below, resulted in a circuit split on the issue of make-whole premium enforceability.

Background

Momentive Performance Materials Inc. and its affiliated debtors formulated a plan of reorganisation against the backdrop of a dispute with holders of $1.0 billion of first lien notes and $250 million of "1.5 lien" notes (notes with a lien ranking between the original first and second lien notes) as to the noteholders' entitlement to a make-whole premium in addition to unpaid principal and accrued interest. In light of this dispute, the plan gave the noteholders, who were viewed as over-secured, the option of either (1) accepting the plan, waiving any claim to the make-whole premium they might have, and receiving payment in cash in full on principal and interest, or (2) rejecting the plan, preserving their right to argue for a make-whole payment, and receiving replacement notes with a principal amount equal to their allowed claims but paying interest rates that the noteholders argued were below-market. Both the first lien and 1.5 lien noteholders voted overwhelmingly to reject the plan, and filed confirmation objections, asserting their entitlement to make-whole payments. The Bankruptcy Court confirmed Momentive's plan despite these objections, concluding that the indentures did not require payment of the make-whole premium. The U.S. District Court for the Southern District of New York upheld the decision of the Bankruptcy Court, and the indenture trustees appealed the decision to the Second Circuit.

Second Circuit's Analysis

The U.S. Court of Appeals for the Second Circuit affirmed the ruling of the lower courts, denying the noteholders' claims for $200 million in make-whole payments. In considering whether the noteholders were entitled to make-whole payments, the Second Circuit evaluated (1) whether there was a "redemption" in the sense contemplated by the make-whole provision in the indenture, (2) whether the redemption was "optional" for those purposes, and (3) whether the noteholders could rescind an acceleration postpetition. The court answered all three questions in the negative.

First, the Second Circuit agreed with the District Court – and the first lien noteholders conceded in their brief – that the term "redemption" generally refers only to pre-maturity repayments of debt. The Second Circuit proceeded from there to hold, relying on *In re AMR Corp.*, 730 F.3d 88 (2d Cir. 2013), that since acceleration of debt moves the maturity of that debt to the acceleration date, and since issuance of the replacement notes occurred post-acceleration, the issuance of the replacement notes by definition was post-maturity, and thus the transaction was not pre-maturity, and not a redemption for purposes of the optional redemption clause in the indenture.

The Second Circuit then analysed the circumstances of the issuance of the replacement notes to determine whether those actions were "optional". Citing *AMR*, the Second Circuit concluded that "the obligation to issue the replacement notes came about automatically" and that "[a] payment made mandatory by operation of an automatic acceleration clause is not one made at [Momentive's] option".

Finally, the Second Circuit agreed with lower courts that the noteholders' postpetition invocation of their contractual right to rescind the acceleration triggered automatically by a bankruptcy filing was barred by the automatic stay as an attempt to modify contract rights. Relying again on its decision in *AMR*, the Second Circuit stated that the right to rescind acceleration in bankruptcy would serve as "an end-run around [creditors'] bargain by rescission".

Circuit Split

The Second Circuit's make-whole decision in *Momentive* created a split with the Third Circuit which, in *In re Energy Future Holdings Corp.*, 842 F.3d 247 (3d Cir. 2016), held that noteholders were entitled to payment of an optional redemption premium at the make-whole price as a result of the repayment of their notes in a bankruptcy proceeding. In that case, the Third Circuit held that, under New York law, a redemption may occur either before or after an automatic acceleration triggered by the filing of a bankruptcy petition. Further, the Third Circuit concluded that despite the automatic nature of acceleration under the indentures, the debtor's note repayments were voluntary, particularly because the noteholders had sought to rescind the acceleration and did not want to be repaid. The circuit split between the Second and Third Circuits on the make-whole premium issue has the potential to increase forum shopping for distressed issuers with possibly significant make-whole premium obligations.

Conclusion

As loan documentation continues to adopt variations of the make-whole premium from the high-yield bond market, practitioners should be aware of both (1) the various traps in applying make-whole premium calculations to loan agreements, and (2) the possibility that a make-whole premium may be declared unenforceable in a bankruptcy proceeding. Given the potential for numerous and material drafting errors in converting loan-style soft and hard call protection to bond-style make-whole premiums in loan agreements, significant care should be taken to ensure that (a) the loan agreement requires payment of the make-whole premium in addition to the principal amount of loans being prepaid, (b) the calculation of the make-whole premium accurately reflects the Redemption Price – as the aggregate amount of principal and premium that the borrower would be required to pay on the first call date – without double counting on either side of the equation, and (c) future payments on the loan are discounted at the appropriate rate. In addition, given the possibility that any negotiated make-whole premium will be declared unenforceable in a bankruptcy, lenders and investors should expressly ensure that make-whole premiums are payable whether upon voluntary prepayment or by acceleration (inside and outside of bankruptcy) in order to prevent the make-whole premium from being disallowed when contested.[6]

Conversely, healthier issuers and borrowers with more bargaining power may seek to foreclose that claim either expressly or simply by remaining silent on the issue in the indenture or loan agreement and relying on the Second Circuit's view of New York law.

Endnotes

1. In contrast, investment grade bonds are typically "non-call" for the life of the bond (except to the extent the issuer pays a make-whole premium), although longer-dated bonds will often include a very short (one to three month) "par call" period immediately prior to maturity.
2. Of course, even during the non-call period, the issuer will be required to repay the bonds upon an acceleration following an event of default (usually at par) or, at the bondholder's option, upon a change of control (at 101%).
3. "Soft call" premiums apply solely to prepayments made in connection with "repricing" transactions and are intended to protect lenders from the borrower prepaying loans with cheaper debt; rather than, as noted above, ensuring minimum economics as in the bond context. In contrast, "hard call" premiums are payable on all optional prepayments during the applicable period.
4. In calculating the present value of the remaining interest payments to the first call date, loan agreements should use the LIBOR rate for a three month interest period in effect on the date of prepayment and assume such rate remains constant to the first call date.
5. *In re MPM Silicones, LLC*, Case No. 15-1682 (2d Cir. Oct. 20, 2017) [ECF No. 256].
6. Explicit language is not necessarily the end to the analysis in allowing a make-whole claim. Debtors may also challenge that the make-whole is an unenforceable penalty or on account of unmatured interest. *See In re Ultra Petroleum Corp.*, Case No. 16-32202 (Bankr. S.D.T.X. Sept. 21, 2017) [ECF No. 1569] (make-whole premiums may be unenforceable liquidated damages provisions under New York law if "the amount fixed is plainly or grossly disproportionate to the probable loss").

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Commercial Lending in a Changing Regulatory Environment: 2018 and Beyond

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In the US, the Trump administration has continued to make clear its desire to ease the regulatory burdens it sees as hampering business generally and, to that end, restricting the ability of banks to lend. It has indicated that it views financial services regulatory reform as a priority and that amending certain provisions of the Dodd-Frank Wall Street Reform and Consumer Protection Act (**Dodd-Frank Act**) will be critical to those efforts. Many major legislative changes are unlikely in the near future, but the consensus is that various material regulatory changes affecting banking organisations are likely to emerge from the exercise of discretion by the new leadership of the key federal banking agencies who share responsibility for supervision of the banking sector: the Board of Governors of the Federal Reserve System (**FRB**)[1], the Office of the Comptroller of the Currency (**OCC**)[2] and the Federal Deposit Insurance Corporation (**FDIC**,[3] and together with the FRB and the OCC, the **Agencies**). As discussed further below, the new leaders of the FRB and the OCC have indicated their support for a more finely calibrated prudential regulatory regime, as has the prospective Chair of the Board of the FDIC.

Prospects for Legislative and Regulatory Reform

At the direction of the President, the US Treasury Department has taken the lead in proposing regulatory change. In February 2017, President Trump issued an Executive Order[4] announcing steps to revisit the rules enacted after the 2008 financial crisis and giving Treasury the direction to review key regulatory structures and propose changes, including changes that could be implemented administratively. Specifically, the Executive Order directed the Secretary of the Treasury to report within 120 days on the extent to which existing laws, treaties, regulations, guidance, reporting and recordkeeping requirements and other government policies inhibit federal regulation of the US financial system in a manner consistent with certain core principles, one of which is fostering economic growth and vibrant financial markets through more rigorous regulatory impact analysis that addresses systemic risk and market failures, such as moral hazard and information asymmetry.

In response to President Trump's Executive Order, Treasury issued three Reports during 2017, in which it addressed relevant features of the US financial regulatory system and executive actions and regulatory changes that can be immediately undertaken to provide regulatory relief on the following broad topics: (1) banks and credit unions;[5] (2) capital markets;[6] and (3) asset management and insurance.[7]

Some of Treasury's recommendations, such as changing statutory requirements under the Dodd-Frank Act, would require new legislation, which, as a general matter, is unlikely to occur in the near term. The reasons that such legislation is unlikely include the necessity of a substantial majority in the Senate, where many Democrats can be expected to resist such legislation, an imposing agenda of critical legislative priorities, and the challenges of achieving any legislation in an election year. Despite these challenges, an ostensibly bipartisan bill, *The Economic Growth, Regulatory Relief, and Consumer Protection Act* (**Economic Growth Act**),[8] which reflects only a limited implementation of Treasury's recommendations, may be passed by the Senate in March 2018, with at least 12 Democratic Senators expected to vote for the bill.[9]

Other than the Economic Growth Act, reform is more likely to take place through administrative change originating from and implemented by the Agencies. Recent leadership changes at the FRB[10] and the OCC[11] and the pending changes at the FDIC[12] indicate that such a shift in regulatory approach is likely. The likelihood of such change is further enhanced by changes in the leadership of other key financial regulatory agencies, including the Commodity Futures Trading Commission (**CFTC**) and the Securities and Exchange Commission (**SEC**), whose cooperation would be necessary for certain discretionary changes in rulemaking associated with the Volcker Rule and around securitisation.

In testimony during the Senate Banking Committee hearing on his nomination to serve as FRB Chairman, then-Governor (now Chairman) Powell stated that under his leadership the FRB would seek to strike a balance between financial stability and financial market efficiency by "continu[ing] to consider appropriate ways to ease regulatory burdens while preserving core reforms", including "strong levels of capital and liquidity, stress testing and resolution planning".[13] This vision of regulatory tailoring is consistent with Chairman Powell's previous statements as a member of the FRB Board of Governors. For instance, in a February 2015 speech, then-Governor Powell expressed the view – largely with reference to the Leveraged Lending Guidance[14] – that regulators should maintain a "high bar" for interfering in credit markets.[15] In June 2017 testimony before the Senate Banking Committee, he emphasised that the FRB should calibrate its requirements to the size, risk and complexity of regulated firms and work to "simplify rules and reduce unnecessary regulatory burden" where possible.[16]

In remarks citing then-Governor (now Chairman) Powell's June 2017 testimony, FRB Vice Chairman Quarles likewise advocated efforts to calibrate rules more precisely and to mitigate unintended adverse consequences of regulation.[17] As examples, he indicated that he favours simplifying loss-absorbency requirements by addressing complexities in the total loss absorbing capacity rule[18] and eliminating the advanced approaches risk-based capital requirements as well as one or more ratios in stress testing. He also expressed support for measures to tailor liquidity regulation to an institution's size and risk profile similar to those advocated by Treasury. In a speech before the International Bankers Annual Washington Conference in Washington, DC on March 5, 2018, FRB Vice Chairman Quarles stated that the FRB is actively working with its fellow regulators to further tailor and reduce the burden of the Volcker Rule, particularly for firms that do not have large trading operations and do not engage in the types of activities that may give rise to proprietary trading. He also stated that the FRB appreciates the "broad extraterritorial impact of the rule in its current form for foreign banks' operations outside of the United States" and that the regulators will be revisiting the application of some provisions of the Volcker Rule to foreign banks.[19]

Comptroller of the Currency Joseph Otting has echoed FRB Chairman Powell and Vice Chairman Quarles, noting concern regarding the complexity of the bank capital framework, particularly as it applies to smaller institutions.[20] This position may arise in part from Comptroller Otting's view, largely shared by FRB Chairman Powell and Vice Chairman Quarles, that banks have established strong capital positions and risk-management programs and that credit quality is generally good across the banking industry.[21] Jelena McWilliams, the nominee for Chair of the Board of the FDIC, indicated during her nomination hearing that she also favours a more tailored regulatory approach, especially with respect to community banks.[22]

In a further shift that aligns with Treasury's recommendations, the FRB has reportedly instructed bank examiners to cease treating the Leveraged Lending Guidance as a binding set of requirements (though technically, as guidance, they should never have been viewed as "binding"), and the FRB, OCC, and FDIC have indicated that they are open to reissuing revised leveraged lending guidance for public comment and revising it accordingly, with an eye toward clarifying ambiguities and alleviating unnecessary regulatory burden. This change in tone is also consistent with some congressional criticism: in October 2017 the federal Government Accountability Office (**GAO**) confirmed Senator Pat Toomey's view that the Leveraged Lending Guidance is potentially subject to legislative repeal under the US Congressional Review Act.[23] Senior House Financial Services Committee member Blaine Luetkemeyer reacted to the GAO's conclusion by writing to the Agencies to inquire as to their plans with respect to the Leveraged Lending Guidance.

This emerging consensus among US federal banking regulators on the need to tailor capital and liquidity requirements and modify lending restrictions appears likely to persist for some time, particularly given strong support for such measures in Congress and Treasury. The shift could bolster commercial lending in the near to medium term by freeing up capital for loans and alleviating industry confusion and concern regarding supervisory expectations on lending standards.

Treasury Reports

First Treasury Report

The first of the three Treasury Reports, relating to Banks and Credit Unions, was issued in June 2017. It contains a number of recommendations that would facilitate discretionary regulatory change that could favourably impact commercial lending, including revising capital and liquidity regulatory regimes to increase banks' lending capacity while maintaining safety and soundness standards. The Report asserts that availability of bank credit to consumers and businesses in the US has been restrained and is growing slowly due in part to regulatory restrictions and requirements. In Treasury's view, burdensome regulatory requirements, such as the enhanced prudential regulations for institutions with total consolidated assets of $50 billion or more and company-administered and supervisory stress tests, which apply beginning with consolidated assets of $10 billion or more, greatly increase regulatory costs and reduce lending capacity, and they should be more appropriately tailored to the size and complexity of a bank's balance sheet and business.

Treasury Recommendations Requiring Legislative Action

The Treasury recommended a number of changes that would require legislative action by Congress:

- raising the threshold for participation in the company-run Dodd-Frank Act stress-testing regime (**DFAST**) from $10 billion to $50 billion in total assets and streamlining the DFAST process;
- amending the $50 billion threshold under Dodd-Frank for application of enhanced prudential standards to more appropriately tailor these standards to the risk profile of bank holding companies; and
- providing a regulatory "off-ramp" from all capital and liquidity requirements, most aspects of enhanced prudential standards and the Volcker Rule to highly capitalised banks, such as those with a 10% non-risk-weighted leverage ratio, consistent with Title VI: *Regulatory Relief For Strongly Capitalized, Well Managed Banking Organizations, of the proposed Financial CHOICE Act* (H.R. 10) (June 13, 2017).[24]

The Economic Growth Act would address the first two Treasury recommendations above by raising the threshold for DFAST participation from $10 billion to $250 billion in total assets and raising the threshold for application of enhanced prudential standards from $50 billion to $250 billion (with the FRB having the authority to raise or lower the thresholds in certain circumstances). Other Treasury recommendations, including the regulatory "off-ramp" for highly capitalised banks, are unlikely to be implemented by Congress in the near future.

Treasury Recommendations Not Requiring Legislative Action

The first Treasury Report includes a number of proposals that can be effected by the Agencies without prior legislative approval:

- narrowing the scope of the application of the Liquidity Coverage Ratio (LCR) to apply only to global systemically important banks, or "G-SIBs", and applying a less stringent standard to other institutions; and
- reissuing the Leveraged Lending Guidance for public comment and refining the Leveraged Lending Guidance to reduce ambiguity in the definition of leveraged lending and achieving consistency in supervision, examination and enforcement. The Agencies jointly issued the Leveraged Lending Guidance in 2013 to set forth their views on key aspects of a safe and sound leveraged lending program. The Leveraged Lending Guidance emphasises the importance of:
  - credit policies and procedures that define the institution's risk tolerance with respect to leveraged lending;
  - loan structures that are based on a sound business premise and support a borrower's ability to repay and de-lever over time;
  - a clear definition of leveraged lending that is used consistently across the institution's business lines;
  - well-defined underwriting standards that identify acceptable leverage levels and amortisation expectations; credit limits and concentration standards that align with the institution's risk tolerance;
  - robust management information systems; and
  - guidelines for portfolio stress testing.

The Leveraged Lending Guidance reflects the Agencies' view that a leverage level after planned asset sales that exceeds six times the borrower's total debt/EBITDA "raises concerns for most industries". But the Agencies have also made clear that the 6× metric is "not a bright line" and that such a level of debt may be permissible in some circumstances where certain compensating factors are present. Treasury noted industry concerns that these statements have together created considerable ambiguity as to the levels of leverage that regulators consider acceptable, leaving financial institutions uncertain as to whether they will face supervisory consequences for failure to satisfy the Leveraged Lending Guidance, which in their view is often treated as binding by bank examiners. Treasury recommended that banks should be encouraged to incorporate a clear set of metrics when underwriting a leveraged loan rather than relying on the 6× leverage ratio discussed in the Leveraged Lending Guidance.

Change in Regulatory Tone on the Volcker Rule

The first Treasury Report also suggests regulatory adjustments with respect to the Volcker Rule,[26] which imposes significant restrictions on "proprietary activities that present particularly high risks and serious conflicts of interest", by limiting proprietary trading by banking entities (insured depository institutions, their affiliates and holding companies, and certain foreign banking organisations with US operations) and restricting banking entities' ownership of and relationships with covered funds. While Treasury does not recommend repeal of the Volcker Rule and supports the Volcker Rule's limitations on proprietary trading, noting that insured banks with access to FDIC insurance and the FRB discount window that engage in proprietary trading "enjoy a government-conferred advantage that invites moral hazard", Treasury believes the Volcker Rule has "far overshot the mark" and places undue compliance burdens on banks that impact market liquidity. The Volcker Rule regulations promulgated by the Agencies, the SEC and the CFTC adopted an expansive view of prohibited activities and imposed a highly complex compliance framework to a broad range of banking organisations.

In the first Treasury Report, Treasury recommended that Congress take the following actions with respect to the Volcker Rule, among others:

- exempt banking entities with $10 billion or less in assets from all aspects of the Volcker Rule because they pose a relatively small risk to the financial system, which does not justify the compliance burden of the Volcker Rule;
- exempt banks with over $10 billion in assets from the proprietary trading provisions of the Volcker Rule if they have less than $1 billion in trading assets and trading liabilities and if their trading assets and trading liabilities represent 10% or less of total assets;
- create an "off-ramp" for highly capitalised banks, as described above, as well as focus and simplify certain covered funds restrictions contained in the Dodd-Frank Act; and
- consider eliminating the "purpose test" from the definition of proprietary trading, which requires a banking entity to determine whether a trade was made principally for the purpose of short-term resale, benefitting from actual or expected short-term price movements, realising short-term arbitrage profits or hedging such a position.

The first recommendation, exempting banking entities with $10 billion or less in assets from the Volcker Rule, is included in the Economic Growth Act. The rest of these legislative recommendations are unlikely to be implemented by Congress in the near future.

Treasury also recommended that the Agencies, CFTC and SEC take the following actions, among others, which could be effected without legislation:

- improve regulatory coordination among the five regulators that have responsibility for overseeing implementation of the Volcker Rule (the Agencies, the CFTC and the SEC);
- reduce the burdens of the Volcker Rule's compliance regime, with all banks being given greater ability to tailor their compliance programs to the particular activities of the bank and associated risk profile;
- reduce the burden of hedging business risks;
- provide increased flexibility for market-making; and
- adopt a simple definition of "covered fund" that focuses on the characteristics of hedge funds and private equity funds, instead of incorporating the overly broad references to Sections 3(c)(1) and (7) of the Investment Company Act, 15 USC 80a-3(c)(1) and (7).[27]

There has been some indication that the Agencies are receptive to reducing the compliance burdens of the Volcker Rule. In August 2017, the OCC published a notice soliciting public input on whether certain aspects of the regulations implementing the Volcker Rule should be revised to better accomplish the purposes of the Volcker Rule while decreasing the compliance burden on banking entities and fostering economic growth. While no official regulatory changes or revisions to existing regulations have been proposed, it is clear that the tone is shifting on the Volcker Rule toward decreasing compliance burdens by more appropriately tailoring its requirements. FRB Chairman Powell has criticised the role of the Volcker Rule in discouraging banks from holding and making markets in corporate debt in ways that had impaired the market. More recently, each of FRB Chairman Powell and CFTC Chairman Giancarlo have suggested that he is confident that the Agencies, CFTC and SEC would reach an agreement to reduce Volcker Rule burdens on banks, but neither suggested that it would be a quick or easy process. FRB Vice Chairman Quarles' recent speech, discussed above,[28] confirms the regulatory appetite of the regulators "to further tailor and to reduce burden" of the Volcker Rule as well as further limiting its extraterritorial reach outside the United States.

Second Treasury Report on Capital Markets

The Treasury Report on Capital Markets, issued in October 2017[29], also makes some observations and recommendations, with respect to the regulatory changes affecting securitisation, that it asserts may enhance lending and that could be put in place without legislative action.

In its review of the securitisation market, Treasury found:

- the current regulatory regime discourages securitisation as a funding vehicle, instead encouraging lenders to fund loans through more traditional methods such as bank deposits;
- regulatory bank capital requirements treat investment in non-agency securitised instruments punitively relative to investments in the disaggregated underlying collateral; and
- regulatory liquidity standards unfairly discriminate against high-quality securitised product classes compared to other asset classes with a similar risk profile.

Treasury recommended that:

- banking regulators rationalise the capital required for securitised products with the capital required to hold the same disaggregated underlying assets. Capital requirements should be set such that they neither encourage nor discourage funding through securitisation, thereby allowing the economics of securitisation relative to other funding sources to drive decision making;

- rationalising banking and trading book capital requirements may encourage additional bank participation in this asset class;
- high-quality securitised obligations with a proven track record should receive consideration as level 2B high-quality liquid assets (**HQLA**) for purposes of the LCR[30] and the Net Stable Funding Ratio (**NSFR**). Regulators should consider applying to these senior securitised bonds a prescribed framework, similar to that used to determine the eligibility of corporate debt, to establish criteria under which a securitisation may receive HQLA treatment; and
- with the cooperation of the SEC, risk retention rules[31] could also be modified in a way that would enhance the linkage between securitisation and extensions of credit:
  - Risk retention is an imprecise mechanism by which to encourage alignment of interest between sponsors and investors. Treasury observed that sponsor "skin-in-the-game" can serve as a complement to other regulatory reforms, such as enhanced disclosure requirements and underwriting safeguards, to provide added confidence to investors in securitised products. Instead of recommending an across-the-board repeal of the retention requirement, Treasury recommends that federal banking regulators expand qualifying risk retention exemptions across eligible asset classes based on the unique characteristics of each securitised asset class, through notice-and-comment rulemaking.
  - Well-documented and conservatively underwritten loans and leases, regardless of asset class, should not require the sponsor to retain an interest as an indicator of the creditworthiness of the underlying collateral. Asset-specific disclosure requirements should provide investors with confidence that securitisations of assets that are deemed "qualified" are sound enough to warrant exemption.
  - This expanded exemption would reduce the cost to issue and could encourage additional funding through securitisation. Treasury reiterates the prior recommendations regarding risk retention for residential mortgage securitisations, as stated in the Treasury Report on Banks and Credit Unions, in which Treasury recommended repealing or substantially revising the residential mortgage risk retention requirement.
  - Regarding the requirement that collateralised loan obligation (**CLO**) managers retain risk even though they do not originate the loans that they select for inclusion in their securitisation, Treasury recommends that the rulemaking agencies introduce a broad qualified exemption for CLO risk retention. CLO managers, like other sponsors who are subject to risk retention, do have discretion in the quality of the loans they select for their vehicles. In the same vein as the broader recommendation that risk retention not be statutorily eliminated but should instead be right-sized, Treasury recommends creating a set of loan-specific requirements under which managers would receive relief from being required to retain risk.

While neither the Agencies nor the SEC have commented on any of the foregoing issues, there remains hope that they may be considered over the next year.

In the meanwhile, on February 9, 2018, in an action brought by the Loan Syndications and Trading Association, a US Court of Appeals for the District of Columbia Circuit panel granted relief from risk retention requirements to some CLO managers.[32] The Panel rejected the rationale of the regulators for coverage of managers of open-market CLOs, in which loans are purchased for the vehicle from the loan market (**Open-Market CLO Managers**), concluding that Open-Market CLO Managers are not "securitizers" within the meaning of Section 941 of the Dodd-Frank Act and that, therefore, the regulators had exceeded their statutory authority in imposing risk retention obligations upon them.[33]

The Panel determined that Section 941 of the Dodd-Frank Act[34] "refer[s] to an entity that at some point possesses or owns the assets it is securitizing and can therefore *continue* to hold some portion of those assets or the credit risk those assets represent"[35] and that, consistent with the premise of these provisions that securitizers may have had a role in the origination or transfer of the underlying financial assets, a securitizer "must actually be a transferor, relinquishing ownership or control of assets to an issuer" in order to satisfy clause B of the statutory definition.[36] Because Open-Market CLO Managers neither originate the underlying loans, nor do they at any point hold such underlying loans as assets and transfer them to an issuing entity, the Court concluded that Open-Market CLO Managers are not "securitizers" within the meaning of Section 941 and therefore should not be subject to risk retention obligations under the risk retention rules.

This holding refers narrowly to Open-Market CLO Managers, although the Panel's reasoning may also have broader ramifications and may impact non-CLO structures that share certain structural features with open-market CLOs.

Challenges to Legislative Fixes Affecting the Secondary Loan Market

Exemplary of the difficulty in resolving issues that affect lending is the status of the legislative response to the 2015 decision of the US Court of Appeals for the Second Circuit in *Madden v. Midland Funding, LLC*,[37] which highlighted potential issues with respect to the secondary market for loans, albeit – most immediately at least – with respect to consumer loans.

In *Madden*, a national bank had originated a credit card loan to Ms. Madden, and charged a rate of interest as permitted for national and other banks under the usury statutes of the state in which the originating bank was located. The originating bank then sold this credit card receivable to Midland Funding, LLC, a debt buyer located in a different state in which the highest rate the non-bank buyer was permitted to charge under the local usury law was lower than the rate charged in the loan to Madden. The Second Circuit held that while the National Bank Act allowed a federally chartered bank to charge interest under the laws of its home state on loans it makes nationwide, non-banks that bought such loans could not continue to collect that interest because non-banks are generally subject to the interest rate limits of the borrower's state. The Second Circuit did not apply the "valid when made" doctrine, a longstanding principle that if a loan is not usurious when it is originally made, it does not become usurious when assigned to another party,[38] and, moreover, held that the National Bank Act did not preempt state usury laws that would have been applicable had the loan been originated by Midland Funding, because Midland was not a national bank or a subsidiary or agent of a national bank. This response fundamentally challenges the principle that a loan that is properly originated may not for any reason become invalid in the hands of a transferee because the transferee lacks privileges enjoyed by the originator. Moreover, it threatens the principle that when federal law accords a special privilege to national or state bank originating a loan, that the states – and the borrower – are bound to acknowledge the privilege in the hands of the transferee.

Responding to the uncertainty caused by the Madden decision, on February 14, 2018, the US House of Representatives passed H.R. 3299, the "Protecting Consumers' Access to Credit Act of 2017", which was originally introduced in July 2017 and would amend the Revised Statutes, the Home Owners' Loan Act, the Federal Credit Union Act, and the Federal Deposit Insurance Act to require the interest rate on certain loans to remain unchanged regardless of whether a bank has subsequently sold or assigned the loan to a third party.

Another bill was introduced in November 2017, H.R. 4439, the "Modernizing Credit Opportunities Act", which was intended to clarify that the role of the bank as lender and the location of a bank under applicable law are not affected by a contract between the bank and a third-party service provider, and to clarify that federal preemption of state usury laws applies to any loan to which a bank is the party to which the debt is initially owed according to the terms of the loan. Loans made by banks with marketing and servicing assistance from nonbank third-party entities and then sold shortly after origination have been challenged by regulators on the theory that the nonbank third party is the "true lender" and, therefore, the loan is subject to state licensing and usury laws, and this bill is intended to address this issue. This bill has not yet been put to a vote.

While a bipartisan bill to reverse the result in *Madden* has been introduced into the US Senate (S.1642, the "Protecting Consumers' Access to Credit Act of 2017"), the chances of passage of a bill in that Chamber, which typically requires larger margins of approval, are remote, thus dooming any legislative solution in the near term.

Endnotes

1. The FRB is the central bank of the United States and also has supervisory and regulatory oversight of bank holding companies, their subsidiaries, state banks that are members of the Federal Reserve System, and state regulated branches and agencies of foreign banks.
2. The OCC, an independent division of Treasury, has supervisory and regulatory oversight of national banks, which includes many of the Nation's largest banks, and federal branches of foreign banks.
3. The FDIC insures the deposits of FDIC member banks and has supervisory and regulatory oversight with respect to state banks that are not members of the Federal Reserve System.
4. Executive Order 13772 (February 3, 2017), *avail. at* https://www.whitehouse.gov/presidential-actions/presidential-executive-order-core-principles-regulating-united-states-financial-system/.
5. US Treasury, First Report, A Financial System That Creates Economic Opportunities: Banks and Credit Unions, *avail. at* https://www.treasury.gov/press-center/press-releases/Documents/A%20Financial%20System.pdf (**first Treasury Report**).
6. US Treasury, Second Report: A Financial System That Creates Economic Opportunities: Capital Markets (October 2017), *avail. at* https://www.treasury.gov/press-center/press-releases/Documents/A-Financial-System-Capital-Markets-FINAL-FINAL.pdf.
7. US Treasury, Third Report, A Financial System That Creates Economic Opportunities: Asset Management and Insurance (October 2017), *avail. at* https://www.treasury.gov/press-center/press-releases/Documents/A-Financial-System-That-Creates-Economic-Opportunities-Asset_Management-Insurance.pdf.
8. *The Economic Growth, Regulatory Relief, and Consumer Protection Act*, S. 2155 (November 16, 2017), *avail. at* https://www.congress.gov/115/bills/s2155/BILLS-115s2155rs.pdf.
9. As of the time of writing, the Senate had not voted on the Economic Growth Act. If passed by the Senate, the Economic Growth Act must then be passed by the US House of Representatives and signed by the President before becoming law, although these do not appear to constitute major obstacles.
10. These include a new Chairman, Jerome H. Powell, who started in January 2018, and a new Vice Chairman for Supervision, Randal K. Quarles, who started in October 2017.
11. Joseph M. Otting joined the OCC, as Comptroller of the Currency, in November 2017.
12. Jelena McWilliams has been nominated by the President to serve as Chairman of the Board of the FDIC, and at the time of writing, her appointment is awaiting confirmation by the Senate.
13. *Avail. at* https://www.federalreserve.gov/newsevents/testimony/powell20171128a.htm.
14. OCC, FRB, FDIC, Interagency Guidance on Leveraged Lending, 78 Fed. Reg. 17766 (March 22, 2013).
15. Jerome H. Powell, Governor, FRB, *Financial Institutions, Financial Markets, and Financial Stability*: Remarks at the Stern School of Business, New York University (Feb. 18, 2015), *avail. at* https://www.federalreserve.gov/newsevents/speech/powell20150218a.pdf.
16. *Avail. at* https://www.federalreserve.gov/newsevents/testimony/powell20170622a.htm.
17. Randal K. Quarles, Vice Chairman for Supervision, FRB, *Early Observations on Improving the Effectiveness of Post-Crisis Regulation*: Remarks at the American Bar Association Banking Law Committee Annual Meeting (Jan. 19, 2018), *avail. at* https://www.federalreserve.gov/newsevents/speech/quarles20180119a.htm.
18. The total loss absorbing capacity (**TLAC**) rule requires top-tier holding companies (including top-tier US holding companies of foreign banking organisations with a significant presence in the US) to restrict their business operations and to issue debt that will be available to absorb losses in any insolvency. FRB, Final Rule, Total Loss-Absorbing Capacity, Long-term Debt and Clean Holding Company Requirements (TLAC), 82 Fed. Reg. 8266 (January 24, 2017).
19. *Avail. at*: https://www.federalreserve.gov/newsevents/speech/quarles20180305a.htm.
20. *E.g.*, Nomination Hearing of Joseph Otting before the Senate Committee on Banking, Housing, and Urban Affairs (July 27, 2017), *avail. at* https://www.banking.senate.gov/public/index.cfm/hearings?ID=D3DED124-900B-4311-A999-1F119AF3BFDC; Comptroller Statement on Meeting with the Acting Director of the CFPB (February 6, 2018).
21. *See, e.g.*, Powell, *supra* note 16; Quarles, *supra* note 17.
22. Nomination Hearing of Jelena McWilliams before the Senate Committee on Banking, Housing, and Urban Affairs (Jan. 23, 2018), *avail. at* https://www.banking.senate.gov/public/index.cfm/hearings?ID=D3DED124-900B-4311-A999-1F119AF3BFDC.
23. Title II, Subtitle E. of the *Contract with America Advancement Act of 1996*, Pub L. 104–121, creates a mechanism through which an agency statement of general or particular applicability and future effect designed to implement, interpret, or prescribe law or policy is subject to review and possible disapproval by Congress and the President. At the request of Senator Toomey, the GAO concluded that the "[t]he Interagency [Leveraged Lending] Guidance is a general statement of policy designed to assist financial institutions in providing leveraged lending to creditworthy borrowers in a sound manner. As such, it is a rule subject to the requirements of [Congressional Review Act]". GAO, Applicability of the Congressional Review Act to Interagency Guidance on Leveraged Lending (October 19, 2017).
24. *Avail. at* https://www.congress.gov/115/bills/hr10/BILLS-115hr10rfs.pdf.
25. FRB, OCC, FDIC, Final Rule, Liquidity Coverage Ratio: Liquidity Risk Measurement Standards, 79 Fed. Reg. 61440 (October 10, 2014).
26. Section 619 of the Dodd-Frank Act, 12 USC 1851 (Section 13 of the Bank Holding Company Act of 1956), and the regulations implemented thereunder, are generally referred to

as the "Volcker Rule". The Volcker Rule regulations were promulgated by the Agencies, the SEC and the CFTC based on Section 619 of the Dodd-Frank Act, which was advanced by former FRB Chairman Paul A. Volcker.

27. Sections 3(c)(1) and (7) of the Investment Company Act are exemptions from the Investment Company Act on which hedge and private equity funds typically rely, but there is a broader range of investment vehicles that rely on these exemption that do not involve similar kinds of risk.

28. *See* note 19 and accompanying text.

29. The Treasury Report on Capital Markets is the second of the three Treasury Reports issued in response to President Trump's Executive Order. The third Treasury Report on Asset Management and Insurance is not discussed here because it is less relevant to commercial lending.

30. The LCR rules were finalised in 2014 to ensure designated banks maintain a sufficient amount of unencumbered HQLA to weather cash outflows during a prospective 30-day period of economic stress. Assets deemed to be liquid and readily marketable are designated as HQLA under three categories: level 1; level 2A; and level 2B. Level 2A and level 2B HQLA are subject to haircuts and caps toward total HQLA. The NSFR is a Basel III requirement that would require banks to maintain an amount of available stable funding at least equal to their funding needs over a one-year period, which complements the LCR rules promoting shorter term liquidity resilience. The Agencies proposed a rule to implement the NSFR requirement in May 2016, which has not yet been finalised. In its Report on Banks and Credit Unions, Treasury recommended delaying the US implementation of the NSFR until it could be appropriately calibrated and assessed.

31. *See* FRB, OCC, SEC, FDIC, FHFA, HUD, Final Rule, Credit Risk Retention, 79 Fed. Reg. 77602 (December 24, 2014).

32. The decision in *Loan Syndications and Trading Association v. Securities and Exchange Commission*, No. 1:16-cv-00652 (D.C. Cir. February 9, 2018) is *avail. at* https://www.cadc.uscourts.gov/internet/opinions.nsf/871D769D4527442A8525822F0052E1E9/$file/17-5004- 1717230.pdf.

33. *LSTA*, No. 1:16-cv-00652 at 2–3.

34. Codified as 15 USC 78o–11, Section 15G of the Exchange Act.

35. *Id.* at 5. Section 15G(a)(3)(B) provides:

(3) the term "securitizer" means—

* *

(B) a person who organises and initiates an asset-backed securities transaction by selling or transferring assets, either directly or indirectly, including through an affiliate, to the issuer.

36. *Id*. at 5-6. *See* 15 USC § 78o-11(a)(3) which defines a "securitizer" to be "(A) an issuer of an asset-backed security; or (B) a person who organises and initiates an asset-backed securities transaction by selling or transferring assets, either directly or indirectly, including through an affiliate, to the issuer." As noted by the Panel, the Agencies have interpreted "issuer" in clause A to be the same thing as the substance of clause B, in effect dropping the actual issuing entity out of the statutory definition.

37. *Madden v. Midland Funding LLC*, 786 F.3d 246 (2d Cir. 2015).

38. *See, e.g., Gaither v. Farmers & Mechanics Bank of Georgetown,* 26 U.S. 37 (1828).

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Faced with an ever wider regulatory framework, Allen & Overy's financial services regulatory practice can help you plan for and navigate these complex developments. We advise the world's leading financial institutions and have invested in building a large team that covers a very wide scope of regulations. With more than 80 experts across our global network, we offer our clients expertise in the key regions, from our large US practice to full-service coverage of the key European jurisdictions. Our well-established offices in the Middle East and Asia Pacific have also been involved in setting up many of the regulatory systems that exist in those regions today.

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Acquisition Financing in the United States: 2018 . . . Continued Growth

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The uncertainty of global politics did not negatively impact 2017 global M&A deal making. Thomson Reuters reports that global 2017 deal volume hit U.S.$3.6 trillion, about the same as 2016's deal volume. The number of announced deals increased slightly, by 3%. While the United States saw a 13.6% increase in the number of deals, Thomson Reuters reports a 15.6% decrease in U.S. deal value.

The lighter impact of the U.S. on global M&A volume may be attributable to uncertainties in the U.S. about healthcare, tax and regulatory policy, as well as an increase in European deal volume. While Brexit concerns were a cause of low deal volume in the United Kingdom in 2016, U.K. 2017 deal volumes increased 14.6%.

Energy, power and technology continued in 2017 to be top industries for global M&A activity. Real estate and, in particular in the U.S., healthcare, banking and financial services were also active. In all industries, 2017 M&A deals continued to be driven by strategic buyers, not financial buyers.

2017 M&A volume was driven by a large number of big ticket deals undertaken for strategic reasons, to drive earnings growth, fend off competition and position acquirers better to dominate their industries. These deals included Broadcom's over U.S.$100 billion proposed takeover of Qualcomm, CVS Health's proposed U.S.$69 billion acquisition of Aetna, and Disney's proposed U.S.$52.4 billion offer for 21st Century Fox assets. There were many smaller deals in the technology sector as certain technologies continue to develop towards successful implementation, such as blockchain, autonomous cars and the internet of things.

Many factors point towards increased deal making in 2018. These include favourable tax changes for corporations in the U.S., less uncertainty about healthcare policy in the U.S., continued stable equity markets and strong corporate balance sheets. The need for acquisition financing will continue to be strong. It is important to review the fundamentals of U.S. acquisition financing using secured loans and monitor trends in this regularly changing area of financing.

The Commitment Letter is Key

The commitment letter for a financing includes the material terms of the lenders' obligations to fund the loans and the conditions precedent to such obligations. Obtaining a suitable commitment letter from one or more lenders is of particular importance to acquisition financing and can be the deciding factor as to whether a seller will sign an acquisition agreement with a particular buyer where the buyer cannot otherwise prove itself able to fund the acquisition from its own funds. As in all committed financings, the borrower wants an enforceable commitment from its lenders which obligates the lenders to extend the loans, subject to certain conditions that have been mutually agreed upon. In acquisition financing, where the proceeds of the loans will be used by the borrower to pay the purchase price for the target company, in whole or in part, the seller will also be concerned whether the buyer has strong funding commitments from its lenders. If the buyer's lenders do not fund the loans, a failed acquisition could result.

In a typical timeline of an acquisition, especially one involving public companies, the buyer and seller execute the definitive agreement for the acquisition weeks, if not months, in advance of the acquisition. Following execution, the buyer and seller work to obtain regulatory approvals and other third-party consents that may be needed to consummate the acquisition, execute a tender offer if required, complete remaining due diligence, finalise the financing documentation and take other required actions.

Signing an acquisition agreement often results in the seller not pursuing other potential buyers for a period of time while the parties work to complete the items noted in the prior sentence. For example, acquisition agreements routinely contain covenants forbidding the seller from soliciting or otherwise facilitating other bids and requiring the parties to work diligently towards closing. Further, many acquisition agreements either do not give the buyer a right to terminate the agreement if its financing falls through (known as a "financing-out" provision), or require a substantial penalty payment to be made by the buyer if the transaction fails to proceed, including as a result of the financing falling through (known as a "reverse break-up fee"). Accordingly, at the signing of the acquisition agreement, and as consideration for the buyer's efforts and costs to close the acquisition, the buyer will want the lenders to have strong contractual obligations to fund the loans needed to close the acquisition.

Who Drafts the Commitment Letter?

Private equity funds (also known as sponsors) are some of the most active participants in M&A transactions and related financings. With their sizable volumes of business that can be offered to banks, sponsors often have greater leverage in negotiations with lenders than non-sponsor-owned companies. Sponsors and their advisors monitor acquisition financings in the market and insist that their deals have the same, if not better, terms. As economic tides shift, the ability of sponsors to leverage their large books of banking business grows and wanes, and the favourability for sponsors of acquisition financing terms shift as well.

Who drafts the commitment papers is one area where sponsors are often treated more favourably than other borrowers. While lenders in most cases expect to draft commitment papers, the larger sponsors are now regularly preparing their own forms of commitment papers and requiring the lenders to use them. From the sponsors' perspective, controlling the drafts can result in standardised commitment letters across deals, and a more efficient and quick process to finalise commitment letters. To get the best terms, the sponsors often simultaneously negotiate with a number of potential lenders and then award the lead role in an acquisition financing to the lender willing to accept the most sponsor-favourable terms.

Conditionality

The buyer's need for certainty of funds to pay the purchase price puts sharp focus on the conditions that must be met before the lenders are contractually obligated to fund the loans. As a result, a buyer has a strong preference to limit the number of conditions precedent in a commitment letter, and to make sure that the commitment letter is explicit as to the included conditions, in order to enhance funding certainty. The buyer and seller want to avoid a scenario where the conditions precedent to the buyer's obligation to close the acquisition has been met but the lenders' obligation to fund the loans has not. Particularly in the scenario where no financing-out clause is included in the acquisition agreement, if the acquisition financing falls through because the buyer cannot satisfy the conditions in the commitment letter, the buyer may not be able to close the acquisition and could be required to pay the seller sizable contractual breakup fees and be subject to lawsuits from the seller. Certain conditions discussed below are commonly subject to heavy negotiation in an acquisition financing.

Conditions Precedent, Covenants and Defaults

Commitment letters for general financings often contain vague and partial lists of documents and conditions that the lenders will require before funding the loans. Phrases like "customary conditions precedent" are often seen. In contrast, a commitment letter for an acquisition financing typically has an explicit, detailed and often lengthy list of conditions.

If the lenders are permitted to require satisfaction of conditions precedent to funding that are not expressly set forth in the signed commitment letter (whether customary conditions or not), this increases the risk to the borrower that these additional conditions cannot be met. It is common in an acquisition financing to see an express statement from the lenders that the list of conditions precedent in the commitment letter are the only conditions that will be required for funding. In some cases, the list of conditions precedent in commitment letters for acquisition finance are so detailed that they are copied directly into the final forms of loan agreements.

Similarly, vague references to "customary covenants" and "customary events of default" in a commitment letter present similar risks, particularly proposed inclusion of unreasonable provisions which could not be met by the borrower. To limit this risk, commitment letters for acquisition financings often include fully negotiated covenant and default packages (which may include pages of detailed definitions to be used in the calculation of any financial covenants).

Form of Loan Documents

Some sponsors even require that the form of the loan agreement be consistent with "sponsor precedent", meaning that the loan documentation from the sponsor's prior acquisition financing will be used as a model for the new financing. Agreeing to use or be guided by "sponsor precedent" limits the risk to the sponsor that the financing will be delayed or not close because the lender and its counsel produce a draft loan agreement with unexpected terms and provisions.

Many acquisition financings, particularly in the middle market, involve multiple classes of loans with complex intercreditor arrangements. These financings include 1st/2nd lien, split-collateral, *pari passu* collateral, subordinated, holdco and unitranche financings. In complex and technical intercreditor agreements, lenders agree on many issues relating to their respective classes of loans, including priority of liens, priority of debt, control of remedies and certain technical bankruptcy issues. Negotiation of these agreements among different classes of creditors can be lengthy and frustrate closing timeframes. As middle market M&A continues to grow, and more deals have complex intercreditor arrangements, some sponsors are also requiring lenders to use a specified form of intercreditor agreement.

Representations and Warranties

Loan agreements typically require that the included representations and warranties be accurate as a condition to funding. Lenders financing the acquisition also want the representations with respect to the target in the acquisition agreement to be accurate. This is reasonable because after consummation of the acquisition, the target is likely to be obligated on the loans (either as the borrower or a guarantor) and thus part of the credit against which the lenders are funding.

"SunGard" (named for an acquisition financing that included these terms) or "certain funds" provisions are now common in commitment letters for acquisition financings. These clauses are relevant to several provisions in a typical commitment letter. With respect to representations and warranties, these clauses provide that on the closing date of the loan, as a condition to the lenders' funding obligations, only certain representations need to be accurate. Strong sponsors even negotiate the precise meaning of the term "accurate". The representations required to be accurate as a condition to the lenders' funding obligation in a typical SunGard clause include the following:

- The only representations and warranties relating to the target are those that, were they untrue, would be material to the lenders and for which the buyer has a right under the acquisition agreement to decline to close the acquisition. While providing certainty of funding, this standard avoids a scenario where the loan agreement has different representations with respect to the target than the acquisition agreement.
- Only certain representations with respect to the borrower set forth in the loan agreement must be accurate (the "specified representations"). These can include those with respect to corporate existence, power and authority to enter into the financing, enforceability of the loan documents, margin regulations, no conflicts with law or other contracts, solvency, status of liens (see below regarding this topic) and certain anti-terrorism and money laundering laws. A financial covenant could also be included as a specified representation in some deals. What are included as specified representations change with changing economic conditions and relative bargaining strength of companies and sponsors. As financial markets have improved and the leverage of sponsors has increased, the typical list of specified representations has shrunk and may well continue to weaken, benefitting sponsors.

These are the only representations applicable as conditions precedent to the initial funding of the loans. Even if the other representations in the loan agreement could not be truthfully made at the time of the initial funding, the lenders nonetheless are contractually obligated to fund the loans.

Company MAC

Company material adverse change (MAC), sometimes referred to as a "company MAC" or a "business MAC", is a type of representation included in some acquisition agreements and loan agreements. This is a representation that no material adverse change in the business of the target has occurred. Inability to make the representations in the acquisition agreement typically permits the buyer to terminate the acquisition agreement and in the loan agreement it excuses the lenders from their funding obligations. A customary MAC definition in an acquisition agreement differs from that in a loan agreement. Acquisition agreement MAC clauses are often more limited in scope and timeframe covered, and have more exceptions (including for general market and economic conditions impacting the target). Like other representations, buyers and sellers often require that the MAC definition in loan agreements mirror the definition in acquisition agreements, but solely for purposes of the initial funding of the acquisition loans (and not for ongoing draws under a working capital revolver or a delayed draw term loan, for instance).

Market MAC and Flex

"Market MAC" is another type of MAC representation in some commitment letters. Seen more in economic down-cycles, these clauses allow the lenders to terminate their commitments if there has been a material adverse change in the loan and syndication markets generally. Strong borrowers and sponsors have had success with excluding these clauses in their commitment letters over the last several years as the economy has continued to improve.

As discussed above, the time between signing the commitment letter, on one hand, and closing the acquisition and funding the loans on the other, is often a lengthy period. Lenders whose commitment letters do not have a market MAC, especially those lenders who fully underwrite the commitments, are subject to deteriorating financial markets during the syndication of the commitments and the risk that they will not be able to sell down the commitments to other lenders. "Flex" provisions limit this risk and allow for amendments to certain agreed-upon terms of the financing without the borrower's consent when necessary to allow the lenders arranging the loan to sell down their commitments.

If, during syndication, there is no market for the loans at the price or terms provided in the commitment letter and term sheet, a flex provision will allow the committed lenders to "flex" the pricing terms (by increasing the interest rate, fees or both) within pre-agreed limits or make other pre-agreed changes to the structure of the loans (such as call protections, shorter maturities, etc.). While these changes provide some comfort to committed lenders in gradually deteriorating financial markets, they may not be as helpful in a dramatic downturn where there is little to no market for loans on any terms.

At times of financial and market uncertainty, flex clauses often became broader in scope and gave lenders greater flexibility to change key terms of a financing. The types of provisions that can be subject to flex include interest rate margins, negative covenant baskets, financial covenant ratios, the allocation of credit between first lien, second lien and high-yield bonds and the amount and type of fees. As markets improve, sponsors are using their leverage to limit the breadth of flex provisions, and to require greater limits on the scope of the changes that can be made without their consent.

Some sponsors require "reverse flex" arrangements. These provisions require the lenders to amend the financing terms under the commitment letters to be more favourable to the borrower if syndication of the loans is "oversubscribed", meaning that there is more demand from potential lenders than available loans.

Perfection of Liens

As in all secured financings, lenders in an acquisition financing need evidence that their liens on the borrower's assets are perfected and enforceable, preferably as a condition precedent to the initial funding under the loan agreement. However, ensuring perfection of the liens is often highly technical and can be a time-consuming process depending on the nature and location of the borrower's assets and the specific legal requirements for perfection. The technical nature of lien perfection raises the risk (to the borrower and the seller) that lenders will delay or withhold funding for the loans because insufficient steps were taken to perfect the liens, and in an acquisition financing, timing and certainty are at a premium.

Typical SunGard provisions limit this risk by requiring delivery at funding of only (i) Uniform Commercial Code financing statements which perfect a security interest in personal property that can be perfected by filing, and (ii) original stock certificates for any pledged shares. Perfecting a security interest in other asset classes is required on a post-funding basis by a covenant detailing what perfection steps are required. The sorts of collateral perfected on a post-closing basis can include real estate, deposit and securities accounts, intellectual property, foreign assets and other more esoteric collateral requiring more complicated efforts.

As financial markets continue to improve, sponsors are likely to continue pushing lenders to increase the timeframes to complete post-closing collateral deliverables, give the administrative agent greater flexibility to extend these timeframes without lender consent and limit efforts by lenders to increase the collateral deliverables required at closing.

The Acquisition Agreement Matters

Delivery of the executed acquisition agreement is a condition precedent to the lenders' obligation to fund the loans. As discussed in more detail below, as a fallback, lenders sometimes accept a near final draft of the acquisition agreement, coupled with a covenant from the buyer that there will be no material changes. The terms of the acquisition agreement are important to lenders in a number of respects, beyond understanding the structure and business of the borrower after consummation of the acquisition. Lenders also regularly require inclusion of certain provisions in acquisition agreements.

Structure of the Acquisition

The structure of the acquisition is important to the lenders as it will dictate a number of issues for the financing, including collateral perfection, identity of the guarantors and borrowers and timing of the acquisition (*i.e.*, how long the lenders need to have their commitments outstanding). There are a number of common acquisition structures. While the specifics of those structures are beyond the scope of this article, these include stock purchases (with or without a tender offer), mergers (including forward, forward triangular and reverse triangular mergers) and asset purchases. Each has its own unique structuring issues for the lenders.

Representations and Company MAC

As described above, the lenders often rely on the representations and warranties in the acquisition agreement, including the definition of material adverse change, and incorporate those terms into the loan agreement.

Obligation to Continue Operating

Lenders often review whether the seller is contractually obligated in the acquisition agreement to continue operating the business in the ordinary course and not to make material changes to the business. Again, the target is a part of the lenders' credit and the lenders do not want to discover after consummation of the acquisition that the target has been restructured in a way that results in its business being different than the lenders' understanding.

Indemnity

Lenders also typically consider the indemnities provided by the seller in the acquisition agreement. If, after the acquisition is consummated, it is discovered that the seller made a misrepresentation or, worse, committed fraud or other wrongdoing as part of the acquisition, those indemnities could affect the buyer's ability to recover against the seller. If the misrepresentation or wrongdoing results in the lenders foreclosing on the assets of the borrower, the lenders could inherit the indemnities if the rights of the borrower under the acquisition agreement are part of the collateral. Acquisition agreements typically contain anti-assignment and transfer provisions. It is important that those provisions expressly permit the lenders to take a lien on the acquisition agreement.

Purchase Price Adjustments and Earn-Outs

Any payments to be made to the seller by the buyer after consummation of the acquisition are important to the lenders. Many loan agreements define these payments, whether based on performance of the target or other factors, as debt and their payment needs to be specifically permitted by the loan agreement. Beyond technically drafting the loan agreement to permit payment of these amounts, the proceeds to be used to make these payments should be viewed as assets of the buyer that are not available to the lenders to repay the loans and this may impact the credit review of the loan facility.

Xerox Provisions

When a proposed acquisition terminates, the commitment letters for the acquisition financing typically state that the lenders' commitments also terminate. That is not always the end of the lenders' concerns. Many terminated acquisitions result in accusations of breach of contract, wrongdoing or bad faith by the parties. Litigation is not uncommon. Lenders want to make sure that any litigation brought by the seller does not look to the lenders for damages.

Xerox provisions (named for a financing with Xerox where these clauses were first seen) give lenders this protection in the form of an acknowledgment by the seller in the acquisition agreement that the seller's sole remedy against the buyer and its lenders for termination of the acquisition is the breakup fee specified in the acquisition agreement. If the acquisition terminates because the lenders fail to fund their commitments, the lenders may be subject to a breach of contract suit brought by the buyer. But the lenders in any termination scenario often seek to restrict suits brought against them by the seller. Conversely, sellers' focus on certainty of the financing has caused some sellers to push back on inclusion of these provisions. Some sellers with strong leverage even negotiate for the right to enforce remedies (or cause the buyer to enforce remedies) against the lenders under a commitment letter.

Since the lenders are not party to the acquisition agreement, applicable law creates hurdles for the lenders to enforce the Xerox provisions. To address these hurdles, lenders seek to be expressly named as third-party beneficiaries of the Xerox provisions. In the event the lenders have claims against the seller for breach of the Xerox provisions, lenders will have customary concerns about the venue and forum of any claims brought by the lenders under the acquisition agreement. Like in loan agreements, lenders often seek to have New York as the exclusive location for these suits and seek jury trial waivers in the acquisition agreement.

Efforts to Obtain the Financing

Lenders will consider provisions in the acquisition agreement regarding the buyer's obligations to obtain financing. Typically, buyers agree to use "reasonable best efforts" or "commercially reasonable efforts" to obtain the financing in the commitment letter. These provisions may include a requirement to maintain the commitment letter, not to permit any modification to the terms of commitment letter without the seller's consent (with some exceptions), to give notice to the seller upon the occurrence of certain events under the commitment letter, and obtain alternative financing, if necessary. As noted above, acquisition agreements may also contain provisions obligating the buyer to enforce its rights against the lender under the commitment letter, or even pursue litigation against the lender. Buyers with strong leverage will want to limit provisions in the acquisition agreement requiring specific actions against the lenders.

Cooperation with the Financing

As discussed above, the lenders have an interest in understanding the acquisition and the nature of the target's business. Further, the conditions precedent will require deliverables from the target and the lenders' regulatory, credit and legal requirements demand that they receive certain diligence information about the target and its business. None of this can be accomplished if the seller does not agree to assist the buyer and its lenders. Lenders often require that the acquisition agreement include a clause that the seller will cooperate with the lenders' diligence and other requirements relating to the acquisition financing.

Amendments to the Acquisition Agreement

Lenders usually have the opportunity to review the acquisition agreement, or at least a near final version, prior to executing their commitment letters. The buyer and seller will want the lenders to acknowledge that the final agreement or draft is acceptable. The lenders, on the other hand, will want to receive notice of any amendments to the acquisition agreement and ensure they do not adversely impact the financing. To avoid the lenders' refusal to fund the loans because of an amendment to the acquisition agreement, buyers and sellers are often careful to ensure that no amendments to the acquisition agreement will be required. Some amendments are unavoidable and commitment letters often contain express provisions as to the nature of those amendments that need lender approval. If lender approval is not needed, then the lenders cannot use the amendment as a reason to refuse funding.

Negotiations of the "no-amendment" condition focus on the materiality of the amendments and whether the change has to be adverse or materially adverse, with some lenders negotiating consent rights for any material change in the acquisition agreement.

Lenders often seek to negotiate express provisions that would be deemed material or adverse, including some of the above clauses that were included in the acquisition agreement at the requirement of the lenders. Some lenders with strong negotiating leverage even negotiate for a clause in the acquisition agreement that any amendments will require the lenders' consent.

Conclusion

Leveraged acquisitions in the United States raise unique structuring issues and techniques, only some of which are discussed here. Expect 2018 M&A volumes to remain high, with sponsors exercising greater leverage over their lenders to further loosen acquisition-lending terms.

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A Comparative Overview of Transatlantic Intercreditor Agreements

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Introduction

The intercreditor frameworks applicable to a given financing structure in a particular market are often fairly settled, but in cross-border financings for European borrowers or other financings involving practitioners and business people in different parts of the world, deal parties may have different expectations as to the key intercreditor terms that ought to apply.

In this chapter, we will compare and contrast the key terms in U.S. second lien and European second lien intercreditors and discuss the blended approach taken in some recent intercreditor agreements for financings of European companies in the U.S. syndicated bank loan markets. Similar dynamics may be involved when documenting intercreditor agreements involving other non-U.S. jurisdictions as well, but for ease of reference, we will refer to these intercreditor agreements as "Transatlantic Intercreditor Agreements".

Assumptions

U.S. second lien intercreditors are predicated on two key assumptions: *first*, that the business will be reorganised pursuant to Chapter 11 of the United States Bankruptcy Code (Chapter 11); and *second*, that the first lien lenders will receive the benefits of a comprehensive guarantee and collateral package (including shares, cash, receivables and tangible assets) pursuant to secured transactions laws that effectively provide creditors with the ability to take a security interest in "all assets" of the borrower and guarantors. European second lien intercreditors, in contrast, (i) assume that it is unlikely that the borrower and guarantors will be reorganised in an orderly court-approved process and indeed more likely that, since there is no pan-European insolvency regime (and thus no pan-European automatic stay on enforcement of claims), the intercreditor terms will have to function in the context of potentially multiple and disparate insolvency proceedings (ideally outside of insolvency proceedings altogether), and (ii) contemplate that not all assets of the borrower and guarantors will be subject to the liens of the first lien and second lien secured parties. As a result, one of the key goals that European second lien intercreditors seek to facilitate is a swift out-of-court, out-of-bankruptcy, enforcement sale (or "pre-pack") resulting in a financial restructuring where the business is sold as a going concern on a "debt free basis", with "out of the money" junior creditors' claims being released and so removed from the financing structure.

Overview

The first lien/second lien relationship in the U.S. closely resembles the senior/second lien relationship in Europe; however, for the reasons stated above, the key terms of U.S. second lien and European second lien intercreditors have been constructed on the basis of different assumptions, which therefore results in significant intercreditor differences.

European second lien intercreditor agreements typically combine claim subordination, payment blockages, lien subordination, broad enforcement standstill provisions restricting the junior lien creditors' ability to take enforcement action (not only with respect to collateral but also with respect to debt and guarantee claims) and extensive release mechanics. U.S. second lien intercreditors establish lien subordination, which regulates the rights of the U.S. second lien creditors with respect to collateral only, and include an enforcement standstill with respect to actions against collateral only. U.S. second lien intercreditors do not generally include payment or claim subordination and they rely heavily on waivers of the junior lien creditors' rights as secured creditors under Chapter 11.

European second lien intercreditors are often based on the Loan Market Association's form (the "LMA"), but are negotiated on a deal-by-deal basis. By contrast, there is no market standard first lien/second lien intercreditor agreement in the U.S. As discussed below, recent intercreditors for financings of European companies in the U.S. syndicated bank loan markets vary even more significantly, but common themes are emerging.

Key Terms of U.S. Second Lien Intercreditor Agreements and European Second Lien Intercreditor Agreements

1. Parties to the Intercreditor Agreement

U.S. second lien intercreditors are generally executed by the first lien agent and the second lien agent and executed or acknowledged by the borrower and, sometimes, the guarantors. Depending on the flexibility negotiated by the borrower in the first lien credit agreement and second lien credit agreement, the intercreditor agreement may also allow for other future classes of first lien and second lien debt permitted by the credit agreements to accede to the intercreditor agreement. U.S. second lien intercreditors also typically allow for refinancings of the first lien and second lien debt.

By contrast, the parties to European second lien intercreditors generally include a longer list of signatories. In addition to the first lien agent and lenders, the second lien agent and lenders and the obligors, the obligors' hedge providers, ancillary facility lenders, the lenders of intra-group loans, the lenders of shareholder loans and the security agent will execute a European-style intercreditor agreement. The longer list of parties to European second lien intercreditors is largely driven by the senior creditors' need to ensure that, after giving effect to the senior lenders' enforcement, the borrower group is free and clear of all claims (both secured and unsecured) against the borrower and guarantors coupled with a desire to ensure that any enforcement action by creditors is choreographed in a manner which maximises recoveries for the senior secured creditors (and thus indirectly for all creditors). With an increased number of incurrence-based TLB deals having been executed, it has become fairly common for refinancing and incremental debt to be permitted in European deals. European intercreditors typically require such debt to be subject to the intercreditor agreement even if (above a certain threshold amount and subject to negotiation) it is unsecured.

Hedge obligations are generally included as first lien obligations (and sometimes also as second lien obligations) under U.S. second lien intercreditors, but hedge counterparties are not directly party to U.S. second lien intercreditors. By accepting the benefits of the first priority lien of the first lien agent, the hedge counterparties receive the benefits of the first priority lien granted to the first lien agent on behalf of all first lien secured parties (including the hedge counterparties) and the hedge counterparties are deemed to agree that the first lien security interests are regulated by the intercreditor agreement and other loan documents. The hedge counterparties under U.S. second lien intercreditors in syndicated bank financings generally have neither the ability to direct enforcement actions nor the right to vote their outstanding claims (including any votes in respect of enforcement decisions).

Cash management obligations (e.g., treasury, depository, overdraft, credit or debit card, electronic funds transfer and other cash management arrangements) are often included as first lien obligations under U.S. second lien intercreditors on terms similar to the terms relating to the hedge obligations. By contrast, European second lien intercreditors typically do not expressly contemplate cash management obligations. In European financings, the cash management providers would typically provide the cash management services through ancillary facilities – bilateral facilities provided by a lender in place of all or part of that lender's unutilised revolving facility commitment. Ancillary facilities are not a traditional feature of U.S. credit facilities, although we do now see them included in transatlantic financings. The providers of ancillary facilities would be direct signatories of a European second lien intercreditor.

2. Enforcement

a. *Enforcement Instructions*

The first lien agent under a U.S. second lien intercreditor takes instructions from the lenders holding a majority of the loans and unfunded commitments under the first lien credit agreement, which follows the standard formulation of required lenders in U.S. first lien credit agreements. (Note, however, that the vote required to confirm a plan of reorganisation in a Chapter 11 proceeding is a higher threshold – at least two thirds in amount and more than one half in number of the claims actually voting on the plan.)

The security agent under European second lien intercreditors, however, takes instructions from creditors holding 66⅔% of the sum of (i) the drawn and undrawn amounts under the senior credit agreement, and (ii) any actual outstanding liabilities (plus any mark to market value if the senior credit agreement has been discharged) under any hedging arrangements.

b. *Enforcement Standstill Periods*

U.S. second lien financings involve lien subordination as opposed to payment (also referred to as debt or claim) and lien subordination. The result of lien subordination is that only the proceeds of shared collateral subject to the liens for the benefit of both the first lien secured parties and second lien secured parties are applied to repayment in full of the first lien obligations before the second lien secured parties are entitled to receive any distribution of the proceeds of the shared collateral, but the second lien secured parties may receive other payments (such as payments of principal and interest and payments from other sources, e.g., unencumbered property) prior to the first lien obligations being paid in full. In the context of U.S. obligors, it is unlikely, in practice, that there would be substantial property that is unencumbered since the security granted would likely pick up substantially all assets – in contrast to a number of European obligors whose unencumbered assets may be significant due to local law limitations.

Payment subordination requires the junior lien creditors to turnover to the first lien secured parties all proceeds of enforcement received from any source (including the proceeds of any unencumbered property) until the first lien obligations are paid in full. In consequence, the difference in recoveries between lien subordination and payment subordination could be significant in a financing where material assets are left unencumbered, as is likely in a financing in which much of the credit support is outside the U.S.

U.S. second lien intercreditors prohibit the second lien agent from exercising any of its rights or remedies with respect to the shared collateral until expiration of the period ending 90 to 180 days after notice delivered by the second lien agent to the first lien agent after a second lien event of default or, in some cases, if earlier, second lien acceleration. The standstill period becomes permanent to the extent the first lien agent is diligently pursuing in good faith an enforcement action against a material portion of the shared collateral. An exercise of collateral remedies generally includes any action (including commencing legal proceedings) to foreclose on the second lien agent's lien in any shared collateral, to take possession of or sell any shared collateral or to exercise any right of set-off with respect to any shared collateral, but the acceleration of credit facility obligations is generally not an exercise of collateral remedies.

European second lien intercreditors typically contain a much broader enforcement standstill provision than U.S. second lien intercreditors, principally because there is no pan-European equivalent of the Chapter 11 stay. The scope of the restricted enforcement actions typically prohibits any acceleration of the second lien debt, any enforcement of payment of, or action to collect, the second lien debt, and any commencement or joining in with others to commence any insolvency proceeding, any commencement by the second lien agent or second lien creditors of any judicial enforcement of any of the rights and remedies under the second lien documents or applicable law, whether as a secured or an unsecured creditor. The enforcement standstill period has traditionally run for (i) a period of 90 days (in most cases) following notice of payment default under the senior credit agreement, (ii) a period of 120 days (in most cases) following notice of financial covenant default under the senior credit agreement, and (iii) a period of 150 days (in most cases) following notice of any other event of default under the senior credit agreement, plus (in some cases) 120 days if the security agent is taking enforcement action. However, the enforcement standstill period is now often subject to negotiation. In European second lien intercreditors, the senior creditors firmly control enforcement. In addition, the senior agent is entitled to override the junior agent's instructions to the security agent, leaving the second lien lenders only able to influence the timing of enforcement action after the standstill period.

Because the enforcement standstill in U.S. second lien intercreditors is limited to enforcement against shared collateral, U.S. second lien lenders, unlike their European counterparts, retain the right (subject to the Chapter 11 stay) to accelerate their second lien loans and to demand payment from the borrower and guarantors during the standstill period. However, in the event any second lien agent or any other second lien creditor becomes a judgment lien creditor in respect of the shared collateral as a result of enforcement of its rights as an unsecured creditor (such as the ability to sue for payment), the judgment lien would typically be subordinated to the liens securing the first lien obligations on the same basis as the other liens securing the second lien obligations under the U.S. second lien intercreditor agreement. This judgment lien provision effectively limits the effectiveness of the junior lien creditors' efforts to sue for payment, since the junior lien creditors ultimately will not be able to enforce against shared collateral, although the junior lien creditors could still precipitate a bankruptcy filing and/or obtain rights against any previously unencumbered assets of the borrower and guarantors.

3. Payment Blockages

U.S. second lien intercreditors do not generally subordinate the junior lien obligations in right of payment to the first lien obligations.

European second lien intercreditors do subordinate the junior lien obligations in right of payment to the senior lien obligations and include a payment blockage period that is typically co-extensive with a payment default under the senior credit agreement and of a duration of 150 days during each year whilst certain other material events of default under the senior credit agreement are continuing. The second lien creditors may negotiate for exceptions to the payment blockage periods, e.g., payment of a pre-agreed amount of expenses related to the restructuring or a valuation of the borrower group (other than expenses related to disputing any aspect of a distressed disposal or sale of liabilities). In addition, separate payment blockage rules typically apply to hedge obligations, shareholder loan obligations and intragroup liabilities in European second lien intercreditors.

4. Releases of Collateral and Guarantees

In order to ensure that the junior lien creditors are unable to interfere with a sale of the shared collateral, both U.S. second lien intercreditors and European second lien intercreditors contain release provisions whereby the junior lenders agree that their lien on any shared collateral is automatically released if the first lien creditors release their lien in connection with a disposition permitted under both the first lien credit agreement and the second lien credit agreement and, more importantly, in connection with enforcement by the first lien creditors.

While important in U.S. second lien intercreditors, the release provisions are arguably the most important provision of European second lien intercreditors. Under European intercreditor agreements, in connection with enforcement by the senior creditors (or a "distressed disposal"), the junior security and debt and guarantee claims can be released (or disposed of) subject to negotiated conditions. Market practice continues to evolve, but fair sale provisions are increasingly common, i.e., public auction/sale process or independent fair value opinion. The LMA intercreditor agreement requires the security agent to take reasonable care to obtain a fair market price/value and permits the sale of group entities and release of debt and guarantee claims, and, in addition, the sale of second lien debt claims. European intercreditor agreements typically provide that the security agent's duties will be discharged when (although this list is not exhaustive): (i) the sale is made under the direction/control of an insolvency officer; (ii) the sale is made pursuant to an auction/competitive sales process (which does not exclude second lien creditors from participating unless adverse to the sales process); (iii) the sale is made as part of a court supervised/approved process; or (iv) a "fairness opinion" has been obtained. Any additional parameters/conditions to the above will be negotiated, particularly in deals where specialist second lien funds are anchoring the second lien facility. Typical points for discussion will be: (i) the circumstances in which/whether the senior creditors are entitled to instruct a sale in reliance on a fair sale opinion rather than a public auction; (ii) terms of any public auction (i.e. how conducted, on whose advice, who can participate, who can credit bid); (iii) any requirement for cash consideration; and (iv) any information/consultation rights.

In addition to the release provisions, European second lien intercreditors typically allow (subject to the fair sale provisions discussed above) the security agent to transfer the junior lien debt, intragroup liabilities and/or shareholder loans to the purchasers of the assets in an enforcement situation. The disposal of liabilities option could be more tax efficient than cancelling the subordinated debt in connection with enforcement.

Many of these conditions with respect to sales of collateral are absent in U.S. second lien intercreditors because meaningful protections are afforded by the Uniform Commercial Code requirement for a sale of collateral to be made in a commercially reasonable manner and, in the case of a 363 sale process, by a court-approved sale in Chapter 11, as discussed more fully below.

In addition, the release provisions in U.S. second lien intercreditors are also premised on the first lien and second lien security interests being separately held by the first lien collateral agent and the second lien collateral agent and documented in separate, but substantially similar, documents that are meant to cover identical pools of collateral. In European second lien intercreditors, the release provisions assume that one set of security interests are held by one security agent on behalf of all of the creditors (senior and second lien).

5. Limitation on First Lien Obligations

U.S. second lien financings typically include a "first lien debt cap" to limit the amount of first lien obligations that will be senior to the second lien obligations. The analogous provision in European second lien intercreditors is referred to as "senior headroom". Amounts that exceed the first lien debt cap or senior headroom will not benefit from the lien priority provisions in the intercreditor agreement. The "cushion" under the first lien debt cap or senior headroom is meant to allow for additional cash needs of the borrower group, whether as part of a loan workout or otherwise.

The first lien debt cap in U.S. second lien financings is typically 110% to 120% of the principal amount of the loans and commitments under the first lien facilities on the closing date plus 100% to 120% of the principal amount of any incremental facilities (or equivalent) permitted under the first lien credit agreement on the closing date. The first lien debt cap is sometimes reduced by the amounts of certain reductions to the first lien commitments and funded loans (other than refinancings), e.g. mandatory prepayments. The first lien debt cap does not apply to hedging obligations and cash management obligations, which are generally included as first lien priority obligations without limitation (although the amounts are regulated by the covenants in the credit agreements). In addition, interest, fees, expenses, premiums and other amounts related to the principal amount of the first lien obligations permitted by the first lien debt cap are first lien priority obligations, but are generally not limited by the cap itself. The trend in U.S. second lien financings is to allow for larger first lien debt caps; some borrower-friendly U.S. second lien financings even allow for unlimited first lien obligations (subject of course to any covenants restricting debt in the applicable credit agreements and other debt documents, including the second lien credit agreement). Additional capacity is often also permitted in the case of DIP financings in the U.S. (as discussed below).

Senior headroom is typically set at 110% of senior term debt plus revolving commitments in European second lien intercreditors, although the headroom concept is of limited relevance where (as is now common on top-tier sponsor deals) it has not been extended to cover incremental and other additional senior debt. Ancillary facilities that would be provided in European deals *in lieu* of external cash management arrangements would be naturally limited by the amount of the revolving commitments since they are made available by revolving credit facility lenders in place of their revolving commitments. Hedging obligations are typically unlimited but naturally constrained to a degree by the fact that most credit agreements will restrict the borrower group from doing speculative trades.

6. Amendment Restrictions

In both U.S. second lien intercreditors and European second lien intercreditors, first lien lenders and second lien lenders typically specify the extent to which certain terms of the first lien credit agreement and the second lien credit agreement may not be amended without the consent of the holder of the other lien. Amendment restrictions are negotiated on a deal-by-deal basis and may include limitations on increasing pricing and limitations on modifications of maturity date and the introduction of additional events of default and covenants. The trend in U.S. second lien intercreditors, in particular in financings of borrowers owned by private equity sponsors, is for few (or no) amendment restrictions. European second lien intercreditors now tend to follow this U.S. approach.

7. Purchase Options

Both U.S. second lien intercreditors and European second lien intercreditors contain similar provisions whereby the second lien creditors are granted the right to purchase the first lien obligations in full at par, plus accrued interest, unpaid fees, expenses and other amounts owing to the first lien lenders at the time of the purchase. This purchase option gives the second lien creditors a viable alternative to sitting aside during an enforcement action controlled by the first lien creditors by allowing them to purchase the first lien claims in full and thereby acquire the ability to control the enforcement proceedings themselves.

The European version of the purchase option is similar but also includes a requirement to buy out the hedging obligations, which may or may not be included in U.S. second lien intercreditors.

The triggering events for the purchase option in U.S. intercreditors vary. They generally include acceleration of the first lien obligations in accordance with the first lien credit agreement and the commencement of an insolvency proceeding. Other potential trigger events include any payment default under the first lien credit agreement that remains uncured and unwaived for a period of time and a release of liens in connection with enforcement on shared collateral. The triggering event for the European version of the purchase option also varies and may include acceleration/enforcement by the senior creditors, the imposition of a standstill period on second lien enforcement action or the imposition of a payment block.

8. Common U.S. Bankruptcy Waivers

First lien secured parties in the U.S. try to ensure that the first lien secured parties control the course of the Chapter 11 proceeding to the maximum extent possible by seeking advanced waivers from the second lien secured parties of their bankruptcy rights as secured creditors (and, in some cases, as unsecured creditors) that effectively render the second lien secured parties "silent seconds". These waivers can be highly negotiated. However, U.S. second lien intercreditors routinely contain waivers from the second lien secured parties of rights to object during the course of a Chapter 11 proceeding to a debtor-in-possession facility (or "DIP facility"), a sale by the debtor of its assets free of liens and liabilities outside of the ordinary course of business during Chapter 11 proceedings, with the approval of the bankruptcy court (a section 363 sale) and relief from the automatic stay. (The automatic stay stops substantially all acts and proceedings against the debtor and its property immediately upon filing of the bankruptcy petition.)

The enforceability of the non-subordination-related provisions in U.S. second lien intercreditors is uncertain because there is conflicting case law in this area. However, garden-variety subordination-related provisions are regularly enforced by U.S. bankruptcy courts to the same extent that they are enforceable under applicable non-bankruptcy law pursuant to Section 510(a) of the Bankruptcy Code.

The second lien creditors in U.S. second lien intercreditors provide their advanced consent to DIP facilities by agreeing that, subject to certain conditions (including a monetary limit), they will not object to the borrower or any other obligor obtaining financing (including on a priming basis) after the commencement of a Chapter 11 process, whether from the first lien creditors or any other third-party financing source, if the first lien agent desires to permit such financing (or to permit the use of cash collateral on which the first lien agent or any other creditor of the borrower or any other obligor has a lien).

In the U.S., second lien claimholders often expressly reserve the right to exercise rights and remedies as unsecured creditors against any borrower or guarantor in accordance with the terms of the second lien credit documents and applicable law, except as would otherwise be in contravention of, or inconsistent with, the express terms of the intercreditor agreement. This type of provision, for the reasons articulated above, does not have a counterpart in and would be inconsistent with the underlying rationale of European second lien intercreditors.

9. Non-cash Consideration/Credit Bidding

The LMA intercreditor agreement includes explicit provisions dealing with the application of non-cash consideration (including "credit bidding") during the enforcement of security. Credit bidding facilitates debt-for-equity exchanges by allowing the security agent, at the instruction of the senior creditors, to distribute equity to senior creditors as payment of the senior debt or to consummate a pre-pack where the senior debt is rolled into a newco vehicle.

In the U.S., the term "credit bidding" refers to the right of a secured creditor to offset, or bid, its secured allowed claim against the purchase price in a sale of its collateral under section 363(k) of the Bankruptcy Code, thereby allowing the secured creditor to acquire the assets that are subject to its lien in exchange for a full or partial cancellation of the debt. In U.S. second lien intercreditors, the second lien creditors consent to a sale or other disposition of any shared collateral free and clear of their liens or other claims under section 363 of the Bankruptcy Code if the first lien creditors have consented to the sale or disposition. However, the second lien creditors often also expressly retain the ability to credit bid their second lien debt for the assets of the borrower and guarantors so long as the first lien obligations are paid in full in cash. In European intercreditor agreements, the second lien creditors would not typically have an explicit right to credit bid their second lien debt.

10. The Holders of Shareholder Obligations and Intragroup Obligations

In addition to direct equity contributions, shareholder loans are often used in European capital structures. Shareholder loans are less common in U.S. capital structures and, if present in the capital structure, would likely be subordinated to the credit agreement obligations under a separately documented subordination agreement (i.e., not included as part of the typical U.S. second lien intercreditor agreement). Similarly, holders of intragroup liabilities would also not be included in U.S. second lien intercreditor agreements. The treatment of intragroup liabilities is often negotiated by the borrower and arrangers in U.S. syndicated credit agreements and, although results differ, the intragroup liabilities are often required to be documented by an intercompany note and made subject to an intercompany subordination agreement. The intercompany subordination agreement would subordinate the intragroup liabilities to be paid by the loan parties to their credit facility obligations and would generally include a payment blockage in relation to intragroup liabilities payable by borrowers and guarantors under the credit facilities during the continuation of an "acceleration event".

Blended Approach Taken in Recent Transatlantic Intercreditor Agreements

Recent intercreditor agreements for financings involving primarily non-U.S. companies in U.S. syndicated bank loan financings, and using NY-law governed loan documents, have taken different approaches to the intercreditor terms, which seem to be determined on a deal-by-deal basis depending on several considerations: (1) the portion of the borrower group's business located in the U.S.; (2) the jurisdiction of organisation of the borrower; (3) the likelihood of the borrower group filing for U.S. bankruptcy protection; and (4) the relative negotiating strength of the junior lien creditors and the borrower, who will be inclined to favour future flexibility and lower upfront legal costs. For these and other reasons, seemingly similar financings have taken very different approaches. Some intercreditor agreements ignore the complexities of restructuring outside of the U.S. and simply use a U.S.-style intercreditor agreement; other similar financings have been documented using the opposite approach – by using a form of intercreditor agreement based on the LMA intercreditor agreement; and still other similar financings have sought to blend the two approaches or to adopt an intercreditor agreement in the alternative by providing for different terms (in particular different release provisions) depending on whether a U.S. or non-U.S. restructuring is to be pursued. Given all of these various considerations, Transatlantic Intercreditor Agreements remain varied. We have highlighted below some of the more interesting points:

- the parties typically have included the holders of intra-group liabilities and shareholder loans, following the European approach, and have embedded restrictions on payment of the intra-group liabilities and shareholder loans under certain circumstances;
- the enforcement instructions are typically required to come from a majority of the first lien loans and unfunded commitments in the U.S.-style while the actual exposures of hedge counterparties (plus mark to market positions post-credit agreement discharge) are taken into account in calculating that majority in the European style;
- the European-style release provisions discussed above generally have been included either as the primary method of release or as an alternative method in the event that a U.S. bankruptcy process is not pursued;
- in certain deals, enforcement standstill and turnover provisions have been extended to cover all enforcement actions and recoveries (broadly defined), rather than just relating to collateral enforcement actions;
- claim subordination of the second lien debt has typically ***not*** been included;
- the full suite of U.S. bankruptcy waivers from the second lien creditors generally have been included; and
- it is sometimes the case, based on the underlying rationale of European intercreditors, that secured or (above an agreed threshold amount) unsecured incremental and refinancing debt (whether *pari passu* or subordinated) is required to be subject to the intercreditor agreement, primarily to ensure it can be released upon an enforcement of this group.

In addition, other provisions appear in Transatlantic Intercreditor Agreements that will not be familiar to those accustomed to the typical U.S. second lien intercreditors, such as parallel debt provisions (a construct necessary in certain non-U.S. jurisdictions in which a security interest cannot be easily granted to a fluctuating group of lenders), expanded agency provisions for the benefit of the security agent and special provisions necessitated by specific local laws to be encountered (or avoided) during the enforcement process (e.g., French *sauvegarde* provisions and compliance with U.S. FATCA regulations).

Conclusion

As the number of financings that touch both sides of the Atlantic continues to rise and the complexity of such financings increases, the intercreditor arrangements for multi-jurisdictional financings will continue to be important and interesting. Whilst there is not a standard or uniform approach to documenting such intercreditor terms, there is now a broad understanding on both sides of the Atlantic in relation to the different provisions and their underlying rationale. Accordingly, most transactions are implemented on a blended basis, combining many of the above-mentioned European or US elements into a US or European intercreditor, respectively. Having said this, as was the case with European second lien intercreditor agreements, a uniform approach is unlikely to emerge until the new forms of Transatlantic Intercreditor Agreement are stress tested in cross-border restructurings.

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Summary of Key Terms of U.S. Second Lien Intercreditor Agreements and European Second Lien Intercreditor Agreements			
Key Terms	**Traditional U.S. Second Lien Approach**	**Traditional European Second Lien Approach**	**Hybrid/Transatlantic Approach**
Parties to the Intercreditor Agreement	The first lien agent and the second lien agent and executed or acknowledged by the obligors.	The first lien agent and lenders, the second lien agent and lenders and the obligors, the obligors' hedge providers, ancillary facility lenders, the lenders of intra-group loans, the lenders of shareholder loans and the security agent.	Generally follows the European approach, except with respect to each lender executing the intercreditor agreement.
Enforcement Instructions	First lien agent takes instructions from lenders holding 50% of the loans and unfunded commitments under the first lien credit agreement.	Security agent takes instructions from creditors holding 66 ⅔% of the sum of (i) amounts under the senior credit agreement, and (ii) any actual exposure under hedging agreements.	Generally follows the U.S. approach, but may include hedge counterparties.
Scope of Enforcement Standstill Provisions	Only applies to enforcement against shared collateral (i.e., lien subordination).	Fulsome enforcement standstill including payment default and acceleration (i.e., payment subordination).	Generally follows the European approach, but depends on negotiation.
Length of Enforcement Standstill Provisions	Typically 180 days but could be from 90 to 180 days depending on negotiation.	Typically (i) 90 days (in most cases) following notice of payment default under the senior credit agreement, (ii) 120 days (in most cases) following notice of financial covenant default under the senior credit agreement, and (iii) 150 days (in most cases) following notice of any other event of default under the senior credit agreement, plus (in some cases) 120 days if the security agent is taking enforcement action.	Generally follows the U.S. approach, but depends on negotiation.
Payment Blockages	None.	Included.	Generally not included.
Releases of Collateral and Guarantees	Releases of collateral included.	Releases of claims included.	Generally follows the European approach.
Limitation on First Lien Obligations	Typically 110% to 120% of the principal amount of the loans and commitments under the first lien facilities on the closing date plus 100% to 120% of the principal amount of any incremental facilities (or equivalent) permitted under the first lien credit agreement on the closing date plus secured hedging and other secured obligations.	Similar to the U.S. approach.	Similar to the U.S. approach.
Amendment Restrictions	May be included depending on negotiation.	Typically included but limited to day-one senior credit agreement.	Generally follows the U.S. approach.
Second Lien Purchase Options (to purchase the First Lien Obligations)	Included.	Included.	Included.
Common U.S. Bankruptcy Waivers	Included.	Not included.	Included.
Non-Cash Consideration/Credit Bidding by First Lien Lenders	Included.	Included.	Included.
Shareholder Obligations	Not included.	Included.	Often included.
Intragroup Obligations	Not included. Often covered by a separate subordination agreement.	Included.	Often included.
Material Unsecured Debt	Not included.	Often included (above a threshold).	Similar.

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- Working capital and letter of credit facilities.
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- Restructurings.
- Vendor financings.
- Structured financings.
- Asset-based lending and securitisation.

A Comparison of Key Provisions in U.S. and European Leveraged Loan Agreements

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There are many broad similarities in the general approach taken to European and U.S. leveraged loan transactions and terms in the documentation of U.S. and European leveraged loans continue to converge with one another (and, in the case of larger leverage transactions, with high-yield bond terms). Supply of leveraged loans in both markets has not kept pace with the growing demand of leveraged loan investors which has fostered an extremely borrower-friendly environment and consistently oversubscribed deals, and sponsors and borrowers in both the U.S. and European loan markets have been increasingly successful in pushing the boundaries of once standard lender protections. But there are also significant differences in commercial terms and overall market practice in the U.S. and European leveraged loan markets. The importance for practitioners and loan market participants to understand the similarities and differences of both markets has grown in recent years as sophisticated European and U.S. investors now routinely seek to access whichever market may provide greater liquidity (and potentially more favourable pricing and terms) at any given time.

This chapter will focus only on a number of the more significant key differences between practice in the United States and Europe that may be encountered in a typical leveraged loan transaction, and is intended to serve as an overview and a primer for practitioners. References throughout this article to "U.S. loan agreements" and "European loan agreements" should be taken to mean New York-law governed and English-law governed leveraged loan agreements, respectively.

Divided into four parts, Part A will focus on differences in documentation and facility types, Part B will focus on various provisions, including covenants and undertakings, Part C will consider differences in syndicate management and Part D will focus on recent legal and regulatory developments in the European and U.S. markets.

Part A – Documentation and Facility Types

Form Documentation

In both the European and U.S. leveraged loan markets, the standard forms used as a starting point for negotiation and documentation greatly influence the final terms. In Europe, both lenders and borrowers, through conduct adopted over a number of years, expect the starting point to be one of the very comprehensive "recommended forms" published by the LMA (or, to give it its formal title, the Loan Market Association) unless exceptional circumstances merit a more bespoke approach. However, in the United States, such practice has not emerged and the form on which the loan documentation will be based (as well as who "holds the pen" for drafting the documentation) – which may greatly influence the final outcome – will be the subject of negotiation at an early stage.

The LMA (comprised of more than 630 member organisations, including commercial and investment banks, institutional investors, law firms, service providers and rating agencies) has achieved widespread acceptance of its recommended forms as a result of the breadth of its membership and the spread of constituencies represented at the "board" level. Formed initially with the objective of standardising secondary loan trading documentation, the LMA now plays a "senior statesman" advisory role in the European loan market by producing, updating and giving guidance on key provisions in its recommended forms for, amongst other things, investment grade loan transactions, leveraged acquisition finance transactions, developing market and commodity finance transactions, real estate finance transactions and most recently, the growing European private placement market. The LMA plays an active role in monitoring developments in the financial markets, responding to regulatory consultation requests and giving guidance on appropriate approaches in documentation in response to market, regulatory and political developments (indeed, most recently in the context of the outcome of the United Kingdom's referendum to leave the European Union and the decision to phase out LIBOR): its influence and authority is significant.

The widespread use of the LMA standard forms has resulted in good familiarity by the European investor market which, in turn, has added to the efficiency of review and comprehension not just by those negotiating the documents but also by those who may be considering participating in the loan. The LMA recommended forms are only a starting point, however, and whilst typically, the "back-end" LMA recommended language for boilerplate and other non-contentious provisions of the loan agreement will be only lightly negotiated (if at all), the provisions that have more commercial effect on the parties (such as mandatory prepayments, business undertakings, financial covenants, representations and warranties, transfer restrictions, conditions to drawdown, etc.) remain as bespoke to the specific transaction as ever.

Similar to the LMA in Europe, the Loan Syndications and Trading Association (the "LSTA") in the United States (an organisation of banks, funds, law firms and other financial institutions) was formed to develop standard procedures and practices in the trading market for corporate loans. One of the main practical differences from the LMA, however, is that although the LSTA has developed recommended standard documentation for loan agreements, those forms are rarely used as a starting draft for negotiation. Instead, U.S. documentation practice has historically been based on the form of the lead bank or agent although many banks' forms incorporate

LSTA recommended language. In relation to market and regulatory developments that could affect both loan markets as a whole, the LSTA and LMA often cooperate and coordinate their approach in issuing guidance and recommended language.

Whilst traditionally, the lender side has "held the pen" on documentation, there is a growing trend, both in the United States and Europe, for the larger sponsor borrowers to insist on taking control of, and responsibility for, producing the key documents which, inevitably, leads to a more borrower-friendly starting point.

Facility Types

The basic facility types in both U.S. and European leveraged loan transactions are very similar. Each may typically provide for one or more term loans (ranking equally but with different maturity dates, amortisation profiles (if amortising) and interest rates) and a *pari passu* ranking revolving credit facility. Of course, depending on the nature of the borrower's business and objectives, there could be other specific, standalone facilities, such as facilities for acquisitions, capital expenditure and letters of credit.

In the United States, as in Europe, typically all lenders in a given facility share the same security package, the same ability to enforce such security and the same priority in relation to payments and the proceeds from the enforcement of security. In the U.S., as in Europe, however, an alternative to the typical structure is the first lien/second lien structure, in which the "first lien" and "second lien" loans are secured by the same collateral but the liens of the second lien lenders are subordinated to those of the first lien lenders (i.e., no collateral proceeds may be applied to any second lien obligations until all first lien obligations are repaid). First lien/second lien structures were traditionally treated as essentially two separate loans, with two sets of loan documents and two agents, with the relationship between the lenders set out and governed under an intercreditor agreement. In the U.S., however, over recent years, a market trend has developed for certain transactions (typically the smaller deals) to instead effect a "first lien/second lien" structure through a unitranche facility: a single loan with two tranches, a first out tranche and a last out tranche, so there is only one set of loan documents, one agent, one interest rate and one set of lenders. A separate agreement among lenders ("AAL") governs the rights and obligations of the first out and last out lenders and also the division of the interest receipts between the lenders (the borrower pays a blended rate and the lenders decide how much of that is paid to the first out lenders and how much to the last out, depending on the market appetite for the different levels of risk). One unknown with respect to unitranche facilities was whether a court presiding over a borrower's bankruptcy could construe and enforce an AAL even though borrowers are not party to AALs. The *In re RadioShack Corp.* bankruptcy litigation largely resolved this question by implicitly recognising the court's ability to interpret and enforce an AAL.

In Europe, driven by the rising prominence of debt funds and alternative capital providers, unitranche and direct loan facility structures are playing a much more significant role in the debt market, particularly in the sub £250m deal bracket. Similarly to U.S. unitranche structures, European unitranche structures also utilise an AAL, to which typically the borrower will not be party. In a restructuring context, European unitranche structures have also raised their own issues – in particular, questions around whether the first out and last out creditors comprise a single class for the purposes of an English law scheme of arrangement under Part 26 of the Companies Act 2006, notwithstanding the various creditors' distinct economic positions and interests as set out in the AAL. Whilst unitranche structures and the rights of unitranche creditors in a scheme of arrangement have not been directly considered by the courts, recent cases suggest that unless creditors can demonstrate that their distinct economic rights are also accompanied by corresponding legal rights enforceable against the borrower (which will not typically be the case where the borrower is not party to the AAL), it is likely to be difficult for junior creditors to maintain that they should form a separate class in a scheme of arrangement (and, as such, forfeiting the potential hold-out value that may entail during the course of a borrower's restructuring).

In the case of European borrowers with both high-yield bond debt and bank debt (usually revolving credit facilities) in their capital structures, so called "super senior" structures are also very common. In such structures, both the lenders under the revolving credit facility and the high yield noteholders rank equally in regards to payment and the security package (where the notes are secured). However, the lenders under the revolving credit facility are "super senior" in that they take priority over the noteholders in relation to the proceeds of recovery from any enforcement action.

Term Loan Types

The terms of a financing are influenced not just by the size and nature of the transaction but also to a large extent by the composition of the lending group. Term A loans are syndicated in the United States to traditional banking institutions, who typically require the amortisation and tighter covenants characteristic of Term A loans. Term B loans, which comprise a large percentage of the more sizeable leveraged loans (especially in the United States), are typically held by investors who also participate in high-yield debt instruments and so are generally comfortable with no financial maintenance covenants and greater overall covenant flexibility. Term B loans have a higher margin and other economic protections (such as "no-call" periods) not commonly seen in Term A loans to compensate for these more "relaxed" terms.

Whilst in the past European sponsors and borrowers unable to negotiate sufficiently flexible or desirable loan terms with their usual relationship banks had to resort to U.S. Term B loans and the U.S. high-yield bond market in order to achieve the flexibility they desired, the growth of debt funds, direct lenders and U.S. institutional investors in the European loan market (who now vigorously compete with banks and other traditional lending institutions) has led to the evolution of the English law "European TLB" market. Indeed, the European TLB market is now an established and attractive funding option for borrowers in larger leveraged transactions (£250m of debt or greater), albeit that some terms are not yet quite as flexible as those seen in the U.S. Term B loan market. Notwithstanding the success of many larger borrowers and sponsors in the European TLB market in negotiating very generous borrower-friendly relaxations in their loan covenants (in particular relating to debt capacity, permitted disposals and acquisitions, and financial covenant cure rights, to the extent the loan is not "covenant lite"), most European TLB instruments are still likely to contain strict guarantor coverage tests (requiring the accession of additional guarantors and the provision of additional security if the required test thresholds are not met), higher lender consent thresholds, as well as more expansive events of default and mandatory prepayment provisions.

Certainty of Funds

In the United Kingdom, when financing an acquisition of a U.K. incorporated public company involving a cash element, the City Code on Takeovers and Mergers requires purchasers to have "certain funds" prior to the public announcement of any bid. The bidder's financial advisor is required to confirm the availability of the funds and, if it does not diligence this appropriately, may be liable to provide the funds itself should the bidder's funding not be forthcoming. Understandably, both the bidder and its financial advisor need to ensure the highest certainty of funding. In practice, this requires the full negotiation and execution of loan documentation and completion of conditions precedent (other than those conditions that are also conditions to the bid itself) at the point of announcement of the public bid.

Whilst not a regulatory requirement, the concept of "certain funds" has also permeated the private buyout market in Europe, so that sponsors are (in practice) required to demonstrate the same level of funding commitment as if they were making a public bid, albeit that this is not a legal or regulatory requirement in a private bid.

In the United States, there is no regulatory certain fund requirement as in the United Kingdom and, typically, only commitment papers, rather than full loan documents, are executed at the time when the bid becomes binding on the bidder (that is, upon execution of a purchase agreement). In the U.S., though, it has become more common for parties to agree on terms while negotiating the commitment letter that traditionally were not settled until negotiation of the definitive loan documentation, such as the definition of EBITDA and related terms, baskets and specified levels for negative covenants and incurrence tests for debt, restricted payments and investments. Ordinarily, when commitment papers are conditioned on the negotiation of definitive loan documentation, they contain "*SunGard*" clauses that limit the representations and warranties made by the borrower and the delivery of certain types of collateral required by the lenders on the closing date of the loan. In practice, given the level of commitment implicit in NY law commitment papers and the New York law principle of dealing in good faith, there is probably little difference between "certain funds" and SunGard commitment papers though it is still most unlikely that SunGard would be acceptable in a City Code bid.

Part B – Loan Documentation Provisions

Covenants and Undertakings

Whilst the dominant theme of recent years has been the increasing European adoption from the U.S. of more flexible, borrower-friendly loan provisions – or "convergence" as it is commonly referred to – there still remains many differences between U.S. and European loan agreements in the treatment and documentation of covenants (as such provisions are termed in U.S. loan agreements) and undertakings (as such provisions are termed in European loan agreements). This Part B explores some of those differences.

Both U.S. and European loan agreements use a broadly similar credit "ring fencing" concept, which underpins the construction of their respective covenants/undertakings. In U.S. loan agreements, borrowers and guarantors are known as "loan parties", while their European equivalents are known as "obligors". In each case, loan parties/obligors are generally free to deal between themselves as they are all within the same credit group and bound under the terms of the loan agreement. However, to minimise the risk of credit leakage, loan agreements will invariably restrict dealings between loan parties/obligors and other members of the borrower group that are not loan parties/obligors, as well as third parties generally. In U.S. loan agreements there is usually an ability to designate members of the borrower's group as "unrestricted subsidiaries" so that they are not restricted under the loan agreement. However, the loan agreement will then limit dealings between members of the restricted and unrestricted group and the value attributed to the unrestricted group might not be taken into account in calculating financial covenants. Borrowers are negotiating for more flexibility with respect to unrestricted subsidiaries but lenders have been pushing back due to recent attempts by borrowers to use these unrestricted subsidiaries to consummate transactions not intended to be permitted. Whilst not historically a feature of the European loan market, the use of the "restricted/unrestricted" subsidiary construct is now also sometimes seen in European loan agreements, particularly in the context of European TLB instruments.

Restrictions on Indebtedness

U.S. and European loan agreements include an "indebtedness covenant" (in U.S. loan agreements) or a "restriction on financial indebtedness" undertaking (in European loan agreements) which prohibits the borrower (and usually, its restricted subsidiaries) from incurring indebtedness unless explicitly permitted. Typically, "indebtedness" will be broadly defined in the loan agreement to include borrowed money and other obligations such as notes, letters of credit, contingent and lease obligations, hedging liabilities (on a mark-to-market basis), guaranties and guaranties of indebtedness.

In U.S. loan agreements, the indebtedness covenant prohibits all indebtedness, then allows for certain customary exceptions (such as the incurrence of intercompany debt, certain acquisition debt, certain types of indebtedness incurred in the ordinary course of business or purchase money debt), as well as a specific list of exceptions tailored to the business of the borrower. The indebtedness covenant will also typically include an exception for a general "basket" of debt, which can take the form of a fixed amount or a formula based on a ratio or a combination, such as the greater of a fixed amount and a ratio formula. Reclassification provisions (allowing the borrower to utilise one type of permitted debt exception and then reclassify the incurred permitted debt under another exception) are also becoming more common in the United States. Some U.S. loan agreements contain reclassification provisions applicable to lien covenants in addition to indebtedness covenants, permitting borrowers to reclassify transactions that were permitted under a fixed basket as permitted under an unlimited leveraged-based basket after the borrower's financial performance improves. Some agreements allow borrowers to use restricted payment capacity to incur debt. This is part of a more general trend of giving borrowers flexibility to use a basket designated for a specific purpose for another purpose.

The loan agreements of large cap and middle market U.S. borrowers also typically provide for an incremental facility allowing the borrower to incur additional debt under the credit agreement (on top of any commitments the credit agreement originally provided for), or in certain cases additional *pari passu* or subordinated secured or unsecured incremental debt outside the credit agreement under a separate facility (known as "sidecar facility" provisions). Traditionally the incremental facilities were limited to a fixed dollar amount, referred to as "free-and-clear" tranches, but now many borrowers can incur an unlimited amount of incremental loans so long as a *pro forma* leverage ratio or secured indebtedness ratio (if the new debt is to be secured) is met. Ratio incremental capacity has been expanding – for example, it is becoming more common to see unsecured incremental capacity subject to compliance with closing date leverage or with a specified interest coverage ratio (typically 2.00:1.00). The use of an interest coverage ratio for debt incurrence borrows from the high-yield bond world. Some deals include increased ratio incremental capacity for acquisitions by providing that the borrower may incur incremental term loans either if the borrower complies with a specified *pro forma* leverage test or if *pro forma* leverage is no greater than leverage immediately prior to the acquisition.

It is common for U.S. loan agreements to contain borrower-friendly incremental provisions. It is becoming more common for borrowers to have both a free-and-clear incremental basket and unlimited incremental capacity subject to a ratio test. Some such borrowers have negotiated the ability to refresh a free-and-clear basket by redesignating debt originally incurred under the free-and-clear basket as debt incurred under the leverage-based incremental capacity. Some U.S. loan agreements permit borrowers to simultaneously use the free and clear basket and the leveraged-based incremental basket without the former counting as leverage for purposes of the ratio test. Borrowers have also become more creative with provisions that allow for increases to the free-and-clear basket over the life of the loan, including *pro rata* increases in free-and-clear baskets upon voluntary prepayments of existing loans and/or voluntary reductions in revolving commitments and free-and-clear baskets with an EBITDA grower providing for an increase in the amount of the free-and-clear basket in tandem with increases in the borrower's EBITDA.

Most incremental facilities have a most-favoured nations clause that provides that, if the margin of the incremental facility is higher than the margin of the original loan, the original loan's margin will be increased to within a specific number of basis points (usually 50 bps but aggressive sponsors increasingly seek 75 bps or, in a recent deal, even 100 bps) of the incremental facility's margin. Sponsor-friendly loan agreements often include limitations with respect to most-favoured nation clauses, usually a "sunset" restricting its application to a certain timeframe, typically 12 months following closing (although the average duration of the "sunset" has been decreasing). Such sponsor-friendly agreements often incorporate further provisions aimed at eroding MFN protection, including (i) limiting MFN protection to incremental term loans borrowed using the free-and-clear capacity, refinancing incremental term loans or incremental term loans that mature within a certain period (say, two years) of the latest-maturing existing term loans, and (ii) setting a threshold amount of incremental term loans that may be borrowed without triggering MFN protection. Rather than providing that the MFN provision is limited to incremental loans incurred under the fixed incremental basket, some U.S. deals provide that MFN protection is limited to incremental term loans incurred under the ratio incremental capacity. This allows borrowers to incur incremental debt under the fixed incremental basket and then reclassify such debt as incurred under the ratio incremental capacity, thereby avoiding the MFN provision and refreshing their fixed incremental capacity.

U.S. loan agreements also typically include an exception to the debt covenant for refinancing debt. Historically, refinancing debt was subject to limitations as to principal amount, maturity, weighted average life to maturity, ranking and guarantees and security. The trend of looser terms in U.S. loan agreements is evident in innovative tinkering with the concept of refinancing debt, though. Traditionally borrowers could incur at most refinancing debt in a principal amount not to exceed the principal amount of the old debt plus accrued interest, fees and costs. But creative drafters have changed that limitation so that the principal amount of the refinancing debt can exceed the principal amount of the old debt (plus interest, fees, etc.) by up to the amount of any unused commitments. Borrowers can obtain commitments that they cannot immediately use because there is no capacity under any of their debt baskets, so this formulation can result in problems – e.g., consider a first lien loan agreement that permits second lien refinancing debt in an amount equal to the old debt plus incremental debt permitted by the second lien loan agreement. The borrower could obtain commitments for second lien refinancing debt exceeding the principal amount of its old second lien debt and then refinance and fully borrow under all the commitments it obtained, sidestepping its incurrence test and any need for first lien lender consent.

The restriction on financial indebtedness undertaking typically found in European loan agreements is broadly similar to its U.S. covenant counterpart and usually follows the same construct of a general prohibition on all indebtedness, followed by certain "permitted debt" exceptions (both customary ordinary course type exceptions as well as specifically tailored exceptions requested by the borrower). A notable recent trend in the European loan market (particularly in larger leveraged transactions) has been the relaxations around the ability of borrowers to incur additional debt. There is now a definitive trend towards U.S. style permissions, such as "permitted debt" exceptions based on a leverage and/or secured leverage (and sometimes interest coverage) ratio test combined with a general fixed permitted basket where such additional (or incremental) debt may be incurred within the loan agreement by way of an accordion facility, or outside the loan agreement by way of a separate side-car facility (demonstrated in the fact that the LMA now includes incremental facility language in its standard form documentation).

Indeed, uncapped, leverage ratio-based incremental debt capacity is now a standard feature of many recent large-cap European loan agreements, and most such agreements will also provide for soft-capped free-and-clear basket (in most cases set by reference to between 75% and 100% of EBITDA) which the borrower can use irrespective of whether it is able to meet the incremental debt ratio test. As in the case of U.S. loan agreements, European loan agreements with incremental facility provisions will invariably also contain MFN protections. Over the last year, borrowers in the European loan market have been successful in achieving relatively aggressive sunset (expiration) periods in respect of such MFN protections. Sunset periods of six to 12 months are now very common, compared to the 18 month periods which were previously the norm.

Restrictions on Granting Security/Liens

U.S. loan agreements will also invariably restrict the ability of the borrower (and usually, its subsidiaries) to incur liens. A typical U.S. loan agreement will define "lien" broadly to include any charge, pledge, claim, mortgage, hypothecation or otherwise any arrangement to provide a priority or preference on a claim to the borrower's property. This lien covenant prohibits the incurrence of all liens but provides for certain typical exceptions, such as liens securing permitted refinancing indebtedness, purchase money liens, statutory liens and other liens that arise in the ordinary course of business, as well as a general basket based on a fixed dollar amount or a percentage of consolidated total assets or EBITDA to secure a specified amount of permitted indebtedness. In some large cap deals, both in the U.S. and in Europe, borrowers are able to secure permitted indebtedness based on a total leverage ratio or senior secured leverage ratio.

The European equivalent, known as a "negative pledge", broadly covers the same elements as the U.S. restriction on liens (with the same business driven exceptions, but typically goes further and restricts "quasi-security" where the arrangement or transaction is entered into primarily to raise financial indebtedness or to finance the acquisition of an asset. "Quasi-security" includes transactions such as sale and leaseback, retention of title and certain set-off arrangements.

Restriction on Investments

A restriction on the borrower's ability to make investments is commonly found in U.S. loan agreements. "Investments" include loans, advances, equity purchases and other asset acquisitions.

Historically, investments by loan parties in non-loan parties have been capped at modest amounts. In some large cap deals, however, loan parties have been permitted to invest uncapped amounts in any of their restricted subsidiaries, including foreign subsidiaries who are not guarantors under the loan documents. Other generally permitted investments include short-term securities or other low-risk liquid investments, loans to employees and subsidiaries, and investment in other assets which may be useful to the borrower's business. In addition to the specific list of exceptions, U.S. loan agreements also include a general basket, sometimes in a fixed amount, but increasingly based on a flexible "builder basket" growth concept.

The "builder basket" concept, typically defined as a "Cumulative Credit" or an "Available Amount", represents an amount the borrower can utilise for investments, restricted payments (as discussed below), debt prepayments or other purposes. Traditionally, the builder basket begins with a fixed-dollar amount and "builds" as retained excess cash flow (or in some agreements, consolidated net income) accumulates. Some loan agreements may require a borrower to meet a *pro forma* financial test to use the builder basket. If the loan agreement also contains a financial maintenance covenant (such as a leverage test), the borrower may also be required to satisfy a tighter leverage ratio to utilise the builder basket for an investment or restricted payment. Some sponsors have also negotiated loan documents that allow the borrower to switch between different builder basket formulations for added flexibility. Another new borrower-friendly development is the use of adjusted EBITDA to determine the seeded amount of the builder basket. In another example of convergence with high-yield bond indentures, many U.S. loan agreements have builder baskets that use 50% of consolidated net income (including the proceeds of equity issuances and equity contributions) rather than retained excess cash flow and an interest coverage ratio rather than a leverage ratio have become more common. This approach gives borrowers more flexibility because a basket using consolidated net income is usually larger and an interest coverage ratio is usually easier to comply with than a leverage ratio.

Investment covenant exceptions in U.S. deals are becoming increasingly permissive. Deals sometimes include unlimited ability to invest in and acquire non-guarantor restricted subsidiaries or provide that capacity for investments in non-loan parties can be redesignated to the general basket, increasing general investment capacity. Another new creative investment covenant change is to provide that all restricted payment capacity may be used for investments. This has its roots in the high-yield bond market where investments are treated as a type of restricted payment.

One area where there has been noticeable loosening of investment capacity is with respect to investments in unrestricted subsidiaries. It is becoming more common to be able to use an increasing number of investment baskets for investments in unrestricted subsidiaries, including the general basket, the available amount basket, the ratio basket and the similar business basket. Some agreements further allow non-guarantor restricted subsidiaries to use any proceeds they receive from investments under other investment baskets to invest in unrestricted subsidiaries, converting all other investment baskets into unrestricted subsidiary investment capacity. All this increasing investment capacity, particularly regarding investments in unrestricted subsidiaries, can be problematic for the lenders to a borrower in need of cash because it allows the borrower to use its large amount of investment capacity to invest in an unrestricted subsidiary and then have that subsidiary borrow additional secured debt. Excessive investment capacity in unrestricted subsidiaries can also be used to increase the available amount restricted payment capacity upon the sale or redesignation of any investments in unrestricted subsidiaries.

European loan agreements will typically contain stand-alone undertakings restricting the making of loans, acquisitions, joint ventures and other investment activity by the borrower (and other obligors) and commonly restricted such activity by way of fixed cap baskets and other additional conditions. While the use of builder baskets is still not the norm (although on the rise) in European loan agreements, often acquisitions will be permitted if funded from certain sources, such as retained excess cash flow.

Whilst (historically) reference to ratio tests alone were not commonly seen in European loan agreements, it is now common for borrowers to be permitted to make acquisitions subject to satisfying a *pro forma* leverage ratio test (with fewer additional conditions on acquisitions generally). For stronger borrowers, it is becoming standard for there to be no restrictions on their ability to acquire entities that will become wholly-owned subsidiaries (as opposed to acquisitions of interests in joint ventures and other investments). Soft-capped baskets for acquisitions and investments (where the monetary limit is based on the greater of a fixed amount and a percentage of earnings or asset value) are also now more commonplace in the European market.

Restricted Payments

U.S. loan agreements will typically restrict borrowers from making payments on equity, including repurchases of equity, payments of dividends and other distributions, as well as payments on subordinated debt. As with the covenants outlined above, there are typical exceptions for restricted payments not materially adverse to the lenders, such as payments on equity solely in shares of stock, or payments of the borrower's share of taxes paid by a parent entity of a consolidated group. Similar to the trend toward broadening investment capacity, U.S. deals are incorporating increasingly permissive restricted payment baskets. For example, it is becoming more common to allow loan parties to dividend equity in unrestricted subsidiaries. Such a basket, together with the increasingly borrower-friendly investment covenant baskets described above which permit larger investments in unrestricted subsidiaries, give borrowers greater flexibility to move assets outside the credit group, such as by contributing assets to an unrestricted subsidiary using their broad investment capacity and then dividending the unrestricted subsidiary to the borrower's shareholders. Under the terms of agreements with these provisions, lenders would have no consent rights if this occurred. Another trend is the removal of event of default conditions on the use of baskets such as the available amount basket and the ratio restricted payment basket or the limiting of an event of default condition to only payment defaults and bankruptcy defaults.

In European loan agreements, such payments are typically restricted under separate specific undertakings relating to dividends and share redemptions or the making of certain types of payments to non-obligor shareholders, such as management and advisory fees, or the repayment of certain types of subordinated debt. As usual, borrowers will be able to negotiate specific carve-outs (usually hard capped amounts) for particular "permitted payments" or "permitted distributions" as required (for example, to permit certain advisory and other payments to the sponsor), in addition to the customary ordinary course exceptions.

In U.S. loan agreements, a borrower may use its "builder basket" or "Available Amount" (increasingly based on consolidated net income rather than retained excess cash flow as discussed above) for restricted payments, investments and prepayments of debt, subject to annual baskets based on either a fixed-dollar amount or compliance with a certain financial ratio test (typically closing date leverage for investments, half a turn inside closing date leverage for restricted payments and a quarter turn inside closing date leverage for junior debt prepayment). In some large cap and sponsored middle market deals in the United States, borrowers have been permitted to make restricted payments subject only to being in *pro forma* compliance with a specific leverage ratio, rather than meeting an annual cap or basket test.

European loan agreements typically have not provided this broad flexibility, although this is changing in the context of large-cap deals and the increasing role of the European TLB market. Whilst strong sponsors and borrowers have typically been able to negotiate provisions permitting payments or distributions from retained excess cash flow, subject to satisfying a certain leverage ratio, deal trends over the last 18 months have revealed that the U.S. approach towards allowing restricted payments is now being accepted in Europe: in particular, consolidated net income based "builder baskets" are now commonly seen in larger transaction, as well as uncapped upstream payment ability, subject to satisfaction of a *pro forma* leverage test, further illustrating the convergence of terms between the U.S. and European markets.

Call Protection

In both European and U.S. loan agreements, borrowers are commonly permitted to voluntarily prepay loans in whole or in part at any time. However, some U.S. loan agreements do include call protection for lenders, requiring the borrower to pay a premium if loans are repaid within a certain period of time (the "call period"). While "hard call" premiums (where term loan lenders receive the premium in the call period for any prepayment, regardless of the source of funds or other circumstances) are rare, "soft call" premiums (typically 1%) on prepayments made within a certain period (typically six months to a year after closing although 18 months has been becoming more common[1]) and funded from a refinancing or re-pricing of loans are common in the U.S. loan market. In some large cap deals, though, lenders waived call protection premiums in connection with a refinancing in connection with any transaction that would constitute an initial public offering, a change of control or, a transformative acquisition. Some deals include no call protection at all.

While call protection is relatively rare in the European market for senior (bank held, term loan A) debt, soft call protections (usually 1% in the first six-month call protection) are now common in European loans that have been structured to be sold or syndicated to institutional investors (for example, TLBs). Hard call protection provisions are more commonly seen in the second lien tranche of European loans and mezzanine facilities (typically containing a gradual step down in the prepayment premium from 2% in the first year, 1% in the second year, and no call protection thereafter).

Voluntary Prepayments and Debt Buybacks

Although debt buybacks have been less frequent in recent years, the provisions allowing for such prepayments are typically found in both U.S. and European loan agreements.

U.S. loan agreements typically require the borrower to offer to repurchase loans ratably from all lenders, in the form of a reverse "Dutch auction" or similar procedure. Participating lenders are repaid at the price specified in the offer and the buyback is documented as a prepayment or an assignment. Loan buybacks may also take the form of a purchase by a sponsor or an affiliate through non-*pro rata* open market purchases. These purchases are negotiated directly with individual lenders and executed through a form of assignment. Unlike loans repurchased by the borrower and then cancelled, loans assigned to sponsors or affiliates may remain outstanding. Lenders often cap the amount that sponsors and affiliates may hold and also restrict the right of such sponsors or affiliates in voting the loans repurchased.

Similarly, in European loan agreements, "Debt Purchase Transaction" provisions have been included in LMA recommended form documentation since late 2008. The LMA standard forms contain two alternative debt purchase transaction provisions – one that prohibits debt buybacks by a borrower (and its subsidiaries), and a second alternative that permits such debt buybacks, but only in certain specific conditions (for example, no default continuing, the purchase is only in relation to a term loan tranche and the purchase is made for consideration of less than par).

Where the loan agreement permits the borrower to make a debt purchase transaction, to ensure that all members of the lending syndicate have an opportunity to participate in the sale, it must do so either by a "solicitation process" (where the parent of the borrower or a financial institution on its behalf approaches each term loan lender to enable that lender to offer to sell to the borrower an amount of its participation) or an "open order process" (where the parent of the borrower or financial institution on its behalf places an open order to purchase participations in the term loan up to a set aggregate amount at a set price by notifying all lenders at the same time).

Both LMA alternatives permit debt purchase transactions by the sponsor (and its affiliates), but only subject to the disenfranchisement of the sponsor (or its affiliate) in respect the purchased portion of the loan.

Mandatory prepayments and change of control

U.S. borrowers are typically required to prepay loans incurred under their loan agreements using the net proceeds of certain asset sales, term debt not permitted to be incurred under the applicable loan agreement and issuances of equity. In many U.S. loan agreements, though, mandatory prepayment provisions relating to asset sales provide greater flexibility for borrowers by carving out more types of dispositions from the definition of asset sale, expanding the duration and scope of reinvestment rights, increasing the threshold amount under which the borrower need not use the proceeds to prepay, adding step-downs permitting borrowers to apply increasingly lower percentages of the net proceeds to prepayment as increasingly tighter leverage ratios are met and allowing the borrower to use asset sale proceeds to ratably prepay *pari passu* debt. Some U.S. loan agreements even exclude investment assets from the mandatory prepayment provision, effectively limiting the mandatory prepayment provision to assets owned at closing.

In U.S. loan agreements a change of control triggers an event of default rather than a mandatory prepayment as is commonly seen in European loan agreements. Recent Delaware Court of Chancery cases have applied increasing scrutiny to the continuing director change of control provisions. The issues raised in the cases include whether a change of control provision may restrict the ability of the existing board of directors to approve a dissident slate; whether a director breaches his fiduciary duty by failing to approve a dissident slate where such failure causes a change of control event of default under an existing credit agreement or indenture; and whether the administrative agent of a company's credit facility aids and abets a breach of fiduciary duty by such company's board due to adoption of a credit agreement containing a change of control provision restricting the ability of existing directors to approve a dissident slate.[2]

A new trend in the European loan market seen in 2017 has been the relative rise in "portability", allowing borrowers to avoid the usual mandatory prepayment upon a change of control of the borrower.

Whereas, historically, a mandatory prepayment of the loan facilities upon a change of control was a standard feature of European loan agreements, deal trends indicate that just over 10% of European leveraged loan agreements in 2017 allowed for some type of portability. It remains to be seen whether portability will become more prevalent in the European market.

Financial Covenants

Historically, U.S. leveraged loan agreements contained at least two maintenance financial covenants: total leverage; and interest coverage, typically tested at the end of each quarter.

In the United States, "covenant-lite" loan agreements containing no maintenance or ongoing financial covenants comprised more than 70% of new leveraged loans issued in the first three quarters of 2017 according to the S&P Leveraged Loan Index (up from 66% for fiscal year 2016 and 58% for fiscal year 2015) and have found their way into many middle market deals (after a poor showing in late 2014 and fiscal year 2015, the volume of covenant-lite middle market deals increased in each of 2016 and 2017). In certain transactions, the loan agreement might be "quasi-covenant-lite" meaning that it contains only one financial maintenance covenant (usually a leverage covenant) which is applicable only to the revolver and only when a certain percentage of revolving loans are outstanding at the testing date (15–25% is fairly typical, but has been as high as 37.5%). Covenant-lite (or quasi-covenant-lite) loan agreements may nonetheless contain other financial ratio incurrence tests – used merely as a condition to incurring debt, making restricted payments or entering into other specified transactions. Unlike maintenance covenants, incurrence based covenants are not tested regularly and a failure to maintain the specified levels would not, in itself, trigger a default under the loan agreement.

European loan agreements historically included a full suite of ongoing financial maintenance covenants. With the influx of institutional investors and increased demand generally affording borrowers increased bargaining power, "covenant-lite" and "covenant-loose" deal structures are much more prevalent, especially where it is intended that the loan will be syndicated to an institutional investor base. European deal activity in 2017 revealed that just over 80% of loan transactions were "covenant lite", meaning that the facility contained only a single financial covenant for the revolving facility lenders (usually a leverage ratio covenant tested on a springing basis) or contained no maintenance financial covenant at all. Springing covenants are typically tested only when the revolving facility is between 30% and 40% drawn (excluding backstopped letters of credit, non-backstopped letters of credit up to a threshold and, for a year or two after closing, closing date revolving borrowings up to a threshold amount). Some more aggressive deals include no cap on the exclusion of letters of credit.

In the United States, the leverage covenant historically measured consolidated debt of the Borrower and all its subsidiaries. Today, leverage covenants in U.S. loan agreements frequently apply only to the debt of the Borrower and its restricted subsidiaries. Moreover, leverage covenants sometimes only test a portion of consolidated debt – sometimes only senior debt or only secured debt (and in large cap deals of top tier sponsors sometimes only first lien debt). Lenders are understandably concerned about this approach as the covenant may not accurately reflect overall debt service costs. Rather, it may permit the borrower to incur unsecured senior or subordinated debt and still remain in compliance with the leverage covenant. This is not a trend that has yet found its way over to Europe.

In the event a U.S. loan agreement contains a leverage covenant, it invariably uses a "net debt" test by reducing the total indebtedness (or portion of debt tested) by the borrower's unrestricted cash and cash equivalents. Lenders sometimes cap the amount of cash a borrower may net out to discourage both over-levering and hoarding cash. The trends with regard to netting illustrated borrowers' rapidly increasing success in pushing for greater flexibility. The LSTA[3] reported that, in the third quarter of 2013, a sample of leveraged loan agreements revealed that nearly half had a fixed cap and the rest had unlimited netting – only a year later, in the third quarter of 2014, loan agreements with an unlimited cap had increased to three quarters of the sample. The percentage of uncapped loans grew to 85% in a sample of sponsor-leveraged loans in the third quarter of 2017.

In Europe, the total net debt test is tested on a consolidated group basis, with the total net debt calculation usually including the debt of all subsidiaries (excluding intra-group debt). Unlike the cap on netted cash and cash equivalents in some U.S. loan agreements, European borrowers net out all free cash in calculating compliance with the covenant.

With strong sponsor backing, borrowers have increasingly eased the restriction of financial covenants by increasing the amount of add-backs included in the borrower's EBITDA calculation. Both U.S. and European loan documents now include broader and more numerous add-backs including transaction costs and expenses, restructuring charges, payments to sponsors and certain extraordinary events. Recently many borrowers have negotiated add-backs (generally to the extent reasonably identifiable and factually supportable) for projected and as-yet unrealised cost savings and synergies. Add-backs have also become increasingly vague and flexible – for example, addbacks 'of a type' similar to those in the model delivered to arrangers during syndication or cost savings addbacks without a requirement relating to when the savings materialise. The Leveraged Lending Guidance and the federal regulatory agencies enforcing it (discussed further in Part D), though, suggest that regulators may apply heightened scrutiny to definitions of EBITDA that provide for add-backs without "reasonable support". This regulatory scrutiny has led to greater negotiation of EBITDA add-backs for projected improvements in operating results, resulting in more frequent use of limits on the timing for the realisation of anticipated synergies, administrative agent approval of add-backs and caps on savings and synergies add-backs, either by reference to a fixed amount or a certain percentage of EBITDA, typically around 15–20% in the United States (although in 2016 one study found that an increasing number of loans had a 25% cap) and 5–20% in Europe. Uncapped add-backs are becoming more common both in the US and European markets, however, in spite of regulatory scrutiny. In the third quarter of 2017 alone, there was a 10% increase in sponsor deals with uncapped add-backs.

Some recent U.S. deals with uncapped cost savings add-backs further provided for no time period during which such cost savings must be realised. Typical deals would include a time period ranging from 12 to 24 months (occasionally 36 months), so this development is further evidence of loosening loan terms and the power of sponsors. There has also been a trend of increasingly broad and vague language in EBITDA add-backs (such as the inclusion of all "business optimisation" expenses) which is potentially fertile ground for inflating EBITDA with arguable add-backs. These vague and broad add-backs, together with the uncapped add-backs that may never be realised within the term of the agreement and the other pro-borrower developments regarding add-backs, may weaken the ability of maintenance covenants to protect lenders and artificially permit borrowers even more flexibility to use both their "ratio" baskets. In addition, it is becoming markedly more common for "grower" baskets to be based on EBITDA rather than consolidated total assets, which compounds the potential threat to creditors from these permissive add-back trends.

In Europe, the European Central Bank (the "ECB") has published draft leveraged lending guidelines (discussed further in Part D).

Whilst still in the consultation process (as at the time of writing), the ECB guidelines (unlike its US counterpart) currently intend to test leveraged transactions by reference to "unadjusted" EBITDA, meaning "*realised EBITDA over the previous 12 months with no adjustments made for non-recurring expenses, exceptional items and other one-offs*".

Equity Cures of Financial Covenants

For the majority of sponsor deals in the United States, loan agreements that contain financial maintenance covenants also contain the ability for the sponsor to provide an "equity cure" for non-compliance. The proceeds of such equity infusion are usually limited to the amount necessary to cure the applicable default, and are added as a capital contribution (and deemed added to EBITDA) for this purpose. Because financial covenants are meant to regularly test the financial strength of a borrower independent of its sponsor, U.S. loan agreements increasingly place restrictions on the frequency (usually no more than two fiscal quarters out of four) and absolute number (usually no more than five times over the term of the credit facility) of equity cures.

In Europe, equity cure rights have been extremely common for many years. As in the United States, the key issues for negotiation relate to the treatment of the additional cure equity, for example, whether it should be applied to increase cash flow or earnings, or to reduce net debt (and, if so, whether it should also be applied in prepayment of the facilities). While historically it was restricted to the latter, European deal activity over the last couple of years has revealed a definitive trend towards "EBITDA cures" – that is, cure amounts being treated as an increase in earnings rather than as a reduction in net debt. In 2017, over 80% of all loan agreements with equity cures allowed for such EBITDA cures. Similar restrictions apply to equity cure rights in European loan documents as they do in the United States in respect of the frequency and absolute number of times an equity cure right may be utilised – however, in Europe the frequency is typically lower (and usually, an equity cure cannot be used in consecutive periods) and is subject to a lower overall cap (usually, no more than two or three times over the term of the facility). Another key difference between the US and European approaches to equity cures is that, unlike in US loan agreements, "over-cures" are typically permitted in European loan agreements (that is, the ability to inject more equity proceeds than is actually required to cure any financial covenant non-compliance). Such an ability is advantageous to some borrowers by allowing them to obscure any possible future underperformance. Another emerging borrower-friendly trend seen in 2017 in the European loan market has been the "prepayment cure", which allows a borrower to avoid being tested against a springing financial covenant by simply prepaying its revolving loans to a level below the relevant springing test threshold (which, as noted above, is typically set at the revolving facility being over 35% to 40% drawn). In most cases, a "prepayment cure" will not require the borrower to cancel the facility by the amount prepaid, and the borrower will not be prohibited from redrawing the prepaid amounts after the (avoided) test date. From a documentation perspective, it is also important to note that there is no LMA recommended equity cure language.

Sanctions, Anti-Money Laundering and Anti-Bribery Provisions

A recent trend in both European and U.S. loan agreements is the increasing expansiveness of (and lender focus on) the representations, warranties and covenants relating to anti-bribery, anti-money laundering and sanctions laws locally and abroad (the "Anti-Corruption/Sanctions Laws") coupled with lenders' increasing rigidity and resistance to negotiation with regard to these expansive Anti-Corruption/Sanctions Laws provisions. In the U.S. market context, additional evidence of this trend is that *SunGard* provisions (discussed in Part A) increasingly identify representations with respect to Anti-Corruption/Sanctions Laws as specified representations. Similarly in the European market, lenders invariably insist on such representations being characterised as "major representations" for certain funds purposes. Negotiation of these provisions may focus on whether it is appropriate to limit these provisions by materiality and/or by knowledge. Both European and U.S. borrowers often are concerned about their ability to fully comply with broadly drafted provisions without some form of knowledge, scope and/or materiality qualifiers.

Part C – Syndicate Management

Voting Thresholds

In U.S. loan agreements, for matters requiring a vote of syndicate lenders holding loans or commitments, most votes of "required lenders" require only a simple majority of lenders (that is, more than 50% of lenders by commitment size) for all non-unanimous issues. In European loan agreements, most votes require 66.67% or more affirmative vote of lenders by commitment size. In some, but not all, European loan agreements, certain votes that would otherwise require unanimity may instead require only a "super-majority" vote, ranging between 85–90% of lenders by commitment size. Such super majority matters typically relate to releases of transaction security or guarantees, or an increase in the facilities (though not an increase that might result in an obligation to fund on the part of the non-consenting lender).

"Unanimous" decisions in U.S. loan agreements are limited to fundamental matters and require the consent only of affected lenders (and are not, therefore, truly unanimous), while in European loan agreements (except where they may be designated as a super majority matter), decisions covering extensions to commitment periods, payment dates and reductions in amounts payable (even certain mandatory prepayment circumstances), changes to currencies and commitments, transfer provisions and rights between lenders all require the unanimous consent of lenders (not just those affected by the proposed changes).

Because of its adherence to requiring 100% lender consent to extend, the European market does not typically provide for amend and extend provisions that permit borrowers to extend their loan's maturity with only the consent of the extending lenders (which is not unusual in the U.S.). Instead, European borrowers have turned to the forward start facility, which is structured as a new loan agreement that sits beside the existing loan agreement but is not drawn until the existing facility matures. The forward start facility is used solely to refinance the indebtedness outstanding under the existing loan agreement.

Yank-a-Bank

U.S. loan agreements often contain provisions allowing the borrower to remove one or more lenders from the syndicate in certain circumstances. A borrower may, for example, remove a lender where such lender refuses to agree to an amendment or waiver requiring the unanimous consent of lenders, if the "required lenders" (typically more than 50% of lenders by commitment) have consented. Other reasons a borrower may exercise "yank-a-bank" provisions are when a lender has a loss of creditworthiness, has defaulted on its obligations to fund a borrowing or has demanded certain increased cost or tax payments. In such circumstances, the borrower may facilitate the sale of the lender's commitment to another lender or other eligible assignee. In most European loan agreements, yank-a-bank provisions are also routinely included and are similar in mechanism and trigger events. However, the threshold vote for "required lenders" is typically defined as at least 66.67% of lenders by commitment.

Snooze-You-Lose

In addition to provisions governing the required votes of lenders, most European loan agreements will also contain "snooze-you-lose" provisions, which favour the borrower when lenders fail to respond to a request for an amendment, consent or waiver. Where a lender does not respond within a specific time frame, such lender's commitment is ignored when calculating whether the requisite vote percentage have approved the requested modification. Similar provisions are rare in U.S. loan agreements.

Transfers and Assignments

In European loan agreements, lenders may assign their rights or otherwise transfer by novation their rights and obligations under the loan agreement to another lender. Typically, lenders will seek to rely on the transfer mechanism, utilising the standard forms of transfer certificates which are typically scheduled to the loan agreement. However, in some cases, an assignment may be necessary to avoid issues in some European jurisdictions which would be caused by a novation under the transfer mechanic (particularly in the context of a secured deal utilising an English-law security trust, which may not be recognised in some European jurisdictions).

Historically, most sub-investment grade European deals provided that lenders were free to assign or transfer their commitments to other existing lenders (or an affiliate of such a lender) without consulting the borrower, or free to assign or transfer their commitments to a pre-approved list of lenders (a white list), or not to a predetermined list of lenders (a blacklist). However, over the course of 2017, there has been a marked trend in transfer restrictions. Indeed, restrictions on transferring commitments to "competitors" of the borrower are now common in European loan agreements, usually without any reasonableness qualification. Another trend has been the increasing restrictions on transfers to loan-to-own and distressed investors, which in 2017 was seen in the majority of large-cap European loan agreements. For stronger borrowers in both Europe and the United States, the lenders must usually obtain the consent of the borrower prior to any transfer or assignment to a lender that is not an existing lender (or affiliate).

In the United States, the LSTA has recommended "deemed consent" of a borrower where a borrower does not object to proposed assignments within five business days, which is the same position taken in the European market. Similar to stronger European borrowers and sponsors who are able to negotiate a "blacklist", stronger borrowers in the United States, or borrowers with strong sponsors, often negotiate a "DQ List" of excluded (disqualified) assignees. In both the European and US contexts, the DQ List or blacklist helps the borrower avoid assignments to lenders with difficult reputations. In the U.S. market, exclusion of competitors and their affiliates is also negotiated in the DQ List. Large cap borrowers in the United States commonly push for expansive DQ lists and the ability to update the list post-closing (a development not seen in European loan agreements). The ability to update the DQ List post-closing could present problems in a workout scenario by giving the borrower veto power over any assignments or sales by lenders to third parties. On the other hand, deals frequently provide the borrower no consent rights over lender assignments following an event of default which can also be problematic if lenders desire to sell the loan to a "loan to own" fund.

Part D – New Regulatory and Legal Developments in the Loan Market

Leveraged lending guidance

U.S. federal bank regulators indicated during the third quarter of 2014 that they would more carefully scrutinise leveraged lending issuances following their determination that a third of leveraged loans they reviewed did not comply with the Leveraged Lending Guidance (the "US Guidance") issued in March 2013 by the Federal Reserve, the OCC and the FDIC. The US Guidance provides, among other things, that a leverage level in excess of 6x total debt over EBITDA will raise regulatory concern for most industries and may result in the loan being criticised (as discussed further in in Part B). In addition, the US Guidance provides that a borrower should be able to amortise its senior secured debt or repay half its total debt with five to seven years of base cash flows.

Regulators have identified some specific ways the US Guidance may affect credit agreement provisions or features. For example, regulators have said they will be critical of credit agreement terms that allow for the material dilution, sale, or exchange of collateral or cash flow-producing assets without lender approval. Sidecar loan agreements or accordion features that allow borrowers to incur more debt without protecting the existing lenders may attract regulatory scrutiny. EBITDA adjustments must be supported by third-party due diligence and a "large-percentage" adjustment will attract regulators' suspicion. Regulators have said that because refinancings or modifications count as originations to which the US Guidance applies, any refinancings or modifications of non-pass loans must show meaningful improvements to structure or controls to avoid being criticised. Such improvements might be new or tightened covenants, additional collateral or restrictions on acquisitions.

Supplementary regulatory commentary provides that failure to adhere to these requirements is not a bright line bar to an issuance if there are other mitigating factors. The lack of a bright line rule may permit some loan issuances that do not achieve complete compliance, but it also introduces significant uncertainty into the process of underwriting a loan issuance for sponsors, borrowers and lenders alike. Experts predicted that the US Guidance could result in more borrowers electing to use non-regulated institutions as agents and lenders, and, as predicted, since 2015, non-regulated financing sources have been more active with respect to loans that might have been criticised. This trend is not without problems. Sponsors are wary of trusting the execution of large deals to non-regulated financing sources, and borrowers are hesitant to rely on revolving commitments from them. Also, overreliance on non-regulated financing sources could create a liquidity problems in a few years when borrowers seek to refinance (regulators have indicated that the US Guidance may be applied to a refinancing). Regulators are considering regulations to address the non-regulated financing sources loophole.

The federal regulators noted in a 2016 review that the banks have made progress in compliance with the US Guidance as the number of non-pass loan originations in the U.S. market reached *de minimis* levels. But the regulators cautioned that some weaknesses in underwriting practices still exist, including liberal repayment terms, structures with "ineffective or no covenants", incremental debt provisions that allow for debt to a level that inhibits deleveraging capacity and dilutes senior secured creditors and unreasonable addbacks to EBITDA. Further part of the decrease in non-pass originations is attributable to the liberal use of addbacks that increase EBITDA substantially, thereby decreasing the leverage ratio below 6×. For example, when the Ultimate Fighting Championship put itself up for sale recently, add-backs to its EBITDA increased its earnings from $170,000,000 in the initial calculation to $300,000,000 in the presentation given to debt investors (which decreased its leverage ratio to 6×). This large increase in EBITDA would permit substantially more debt to be incurred in connection with the sale. Regulators caught on and cautioned Goldman Sachs, the arranger. When Bain Capital decided to buy online jeweller Blue Nile, addbacks increased Blue Nile's EBITDA from approximately $19,000,000 to approximately $45,000,000, dropping its leverage ratio from 9× to 4×. The concern of regulators is that, regardless of the decrease in non-pass originations, this type of creative accounting does not represent true progress toward tighter underwriting practices.

Similar leveraged lending regulation is likely to be introduced in Europe shortly. On 23 November 2016, the ECB published (for consultation purposes) an initial draft guidance to banks regarding leveraged transactions, which is intended to apply to all "significant credit institutions" supervised by the ECB under the Single Supervisory Mechanism (the "ECB Guidance"). The ECB Guidance will not apply to "credit institutions" based in member states outside the Single Supervisory Mechanism and not directly supervised by the ECB (such as the United Kingdom, although the Bank of England has itself from time to time considered leveraged lending levels). Although the ECB Guidance will not be legally binding, affected institutions are expected to incorporate the ECB Guidance as part of their internal lending policies, which will undoubtedly affect credit and lending decisions once the ECB Guidelines are finalised and implemented.

For the purposes of the ECB Guidance, a "leveraged" transaction will include all types of loans or credit exposures where the borrower's post-financing level of leverage (i.e. the ratio of total debt to EBITDA) exceeds 4.0× as well as all types of loan or credit exposures where the borrower is owned by one or more financial sponsors. Under the ECB Guidance, affected credit institutions are expected to ensure that transactions which have a "high level" of leverage – meaning transactions where the ratio of total debt to EBITDA exceeds 6.0× at the time of deal inception, remain "exceptional" (in similar vein to the US Guidance). As mentioned above, the ECB Guidance proposes to test leveraged transactions by reference to "unadjusted" EBITDA, unlike the US Guidance which acknowledges adjustments to EBITDA. At the time of writing, the ECB Guidance was still in the consultation phase and far from being finalised, and so whilst it will be certainly significant from a compliance and risk perspective, the real impact on deal levels and loan terms cannot be meaningfully determined at this stage.

Conclusion

As highlighted in this chapter, it is important for practitioners and loan market participants to be aware of the key differences in the commercial terms and market practice in European and U.S. leveraged loan transactions. While there are many broad similarities between the jurisdictions, borrowers and lenders that enter into either market for the first time may be surprised by the differences, some of which may appear very subtle but which are of significance. As more and more borrowers are prepared to look beyond their domestic market and willing to seek access to whichever debt market (whether U.S. or European) offers greater liquidity and more favourable pricing and terms at any given time, and as a wider range of alternative and non-bank investors are attracted to the investment opportunities presented by both the European and U.S. loan markets, the importance of having a general understanding of the differences is now even more critical.

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The Global Subscription Credit Facility and Fund Finance Markets – Key Trends and Forecasts

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Introduction

The Subscription Credit Facility (each, a "Facility") and related Fund Finance markets had a fascinating 2017. On the one hand, everything stayed exactly the same. Like virtually every year since the financial crisis, Facility credit performance remained pristine, with no monetary defaults having become public last year. And the out-paced growth rate continued. But, on the other hand, outside of the four corners of the transactions, change seemed to come daily. This chapter summarizes the key trends in the Facility and Fund Finance markets in 2017 and forecasts developments for the coming year.

Credit Performance

To our knowledge, there were again no payment events of default in the Facility or related Fund Finance markets in 2017. Virtually all of our transactions, both Facilities and on the NAV-side, performed from a credit perspective last year. We are for the first time in current memory aware of several funding defaults by limited partners ("Investors") on their capital calls ("Capital Calls"), but these defaults seemed to be isolated to Chinese Investors grappling with local law monetary policy preventing cash outflows. As we understand it, none of these Investor defaults led to Facility problems.

Resilient Growth

2017 was another very healthy year for private equity fundraising and, correspondingly, the Facility markets. According to Preqin research, private capital raised in 2017 exceeded $750 billion and private equity dry powder climbed to $1 trillion. Many of the major lending institutions in the market (each, a "Lender") again reported portfolio growth in excess of 20% last year, exceeding our forecasts. While there are certain Lenders that have reached their institutional lending limits for particular Fund sponsors (each, a "Sponsor") and for the Facility product, the market continued its expansion. Many lenders increased their Facility program limits and new entrants continued efforts to gain traction.

Structural Evolution

Last year remained very muted in terms of structural evolution in the Facility market. Frankly, very little changed. From a Lender's viewpoint, private equity fund (each, a "Fund") limited partnership agreements ("Partnership Agreements") continued to improve, likely driven by the increasing concentration of Fund formation occurring at a fewer number of highly experienced law firms. Transaction terms moved slightly in favor of the borrowers; not a surprising development at this point in the cycle. Facility borrowing bases ("Borrowing Bases") largely held to the traditional Included Investor/Designated Investor structure (particularly in the United States). Advance Rates moved slightly higher and concentration limits were relaxed moderately. But these changes were really at the fringe; Facility structures remain quite consistent with where they have been in recent years. Spreads changed very little in 2017.

Industry Developments and Press Coverage

A. ILPA Guidelines. In June 2017, the Institutional Limited Partners Association ("ILPA") published a guidance paper to their constituents on Facilities (the "Guidelines"). The Guidelines dominated market discussion the remainder of the year, and have been the subject of multiple seminars, conference panels and articles. At the suggestion of market participants, the Fund Finance Association (the "FFA") published an analysis and set of recommendations on the Guidelines in the Fall (the "FFA Response"). The FFA Response sought clarification on several items in the Guidelines and made suggestions to the Guidelines to ensure they protected Investor interests without unintentionally prescribing key aspects of the utility of a Facility.[1] In January 2018, ILPA invited the FFA board of directors to join a call to discuss the Guidelines and the FFA Response with ILPA personnel and several large institutional Investors. The call was productive and both sides received a good explanation of the other's perspective. ILPA indicated that they do not forecast publishing an updated version of the Guidelines in the immediate future, but may publish some interpretive guidance.

B. Press Coverage. The steady stream of coverage of Facilities in both the private equity and mainstream press continued throughout 2017. Even accounting and consulting firm PwC published a "thought leadership" piece on Facilities.[2] The Facility market has seemed to have gotten accustomed to this; these articles cause far fewer fire drills than they did originally. The market does not appear impacted by the published inaccuracies.

C. Bank Hiring. For many years, growth in the Facility market substantially exceeded Lender hiring, leading to growing workloads. That finally shifted in 2017. Many Lenders in the Facility market invested substantially in staffing in 2017, hiring at both senior and junior levels. Several prominent bankers switched firms and many Lenders are advertising open positions. We expect to see additional transitions in 2018. Many bankers also received promotions in 2017 putting upward pressure on compensation.

D. Publications. Global Legal Group Ltd., the publisher of this Legal Guide, published the second edition of *Global Legal*

Insights – Fund Finance 2018, a comprehensive legal guide on the Fund Finance markets. The guide includes 18 product-oriented chapters and 20 jurisdictional updates contributed by many of the world's preeminent Fund Finance law firms, a substantial improvement over the inaugural edition.[3]

2018 Market Forecast

From a Facility structural perspective, we expect evolution to continue to be limited to the margins in 2018. Credit performance of Facilities during the financial crisis validated current structures and Lenders have expended significant institutional resources the past several years developing their Facility product programs and policies. Borrowers are familiar with current structures and they seem to be working well. We believe any structural changes will be incremental.

While we do expect the rate of Facility growth to slow in 2018 as compared to the 20%+ of the past few years, we forecast 2018 growth in Lender portfolios in the 8%–12% range year-over-year. The historical factors supporting expansion remain sufficiently pronounced. But there are market realities that will push against historical growth rates. Lenders are going to be more focused on their internal policies, form documentation, hiring and staffing, and credit and risk analysis in 2018 as they try to absorb the growth of the past few years. And benchmark interest rates are widely forecasted to increase in 2018, creeping up as a percentage of preferred returns. We also think that the ILPA Guidelines may result in side letter provisions that conflict with certain Lender credit parameters, potentially slowing certain transactions.

Upcoming Events

On March 21, 2018, the FFA is hosting the 8th Annual Global Fund Finance Symposium at the Grand Hyatt in New York, New York. And, on June 13, 2018, the FFA is hosting the 2nd annual Asia-Pacific Fund Finance Symposium at the Four Seasons Hotel in Hong Kong. The 4th Annual European Fund Finance Symposium is scheduled for October 24, 2018, to be held at the Landmark Hotel in London.[4] Look out for an exciting announcement from the FFA as to its 2019 slate of events.

Conclusion

The Facility market appears poised for another solid year in terms of portfolio growth in 2018. While Facility structures have been trending ever so modestly in favor of Fund borrowers, we continue to believe that the credit profile of market-structured Facility transactions forecasts well for Facility performance in the coming year.

Endnotes

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3. An electronic copy of *Global Legal Insights – Fund Finance 2018* can be accessed at https://www.globallegalinsights.com/practice-areas/fund-finance-laws-and-regulations.
4. Information on these events is available at the FFA's website, http://www.fundfinanceassociation.com/.

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Recent Developments in U.S. Term Loan B

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Introduction

2017 was a record breaking year for the U.S. leveraged loan market, reaching levels of activity not seen since 2007. Opportunistic repricings and refinancings once again led the way at the start of the year and remained strong throughout but, happily for loan investors, M&A and other event driven new-money financings fought back to reclaim center stage in the latter stages of 2017.

Leveraged loan volume in the U.S. during 2017 increased by a remarkable 60% compared with 2016 levels, with a huge $1.4 trillion of issuance, up from $875 million in 2016. 'Yankee' loans issued by European borrowers in the U.S. market also had a record year, with over $70 billion raised, smashing previous volume records set in 2014 and more than five times the volume of 'reverse-Yankee' loans issued by U.S. borrowers in the European market in 2017.

Against this background, it is no surprise that loan documentation in the U.S. market continued its trend towards ever-more friendly waters for Term Loan B (***TLB***) borrowers, which has been a consistent theme for the last few years. This article examines some of those developments.

Market Fundamentals

Attitudes

Investment banks in today's TLB market operate an originate-to-distribute model, arranging the financing package before distributing all or a significant portion of TLBs to investors (although they will usually retain a portion of the revolving or other liquidity facility, which is still the domain of traditional banks). The ultimate TLB holders are more likely to be non-bank lenders, i.e. institutional investors such as hedge funds and issuers of collateralized loan obligations (***CLO***s).

Institutional investors take a different approach to their participation in a loan syndicate when compared to traditional banks, viewing loans as liquid, tradable and impersonal investments, rather than part of a broader banking relationship with that borrower. Individual investors buy and sell loans opportunistically instead of holding them to maturity, meaning that they are less reliant on the protection that a more traditional term loan covenant package affords. An institutional investor's overall portfolio will include high-yield bonds as well as loans and, accordingly, they have gotten comfortable with high-yield incurrence-based covenants for both bonds and leveraged loans in their portfolio. Sponsors and borrowers have been able to use this shift in composition of the lender base, as well as the strong demand for the TLB product, to their advantage in order to push for greater flexibility in terms, in the knowledge that investors will continue to tolerate weaker covenant packages and 'cov-lite' structures as long as the debt is sufficiently liquid. The increase in secondary market activity, absence of a close relationship between a borrower and its lenders and increasing syndicate sizes mean that covenant flexibility becomes even more important for a borrower, as larger and more impersonal syndicates mean that amendments to loan documentation can no longer be quickly, easily or cheaply obtained.

Legal and regulatory developments

The impact of the Leveraged Lending Guidance (***LLG***) jointly issued in 2013 by the Board of Governors of the Federal Reserve System, the Office of the Comptroller of the Currency and the Federal Deposit Insurance Corporation (collectively, the ***Agencies***) has been widely reported and LLG continued to have an influence on the market in 2017, although less than years prior for reasons discussed below. Under LLG, banks are required to report all leveraged loans to the Agencies for *post-hoc* review, and the Agencies have the power to find that banks under their supervision are engaged in unsafe and unsound banking practices. LLG states that the Agencies will apply additional scrutiny to transactions where leverage levels exceed 6.0x and/or the borrower is not able to repay all senior debt or half of total debt within five to seven years.

While the Agencies have remained focused on the second of these tests, LLG is notably having less of an impact in terms of reducing overall leverage for corporate borrowings. In 2017, leverage multiples above 6.0x on financings supporting LBO activity in the U.S. were at their highest proportions since 2007. There are various reasons for this: sponsors and arrangers have relied on more adjustments and add-backs when determining the "adjusted EBITDA" number presented to TLB investors while, at the same time, unregulated non-bank and direct lenders have demonstrated a willingness to finance highly leveraged deals and increased their market share in terms of volume in 2017. The rise in leverage multiples also indicates that the market expected a more relaxed approach to enforcement by the Agencies under the current U.S. presidential administration. Doubts raised by Senator Pat Toomey in October 2017 concerning the validity of LLG and whether they constituted a 'Rule' for the purposes of the Congressional Review Act (therefore requiring Congressional approval) showed that LLG did not have the political support it once did. Most recently, in February 2018, the Ooffice of the Comptroller of the Currency stated publicly that it would not challenge bank activities that violate the guidelines provided that a bank's "safety and soundness" is not impaired.

The other significant legal development was, of course, the passage of the Tax Cuts and Jobs Act, bringing about the most extensive changes to corporate taxation in the U.S. in a generation. The legislation will affect both financing markets and M&A activity in a number of ways. Key changes include the reduction in the corporate tax rate from 35% to 21% and the caps imposed on deductions for net business interest expense at 30% of adjusted taxable income or ATI, calculated to approximate EBITDA initially, and then EBIT from 2022 onwards. In addition, deductions for interest paid to foreign related parties are subject to further limitations (under a "base erosion anti-avoidance tax" or "BEAT"), affecting "push downs" of debt to US affiliates of non-US borrowers. Given that interest deductibility in respect of acquisition financing is a prominent tool employed by sponsors to maximise their returns on highly leveraged buy-outs, it remains to be seen whether these tax reforms will succeed where LLG has so far failed in limiting the overall leverage multiples for corporate borrowings in the U.S. while providing some incentive to shift debt to a group's foreign subsidiaries. The act retained the "deemed dividend" provisions of Section 956, which historically have been the basis of excluding non-US subsidiaries from the guarantee and collateral requirement in credit agreements, while also introducing new provisions that change the tax code from a worldwide to a "territorial" regime in order to incentivize US-parented companies to repatriate earnings. Given, however, that pre-2018 earnings of non-US subsidiaries have already effectively been deemed distributed (under a "transition tax") and given that certain post-2017 foreign earnings can be distributed free of tax (either through a "participation exemption" or because the earnings are previously taxed under either Subpart F or as "global intangible low taxed income"), with proper planning it may be possible to implement pledges and guarantees that would not previously have been possible without adverse effects under Section 956. Thus, while the tax changes are still being digested by the market, they could lead to changes in certain credit agreement provisions, particularly around guarantor coverage, restricted payments and excess cash flow provisions.

Economic Terms

Pricing

Borrowers squeezed loan margins even further in 2017 with a continued cycle of repricings. In 2016, we began to see signs of erosion of the LIBOR 'floor', which has typically been set at 1%, to prop up low margins in an era of historically low interest rates. With three separate borrowing rate hikes in 2017 and forecasters predicting three more in 2018, LIBOR now stands well above the typical floor rate so leveraged loans have become true floating rate instruments once again, just as they were before the financial crisis. While a 1% LIBOR floor remained typical in 2017, we saw an increasing trend towards lower LIBOR floors and increasingly at 0.0% or with no floor at all, which had previously been more a feature of the European market.

Optional prepayments

Unlike bonds, investors still generally accept that a TLB is prepayable without penalty or premium. With the increase to the depth and liquidity of the TLB investor base in 2017, borrowers took advantage of high demand in the market to reprice (either by way of an amendment to a loan agreement or a refinancing of outstanding loans) and looked to do so even fairly quickly after initial issuance. As a result, investors continue to demand that some limited pricing protection be included in TLB facilities from the outset. The typical protection is a 1% prepayment premium for refinancings at a lower interest rate within an agreed period of time (known as 'soft call' protection). In 2017, the majority of soft call protection provisions included a 'sunset' of six months, while a minority lasted for a full year after initial issuance. While soft call protection as a concept remained, borrowers in 2017's hot market continued to press for broader exceptions to the requirement to pay a prepayment premium, including when prepayments are made in connection with another transaction, such as a material acquisition, a change of control or an IPO. The broadest formulation of such a carve-out permits a prepayment without a premium where the repricing of the loan is not the 'primary purpose' of the transaction, which featured in the majority of leveraged loans in 2017.

Mandatory prepayments

Mandatory prepayment requirements became less onerous in 2017, continuing the trend in TLB that lenders have pulled back from requiring borrowers to de-lever with excess cash. Many loan agreements no longer require prepayments from issuance of new equity proceeds. Excess cash flow (***ECF***) sweeps were absent from some sponsored deals and, where they were included, were often undermined by borrower-friendly deductions and carve-outs to the definition of ECF, as well as minimum thresholds for ECF before a prepayment is required.

For asset dispositions, where TLB lenders once required 100% of the proceeds from asset dispositions to be applied to pay down debt (with a short reinvestment period), TLB borrowers in 2017 typically may reinvest proceeds during a period of up to 18 months or longer – and the criteria for qualified reinvestments continue to expand to the point that nearly anything the borrower believes to be used or useful to its business is permitted. Moreover, TLB borrowers typically may utilise the asset sale proceeds to pay down debt from other secured lenders on a *pro rata* basis together with the TLB and, if certain leverage thresholds are met, the percentage of asset sale proceeds which is required to be used to pay down the TLB may step down (a concept borrowed from the ECF sweep provision). Even where a TLB requires the borrower to pay down debt with a percentage of proceeds from an asset sale, some borrowers have obtained changes to the asset sale covenant that permit asset sales to be made without a minimum amount of cash consideration, another way in which TLB lenders receive fewer prepayments.

Restrictive Covenants

Although TLB terms continued to loosen in 2017, the format and structure of the covenants in TLB, for the most part, remained consistent. TLB facilities have until now generally resisted incorporating the form of high-yield covenants wholesale, although this approach has been seen in some circumstances, usually where the TLB sits alongside high-yield bonds in the capital structure. While the use of high-yield covenants in a TLB is still very much an outlier, the substance of TLB covenants continued to become more akin to high-yield bond incurrence covenants, where many corporate actions are permitted subject to the meeting of certain ratios on the date of such action. For example, most TLB facilities keep payments to shareholders (also known as 'restricted payments'), investments and prepayments of subordinated debt as separate covenants but have builder baskets and general baskets that net across the three covenants. This bond-like flexibility allows borrowers more and more to enter into strategic transactions and incur or refinance debt without seeking the consent of their lender syndicate and without incurring the associated consent fees otherwise required to be paid.

As in high-yield bond indentures, TLB facilities also now typically include the concept of restricted and unrestricted subsidiaries, where the borrower may designate certain subsidiaries as unrestricted subsidiaries. Unrestricted subsidiaries are not subject to guarantee and security requirements, compliance with covenants and events of default, but their EBITDA and earnings (and debt) are excluded from the calculation of financial definitions and ratios. These provisions were thrown into the spotlight in 2017 after J. Crew took advantage of this flexibility in their credit agreement covenants to transfer approximately $250 million worth of intellectual property to an unrestricted subsidiary with the aim of borrowing against the transferred assets and using the proceeds to repay subordinated debt of its parent. Shutting off these ‘trapdoor' provisions were a focus for investors in 2017 and a rare example of terms actually being tightened in syndication.

Financial covenants

The prevailing trend over the last few years toward ‘cov-lite' TLB continued in 2017, with no maintenance covenant protection available to the transaction's term lenders. It should come as no surprise that the vast majority of large cap TLB deals in 2017 were ‘cov-lite', but perhaps more noteworthy was that around three-quarters of sponsored leveraged loans in the mid-market were also ‘cov-lite'.

Even if a traditional maintenance covenant is not included for the benefit of TLB lenders, a facility may include a ‘springing' maintenance covenant. Springing covenants are typically tested only when the relevant revolving lending facility is drawn above a certain threshold and are solely for the benefit of the revolving lenders. For large and mid-market sponsor deals, if a springing maintenance covenant was included, the vast majority ‘sprung' the maintenance covenant when the revolver was drawn by more than 35% of revolving commitments.

Debt incurrence

TLB facilities continue to allow broad flexibility to incur additional debt, whether on a first-lien, junior-lien or unsecured basis, inside or outside the credit facility and/or in the form of loans or bonds. TLB facilities typically still include more stringent parameters around the terms of secured debt than unsecured debt, including tighter limitations on the borrowing entity, final maturity, weighted average life, prepayments and, sometimes, more restrictive terms (for example, requiring a ‘most favored nations' (***MFN***) provision in the case of the inclusion of a financial covenant in any *pari passu* term debt).

Broadly, there is a distinction between refinancing or replacement loans, which may be incurred within certain parameters (relating to maturity, identity of the borrower and guarantors, etc.) and additional debt (including incremental facilities), which are subject to similar parameters but also to *pro forma* compliance with a financial ratio.

Additional debt (including incremental facilities)

TLB facilities in 2017 continued the ever-widening variety of approaches to providing borrowers flexibility to incur additional debt, and most loan documents will contain more than one overlapping means by which a borrower may incur additional debt. Permitted additional debt baskets can be grouped into those that will be governed by the borrower's original credit agreement and those governed by separate documentation.

Incremental Facilities. Additional debt incurred under a particular credit agreement is typically referred to as an incremental facility. For years, TLB credit agreements have included a right to add one or more new tranches of TLB (or increase the size of an existing tranche) on a *pari passu* basis within the framework of the original credit agreement. This ability is usually subject to both (i) a restriction on the aggregate amount of new debt that can be issued, and (ii) the protection of an MFN provision that ensures any newly incurred debt will be issued with an all-in-yield of no more than a threshold amount (traditionally 50 bps, although increasingly borrowers are looking for 75 or 100 bps of headroom) in excess of the all-in-yield on the original TLB facility. The MFN provision will require the margin of the original debt to be adjusted to ensure the variance is no greater than the threshold, and as a result, MFN provisions provide further economic disincentive for a borrower considering incurring debt under an incremental facility at a higher price. For this reason, borrowers typically push for an MFN provision to expire (or ‘sunset') after a certain period has passed since the initial closing.

MFN Sunset Provisions. The details of MFN provisions were again heavily negotiated in 2017. In underwritten financings, MFN sunsets remained a focus of flex provisions, even if they were seldom exercised by the arrangers given the favorable market conditions, resulting in an increase in deals with a sunset provision in 2017. The incidence of sunsets increased and the duration has varied from anywhere between six and 24 months, with the most commonly agreed period being 12 months.

Exceptions to MFN for Incremental Facilities. Some more recent TLB facilities also incorporate new and varied exceptions, under which the borrower may incur additional debt that is not subject to the MFN provision. These exceptions include MFN provisions which are not triggered by additional debt that has a maturity date later than the maturity date of the original term loan by an agreed period (typically more than two years). Other deals include a new basket for additional debt that is not subject to the MFN, either for the ‘freebie' basket of additional debt discussed below or another agreed fixed amount and separate exceptions from the MFN where the incremental debt is being raised to finance an acquisition or other permitted investment. Finally, with an increasing number of cross-border facilities, it is becoming more common for TLB facilities to specify that the MFN will apply only to the original term loans incurred in the same currency as the new incremental facility.

Amount of Incremental Debt. The total amount of incremental debt that TLB borrowers were permitted to incur has also evolved. Size was typically determined by one or more of the following three components: (1) a ‘freebie' amount that may be incurred irrespective of *pro forma* compliance with a financial ratio; (2) a ratio amount limited only by such *pro forma* compliance; and (3) an add-on amount equal to voluntary prepayments of the existing debt. While ‘freebie' baskets typically are a fixed dollar amount, over half of ‘freebie' baskets in large and mid-market sponsor TLB loan agreements included a ‘grower' concept that set the size of the ‘freebie' basket at the greater of a fixed amount and a percentage of EBITDA, providing greater flexibility to the borrower to incur debt without the limitations of *pro forma* compliance. The ratio used to determine *pro forma* compliance is a point of negotiation as well. A first lien leverage ratio (often set at first lien leverage on the closing date) is the most common, but overall secured leverage is common as well and a small number of TLB will determine the size of the ratio amount by reference to total leverage.

Incremental Equivalent Debt. In recent years, TLB facilities have also included a right to incur additional debt within the same parameters negotiated for incremental facilities under documents other than the original credit agreement that meet certain pre-agreed criteria – called ‘incremental equivalent debt’ or a ‘side-car facility’ – on the theory that the economic effect is the same as an incremental facility. Lenders typically permitted borrowers to incur incremental equivalent debt under bond offerings, but some TLB include a right to incur side-car facilities in the form of term loans. These typically do not trigger MFN protections for the incurrence, although there has been some push by investors for the MFN to apply to side-car facilities that are incurred in the form of *pari passu* secured term loans.

Reclassification. Other debt that TLB credit agreements permit a borrower to incur includes capital expenditure-related debt, acquisition-related debt and permitted ratio debt, among others, with basket sizes typically comprised of an initial ‘seeded’ amount plus an amount that can be incurred subject to a *pro forma* ratio compliance test. An increasing number of TLB facilities now allow the borrower to reclassify debt that was initially incurred under the initial ‘seeded’ amount as debt incurred under the ratio amount when capacity becomes available under the ratio (a concept borrowed from high-yield bonds). These ‘reclassification’ provisions have been incorporated into the additional debt baskets as well as the incremental facility amount. In practice, reclassification permits a borrower to refresh the initial ‘seeded’ amount it can borrow without complying with the ratio tests whenever capacity under the ratio amount or another additional debt basket later becomes available. Such provisions will also now typically provide that additional debt is deemed to be incurred first under any ratio capacity before the ‘seeded’/‘freebie’ basket in order to preserve the amount that may be borrowed without being subject to the ratio cap.

Acquisition Debt. To facilitate using incremental facilities to finance acquisitions, it is now common to allow the testing of the conditions to incurring an incremental acquisition facility (including projected compliance with any ratios and whether a default or event of default has occurred, other than a payment or insolvency default) to be tested only at the time of signing the related acquisition agreement, in order to provide the borrower (and an acquisition counterparty) with more certainty around the availability of their financing to close the acquisition. TLB facilities have not settled, however, on whether a borrower must calculate and comply with ratio thresholds while the acquisition is pending by reference to financials assuming the acquisition has not occurred, by reference to *pro forma* figures that assume closing of the acquisition or both. We expect further market developments on this point during the course of 2018.

Replacement debt

As it became increasingly difficult during the Great Recession to replace debt under a new loan agreement, TLB borrowers and lenders created alternative ways to restructure loans within the framework of an existing credit agreement. Typical TLB facilities provide the flexibility to borrowers to incur debt pursuant to provisions that permit refinancings, repricings, rights to ‘amend and extend’ outstanding loans and rights to add tranches of debt, in each case, typically subject only to the consent of the lenders participating in such debt and the agent. Each form of replacement debt is accompanied by a list of requirements regarding the form that the replacement debt may take, generally limiting the final maturity, weighted average life, and otherwise requiring that the replacement debt be on terms no more favorable to the new lenders than the old debt being refinanced.

Typically, the principal amount of replacement debt that may be incurred is limited to the actual outstanding principal amount of the debt being refinanced plus fees and expenses for the transaction. While undrawn commitments are not typically considered debt ‘incurred’ for purposes of the additional debt restrictions until they are drawn, some recent TLB facilities now include undrawn commitments under a facility in calculating the maximum principal amount of permitted refinancing debt which can be refinanced. Since permitted refinancing debt is not subject to the *pro forma* compliance ratios that apply to additional debt, including undrawn commitments in the maximum amount of permitted refinancing debt effectively permits a borrower to incur additional debt it would otherwise have been unable to draw without complying with the *pro forma* ratio.

Other covenants and covenant exceptions

Permitted acquisitions, investments, restricted payments and junior debt prepayments

The conditions to making acquisitions, investments, restricted payments, junior debt prepayments and similarly restricted transactions continue to loosen. One typical condition to such transactions has traditionally been an absence of either (i) a continuing event of default, or, more restrictively, (ii) any event which after the giving of notice or passage of time would give rise to an event of default if not cured (i.e., a ‘Default’). It is becoming more common for conditions to be limited to events of default only (so a restricted transaction may be permitted while a Default is continuing) and in some cases such transactions are permitted even while an event of default has occurred or is continuing so long as the event of default does not arise as a result of a non-payment or an insolvency proceeding. Conditions for permitted acquisitions and investments may also be tested upon signing of an acquisition agreement, mirroring the flexibility provided for incurring acquisition debt.

For acquisitions, borrowers are increasingly permitted to acquire entities that are not required to accede as guarantors. Similarly, it is not unusual, particularly where a borrower has significant non-U.S. operations or a non-U.S. growth strategy, for investments in subsidiaries that are non-guarantors (which most often are non-U.S. entities) to be uncapped. The borrower generally remains subject to the overriding requirement that material subsidiaries contributing an agreed percentage of the group’s EBITDA (typically somewhere between 80 and 90%) must become guarantors and grant security. This will often not require controlled foreign corporations (or in some cases, all foreign subsidiaries) to become guarantors. EBITDA calculations to determine the guarantor threshold may also have specific exclusions that further reduce the number of subsidiaries that must become guarantors.

Ratio-based permissions and available amount baskets

There is no dominant approach as to which financial ratio should govern ratio-based covenant exceptions, including those for debt incurrence – first lien leverage; total secured leverage; total leverage; and a fixed charge coverage ratio are all used. For incurrence of *pari passu* debt, for example, first lien leverage remains the most common formulation, accounting for nearly two-thirds of large syndicated TLB facilities in 2017, but the total secured leverage ratio accounts for nearly a quarter. A number of TLB facilities now permit the incurrence of an unlimited amount of unsecured debt subject to satisfaction of a minimum fixed charge cover ratio (in many cases set at 2x) instead of a maximum total leverage ratio, aligning the standard to incur unsecured debt with that commonly found in high-yield bonds. Similarly, restricted payments may be permitted in unlimited amounts subject to satisfaction of a leverage ratio, which may be total leverage, total secured leverage or first lien leverage.

Borrowers are also now often permitted to reclassify prior transactions among dollar baskets so that they are deemed to have been permitted under another exception within a particular covenant (such as the restricted payment covenant or the investments covenants) in the same manner as discussed above with respect to debt baskets. Some TLB facilities will also permit reclassification across certain covenants, such as, for example, reclassifying a fixed dollar basket for restricted payments to be used to make a junior debt prepayment. TLB facilities rarely specify that a borrower must give notice or justify a reclassification (as reclassification is a borrowed concept from high-yield bonds, which do not require notice or explanation of reclassification).

As with the ‘freebie’ basket for incremental facilities, it is also typical for TLB loan agreements to provide flexibility to borrowers to undertake acquisitions, investments, restricted payments, junior debt prepayments and similarly restricted transactions that would otherwise require *pro forma* ratio compliance up to a total maximum amount. This maximum amount, called the ‘Available Amount’ or the ‘builder basket’, has traditionally been pegged to earnings which were not swept as ECF with the result that the basket’s size built up over time. Now, instead of retained earnings, nearly half of large TLB facilities peg the size of the ‘Available Amount’ to a percentage of consolidated net income (usually 50%), which permits the borrower to build the basket faster. In addition, the ‘Available Amount’ now typically includes a fixed ‘seeded’ amount that is available immediately, and an increasing number of large TLB provide that the seeded amount is the greater of a fixed dollar amount and a ‘grower’ amount equal to a percentage of borrower’s EBITDA (or sometimes total assets). Seeded amounts permit borrowers to do investments, restricted payments and other transactions from day one. Grower baskets like those that are now being used for seeded amounts remain a generally accepted TLB concept for many covenant baskets, including restricted payment baskets and often the size of these baskets is generally pegged to a percentage of EBITDA, although in non-sponsored and middle market deals it may be pegged to a percentage of total assets.

Financial definitions

Despite scrutiny by the Agencies on permitted debt incurrence, the ways in which borrowers can calculate the ratios that permit additional debt incurrence have been more heavily negotiated than ever.

On the cash flow side, EBITDA definitions historically permitted borrowers to add back to EBITDA prospective cost savings from synergies arising from reorganizations and acquisitions, but such savings historically needed to be expected to be realised within a period of time (traditionally 12 months) and the amount of the add-back was capped to a percentage of total EBITDA. More recently, however, borrowers have pushed for more flexibility in several ways. First, more recent definitions expand the scope of what qualifies as a reorganization transaction. Some TLB facilities now even permit add backs for expected synergies arising from any ‘cost savings initiative’ (i.e., not in connection with a specific acquisition or in connection with an overall reorganization plan) and leave it to borrowers to determine what initiatives qualify. Second, the period of time within which cost savings must be expected to be realised has increased. While 12 months used to be typical, 18 and 24 months are now the new standard and in some cases the period can stretch out to 36 or 48 months or even without any time limit at all. Some TLB facilities no longer require the cost savings to be expected to be realised within the agreed period but rather require only that the reorganisation or acquisition that will give rise to the expected cost savings be completed (or in some cases, committed to) within the agreed period. Finally, the cap on the amount of EBITDA add-backs has either increased (most commonly to 25% but sometimes higher) or been removed. Nearly half of large syndicated TLB facilities in 2017 permitted such add-backs without a cap, although add-backs without a cap were rarer in smaller TLB facilities, they appeared in around 30% of mid-market deals. Where a cap is present, it will still generally apply to all add-backs over a four-quarter period as opposed to per individual transactions, which is a formulation sometimes seen in European deals.

On the debt side of the ratio, TLB facilities have for some time permitted borrowers to calculate debt net of unrestricted cash held by the borrower and its subsidiaries. Cash netting was traditionally capped to a maximum dollar amount, but the number of TLB facilities that permit cash netting without any cap has increased over time and is now present in the majority of TLB facilities.

Assignments and Amendments

Some constraints on assignments of TLB remain customary. In general, a borrower’s consent to assignments (not to be unreasonably withheld) is required. However, the consent requirement falls away while certain events of default (typically limited to non-payment and insolvency) are continuing. Generally, consent will also be deemed to be given if the borrower fails to respond within a specified period. The length of such period continues to be a point of negotiation, with borrowers pushing for periods longer than the LSTA-recommended position of five business days.

Assignments to disqualified institutions (i.e. competitors and other identified institutions) are also typically prohibited. A list of disqualified institutions is typically frozen at the start of primary syndication (other than as to competitors, which can be updated over the life of the TLB). Many TLB facilities now state that the list will be provided to individual lenders upon request instead of posted generally, making it more difficult for a lender to market a loan generally to secondary purchasers who do not know whether a trade will ultimately be permitted and settle. One increasing trend in recent years has been loan investors buying debt with the intention of profiting if the loan fails to perform, either through a loan-to-own strategy or through large credit default swaps that will pay off if the borrower defaults. In response to this, 2017 saw an increasing number of borrowers looking to restrict transfers to such loan-to-own or net short investors as a general overriding rule and without naming specific institutions on the list of disqualified institutions (given the rapid emergence of new players in this space).

Finally, assignments to the borrower and its affiliates are generally permitted, although the total amount of loans that may be held by any other affiliate lenders is generally capped to an agreed percentage, typically falling around 20 to 25%, and *bona fide* debt funds of affiliates are often excluded from this cap.

The thresholds for amendments have historically been set at a simple majority of lenders. Fundamental rights (including economic rights and release of substantially all guarantees and security) require the consent of all lenders. These thresholds now typically permit partial refinancings of TLB and incurrence of additional debt with consent only from ‘each affected lender’ so that lenders who do not agree to participate in the change do not have any blocking right. In practice, some amendments (e.g. the release of all or substantially all guarantees and/or collateral) will still require unanimous consent. Agents are typically permitted, however, to agree to consequential amendments (such as those to security documentation) that implement permitted additional or replacement debt without any further lender consent.

Conclusion

Despite such a record year for the U.S. leverage finance market, it remains to be seen how long the current cycle can last. Will TLB covenant packages continue to erode in favor of increasing bond-like flexibility and away from the traditional model requiring delevering and consistent engagement with lenders? It is difficult to see any other outcome if market conditions remain as they were throughout most of 2017, with demand consistently far outstripping supply.

On the horizon, borrowing rates are expected to increase again throughout 2018 and, although all signs point to less regulatory pressure under the current presidential administration, market participants will be watching carefully to assess the impact of the Tax Cuts and Jobs Act on the U.S. leveraged finance market.

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The Growth of European Covenant Lite


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In 2016, global sponsors and their advisers were successful in continuing to export their experiences from financing transactions in the US leveraged loan and global bond markets to the European leveraged loan market and this continued apace in 2017 and into 2018. Momentum behind the continued adoption of US covenant-lite terms into European loans is strong as there is now a growing body of European "cov-lite" precedents, demonstrating a growing and now deep market acceptance of cov-lite. This convergence brings a number of documentation issues to consider.

Covenant-lite Loans

In a covenant-lite loan, either there is no financial maintenance covenant or there is a single financial covenant solely for the benefit of the lenders under the revolving credit facility with no financial maintenance covenant for the term lenders. The covenant benefitting the revolving lenders typically is a "springing" covenant, i.e., tested when the revolver is drawn and such usage exceeds a certain percentage of the revolving credit commitments, often 25–35%, with the applicable levels set with significant EBITDA "cushion" or "headroom" of around 30% or more and no or very few step downs. Associated provisions customary in US covenant-lite structures are also now being adopted in Europe and in some cases are being made even less restrictive in Europe. For example, the US-style equity cure, with amounts being added to EBITBA and no requirement for debt pay-down, is now being regularly accepted in European covenant lite, but the US approach of limiting EBITDA overcures currently is a point for negotiation in Europe.

Documentation

In the past there was a 'battle of the forms' in relation to documenting European covenant-lite loans, with the first covenant-lite loans emerging in Europe in 2013 being documented under New York law. The next generation were governed by LMA-based credit agreements, stripped of most financial covenants and otherwise modified in certain respects to reflect "looser" US practice on terms for covenant-lite deals, including primarily leverage or coverage based incurrence style ratio baskets rather than traditional loan market baskets fixed at a capped amount. We now also regularly see LMA-based loan agreements that in addition to the absence of financial covenants for the term loan adopt bond-like covenant schedules, sometimes paralleling a bond in the borrower's debt capital structure but also increasingly frequently, on a standalone basis. A number of the other features of current covenant-lite European leveraged loans are considered below.

Increased Debt Baskets

Limitations on borrowings often have US-style characteristics, so rather than a traditional debt basket with a fixed capped amount, we now see permitted debt limited solely by a net leverage or senior secured leverage test with a separate fixed ("freebie") basket alongside. This debt can be raised through an incremental "accordion" feature and increasingly separate "sidecar" financings. This style of covenant leads to far greater flexibility for a borrower to raise additional debt as pari secured, junior secured, unsecured or subordinated loans or bonds. In some financings, reclassification is permitted so that the "freebie" basket can be used if the ratio basket is unavailable, and then subsequently moved into the ratio basket once the ratio is met, thus freeing up the "freebie" basket.

Builder Baskets

Another trend from the US covenant-lite loan market (which is also a feature of the high yield bond market) that is being adopted in European loan deals is a "restricted payments builder basket," where the borrower is given "credit" as certain items "build up" to create dividend capacity, starting with the borrower's retained portion of excess cashflow ("ECF"), IPO and other equity proceeds, and unswept asset sale proceeds, usually subject to a net leverage ratio governor as a condition to usage. In many cases there may be no limit on distributions if a lower leverage ratio test is met. There is a trend towards an even more aggressive variant based more closely on the high yield bond formulation, which credits a percentage of consolidated net income ("CNI") (usually 50%) rather than retained excess cashflow, with the disadvantage for lenders in that CNI is not reduced by the deductions used to calculate ECF and because the build-up may begin for years prior to the onset of the ECF sweep.

US-style Events of Default

US loan or high yield bond-style events of default can be controversial with European loan syndicates, but we have seen more loan financings that include defaults more akin to the US loan approach, e.g., removal of material adverse change default; no audit qualification default or even the high yield bond approach (more limited defaults, including cross acceleration rather than cross default, with longer remedy periods and the longer periods for bankruptcy defaults that are standard in the US but historically unusual in Europe).

Other Provisions

There are a few other provisions we are seeing migrate from the US covenant-lite (or high yield) market to Europe and becoming well-established, including:

- "Permitted Acquisitions" controlled by the overall leverage test rather than by imposing absolute limits – and generally fewer controls on acquisitions.
- "Permitted Disposals" similarly trending towards a high yield formulation that does not impose a cap and has varying requirements for reinvestment/prepayment and cash consideration.
- Guarantor coverage ratios are trending towards an EBITDA test only (at 80–85%).
- Change of control mandatory prepayment being adjusted to allow individual lenders to waive repayment (becoming effectively a put right).
- Increased use of general "baskets" (as distinct from and in addition to ratio-based incurrence tests) with a soft dollar cap that increases as total assets or EBITDA grows.
- Provisions that state that if FX rates result in a basket being exceeded this will not in and of itself constitute a breach of the debt covenant (or other limitation).
- Use of the concept of a "Restricted Group" and ability to designate subsidiaries as "Unrestricted" and therefore outside the representations and covenants.

Economic Adjustments

Economic adjustments such as a 101% soft call for six months, (sometimes) a positive EURIBOR floor, and nominal (0.25%) quarterly amortisation are also often introduced to make loans more familiar to US loan market participants.

Structural Consequences – The Intercreditor Agreement Revisited

Adopting products from other jurisdictions brings with it the risk of unintended consequences. US terms and market practice have developed over decades against a background of the US bankruptcy rules and US principles of commercial law. The wholesale adoption of US terms without adjustment to fit Europe's multiple jurisdictions can lead to a number of unintended consequences.

A good example of this relates to European intercreditor agreements, which have over time developed to include standstills on debt claims and release provisions. At heart is the continuing concern that insolvency processes in Europe still, potentially, destroy value and often do not automatically impose creditor standstills while matters are being sorted out. Although significant steps have been taken in many jurisdictions to introduce more restructuring friendly and rescue-driven laws, it remains the case that in Europe there is a far greater sensitivity to the ability creditors may have in times of financial difficulty to force an insolvency filing by virtue of putting pressure on boards of directors through the threat of directors' liability under local laws. A significant feature of the restructuring market in Europe for many years has been the use of related techniques that creditors, particularly distressed buyers, adopt to get a seat at the table by threatening to accelerate their debt claims. Intercreditor standstill provisions evolved to prevent creditors from using this type of action to disrupt a restructuring without having to resort to a bankruptcy proceeding to provide a stay and thereby obtain increased recoveries.

Another intercreditor provision of great focus over the years has been the release provision, which provides that in the case of distressed asset sales following default and acceleration, the lenders' debt and guarantee claims against, and security from, the companies sold are released. In some deals from the last decade, these protective provisions had not been included, with the result that junior creditors could gain significant negotiating leverage because their approval was needed for the release of their claims and security, without which it is not possible to maximise value in the sale of a business as a going concern.

The potentially significant debt baskets referred to above become relevant in this context. In the US, where this flexibility originated, debt baskets do not legislate as to where in the group debt can be raised as long as the borrower is also a guarantor of the primary debt – structural subordination does not often play a significant role in a US bankruptcy because of the way that regime deals with competing claims. In Europe, structural subordination can have a dramatic effect on recoveries (as suffered by the first wave of European high yield bonds in the 1990s, which were structurally subordinated). Even if those subsidiaries have granted upstream guarantees, the value of the claims under such guarantees are often of limited value.

Until recently, most provisions allowing the incurrence of third party debt did not require the debt providers to sign up to the intercreditor agreement unless they were sharing in the security package – this was on the basis that the third party debt was limited in amount. With more flexibility to incur third party debt it is very possible that an unsecured creditor under a debt basket can have a very strong negotiating position if the senior secured creditors are trying to sell the business in an enforcement scenario, given the lack of standstill and release provisions. The degree to which third party debt (including unsecured debt) over a materiality threshold is required to become subject to the main intercreditor agreement is very much a point of negotiation in the loan but not bond market at the moment.

What Does This Mean for the Rest of 2018?

While some tightening has already occurred in the US and may be followed in Europe during 2018, nonetheless it seems likely that low interest rates by historical if not recent standards may well prevail in the Eurozone for some time, and a relative shortage of deals compared to the depth of the investor base looking both to deploy capital and seeking yield will continue to permit significant flexibility in covenant and documentation issues. Further loosening of terms will likely continue if this environment continues.

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Yankee Loans and Cross-Border Loans – Recent Developments

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Introduction

This chapter is intended to provide an introduction to practitioners to explain the issues that arise in connection with Yankee Loans and other Cross-Border Loans:

- What is a Yankee Loan? What about a Cross-Border Loan?
- Look back at the Yankee Loan market and the emergence of the Cross-Border Loan market in 2017.
- Outlook for Yankee Loan and Cross-Border Loan market in 2018 (amid the continuing convergence of covenant terms between the US and European Term Loan B markets and between the Term Loan B and High Yield Bond markets).
- Summary of Key Structuring Considerations for Yankee Loans and Cross-Border Loans.
- Comparison of certain key terms in US, European and Asian leveraged finance markets (and related credit documentation) in light of the Key Structuring Considerations.

What is a Yankee Loan? What About a Cross-Border Loan?

"Yankee Loans" are US dollar-denominated term loans that are provided to non-US borrowers which are syndicated in, and usually include terms typical for, the US Term Loan B institutional market.

Usually, these have been based on **New York law** credit documentation, but on the back of the strong growth of the European Term Loan B market in 2017 (which has continued into 2018), the market is now starting to see some cross-border deals with US dollar-denominated term loan tranches that are provided to non-US borrowers, based on **English law** credit documentation, which are syndicated in the US Term Loan B institutional market. So far, these have comprised more of a hybrid of US and European Term Loan B market terms. In this chapter, we refer to this new style of Yankee Loans simply as "Cross-Border Loans".

A Look Back at the Yankee Loan Market and the Emergence of the Cross-Border Loan Market in 2017

In 2017, the US market saw a substantial increase in the amount of US-dollar denominated loans issued to non-US borrowers, reaching a record-high of $74.7 billion, up 174% from 2016 issuance volume of $27.3 billion.[i] This is commensurate with the increase in overall lending volumes in 2017 in general.

Separately, the European Term Loan B market (for all currencies) saw 2017 issuance volume reach $166.7 billion, almost doubled from $85.5 billion in 2016, with the number of deals leaping from 237 to 402.[ii] More importantly, terms in the European Term Loan B market have evolved so rapidly over the past 6–12 months that, in some instances, borrowers have been able to obtain more friendly terms in the European market than the corresponding terms available in the US market.

For Asian borrowers, the continued high level of liquidity available from local lenders (which comprises domestic champions in each of the key markets in the APAC region, as well as the local branches of major international investment banks), makes local pricing too competitive for the international institutional markets. The arbitrage on covenant and terms flexibility offered by the international institutional markets has not been enough to overcome this pricing differential across most local markets and, in addition, strong Asian borrowers backed by international financial sponsors have been able to negotiate a large number (if not all or most) of the "bells and whistles" on covenant and terms flexibility that would be available in the US or European Term Loan B markets in certain transactions.

Outlook for 2018

The outlook for Yankee Loan issuance over the course of 2018 remains difficult to predict.

Factors that might contribute to a possible decline include the continuing growth in depth and liquidity in the European Term Loan B market and the current low interest rate environment in Europe, which may make that market more attractive to issuers, coupled with a rising interest rate environment in US loan markets.

However, factors that may result in a trend in the opposite direction include the impact of the introduction of the ECB leveraged lending guidelines on European leveraged lending, and the continuing uncertainty that may arise during Brexit negotiations between the UK and the EU.

Furthermore, the impact of recent changes to the US tax code introduced by the 2018 Tax Cuts and Jobs Act may possibly result in multinational companies looking to utilise more non-US borrowing capacity to mitigate the effect of the new cap on interest deductibility on US companies introduced by these reforms.

The choice of market in which to syndicate debt will, however, still be largely driven by pricing, currency needs and quantum at the relevant time of issuance.

In terms of documentation trends, now that the US and European Term Loan B markets are matching each other much more closely on most key terms, especially on large cap deals, we may start to see more deals that feature US dollar-denominated loan tranches made available under English law-governed credit documentation for new facilities. However, we would continue to expect New York law to be the main choice of law for credit documentation for US dollar-denominated Term Loan B tranches. At the same time, we expect that US market terms are likely to become more strongly influenced by terms obtained by issuers in the European Term Loan B market than in previous years.

Summary of Key Structuring Considerations for Yankee Loans and Cross-Border Loans

Analysis of the applicable insolvency regime is key

When structuring Yankee Loans or Cross-Border Loans, it is essential to give due consideration to the insolvency regime that is likely to apply in an enforcement scenario. Thus, an accurate and complete understanding of the insolvency laws in the jurisdiction and the location of the borrower(s) and the guarantor(s) of the senior secured debt is of paramount importance.

A primary focus of senior secured lenders in structuring any leveraged finance transaction is to maximise the likelihood of repayment in a default or restructuring scenario. This is generally achieved by ensuring that senior secured lenders can control any restructuring process, and the mechanisms for doing this differ between the US, Europe and Asia.

Snapshot of the global position

Whereas the US benefits from Chapter 11 and the UK has developed the court-approved scheme of arrangement to deal with restructurings, the applicable restructuring regimes in other jurisdictions are considerably less uniform, codified and comprehensive. However, in 2017 certain jurisdictions recognised the need to overhaul their local insolvency processes (with notable developments in India, the Netherlands, Singapore and Spain) and a new Dutch scheme and pre-pack arrangement is expected to come into effect in 2018. It remains to be seen whether the changes introduced in these jurisdictions will significantly improve the position of senior secured lenders.

United States Chapter 11

In the US, a typical in-court restructuring in a leveraged finance transaction is usually accomplished through a Chapter 11 case under the US Bankruptcy Code. Chapter 11 allows senior secured lenders to cram down "out of the money" junior secured or unsecured creditors and release the related debt claims, guarantee claims and security pursuant to a Bankruptcy Court-approved plan of reorganisation.

A Chapter 11 restructuring is an in-court process where the primary aim is to allow a business to restructure its operations and capital and emerge out of bankruptcy as a going concern. Approved Chapter 11 plans are binding on all creditors of a debtor (or group of debtors). Prior to a Chapter 11 plan being approved, an automatic stay applies (with global effect) that prohibits any creditor, including trade creditors and suppliers, from taking enforcement action which could diminish the value of the business.

Europe and Asia – Out-of-court process

By contrast, in Europe and Asia, it is more usual for a restructuring in a leveraged finance transaction to be accomplished through an out-of-court process. Most commonly, this is achieved through enforcement of share pledge security in order to transfer ownership of the top holding company of the credit group and effect a sale of the business as a going concern.

One of the key reasons for this is that placing a company into local insolvency proceedings in many European and Asian jurisdictions is viewed very negatively – quite often only as the option of last resort. Suppliers and customers typically view it as a precursor to the corporate collapse of the business and often there is no Chapter 11 equivalent restructuring process available in the applicable European or Asian jurisdiction. The result is that entering into local insolvency proceedings can be value-destructive (in particular because of the lack of an automatic stay that binds trade creditors and suppliers and, in some cases, because of a lack of clear procedures for cramming down junior creditors).

Europe and Asia – an alternative – the English court-based scheme of arrangement

As an alternative to an out-of-court process, creditors in Europe and Asia who document their transactions under English law may be able to take advantage of a scheme of arrangement – a statutory procedure under the UK Companies Act which allows a company to enter into compromises and arrangements with its creditors, with those compromises and arrangements then being sanctioned by an English court.

Notwithstanding that a European- or Asian-centric transaction may have no substantive nexus to England, the scheme of arrangement option may still be available, as the English courts have determined that a sufficient connection will exist to enable an English court to sanction a scheme of arrangement so long as a primary finance document contains an English choice of law and exclusive jurisdiction clause.

The primary aim of a scheme of arrangement is to allow an arrangement or compromise in respect of debt claims of a (solvent or insolvent) company to be made, and to be binding on all creditors, if the scheme is agreed by a majority in number and 75% by value of all creditors (or each class of creditors) including secured creditors. This approach effectively enables a 'cram-down' of minority creditors in a similar manner that Chapter 11 would in the US even if the other benefits of a Chapter 11 proceeding (e.g., the automatic stay) may not be present. However, it should be noted that the English courts may use their discretion to grant a stay on action by creditors on a case-by-case basis if the court considers, among other things, that the scheme of arrangement is reasonably likely to succeed.[iii]

The role of the intercreditor agreement in out-of-court processes

In order for senior secured lenders to retain control of an out-of-court restructuring process (in situations where it is not possible to rely on a Chapter 11 process, an English scheme of arrangement or any other similar local insolvency in-court process), they have traditionally relied on contractual tools contained in a European-style intercreditor agreement, with specifically tailored provisions relating to enforcement standstills and release provisions.

An enforcement standstill operates to limit or prohibit junior creditors from taking any enforcement action including taking any steps to accelerate their debt claim or to enforce (or instruct the security agent to enforce) the transaction security. Standstills are designed to prevent junior creditors from obtaining leverage by threatening to force borrowers or guarantors into a value-destroying local insolvency proceeding and to allow the senior secured lenders time to implement a controlled disposal of the credit group through enforcement of their own, higher ranking, transaction security.

Release provisions apply upon a "distressed" disposal of the credit group, i.e. a disposal following an acceleration event or when transaction security has otherwise become enforceable. The release provisions allow senior secured lenders to sell a business free of the claims of junior creditors that are party to the intercreditor agreement. Such release provisions provide that all of the borrowing and guarantee liabilities of, and the security granted by, the borrower or guarantor being sold (together with the borrowing and guarantee liabilities of, and the security granted by, any of its subsidiaries) will be released upon a distressed disposal.

Because the release provisions give senior secured lenders the right to eliminate the debt claims of junior creditors, so called "fair value protections" are typically included to give junior creditors some degree of comfort that the enforcing senior secured lenders will sell the business for a "fair price" on arm's length terms. This "fair value protection" is a contractual attempt to provide comfort similar to that obtained through the judicial oversight afforded in a Chapter 11 or scheme of arrangement in-court process.

Location location location – key considerations regarding the jurisdiction of borrowers and guarantors

In US secured loan transactions, the borrower could be organised in any state of the US without giving rise to material concerns for senior secured lenders. In Europe or Asia, however, there are a number of considerations which are of material importance to senior secured lenders when evaluating in which European or Asian jurisdiction a borrower should be organised and the quality and value of credit support that will be available.

Lender licensing rules

Many European and Asian jurisdictions impose regulatory licensing requirements for lenders providing loans to borrowers organised in that particular jurisdiction (which is not a consideration that generally causes concern in US deals).

Withholding tax on interest payments

Withholding tax may be payable in respect of payments made by borrowers organised in many European or Asian jurisdictions to lenders located outside of the same jurisdiction (in particular, many "offshore" US Term Loan B investors are unable to lend directly to a borrowers located in certain European and Asian jurisdictions without triggering withholding tax or interest deductibility issues). In addition, some European jurisdictions may impose limits on the number of creditors of a particular nature that a borrower organised in that jurisdiction may have without triggering additional withholding tax obligations.

Foreign debt restrictions

In certain jurisdictions in Asia, there are restrictions prohibiting or limiting local borrowers from issuing foreign debt (i.e. debt that is either provided by a non-resident lender or that is not denominated in the borrower's local currency).

Foreign exchange restrictions

In certain jurisdictions in Asia and Latin America, foreign currency exchange rules mean that there are limitations – or in some cases, prohibitions – on expatriating cash and, to add to the complexity, these rules in some cases can be vague, untested and subject to frequent and unpredictable change.

Other considerations to note

US Co-Borrower for US institutional market

Many institutional investors in the US leveraged loan market (CLOs in particular) continue to have investment criteria which govern the type of loans in which they may participate. These criteria usually include specifying the jurisdiction of the borrower of the relevant loans, with larger availability or "baskets" for loans to US borrowers, and smaller "baskets" for loans to non-US borrowers. As a result, some Yankee Loan deals and Cross-Border Loan deals have included US co-borrowers in an effort to ensure that a maximum number of US Term Loan B institutional investors can participate in any US-dollar term loan financings.

Automatic acceleration

The US Bankruptcy Code does not permit lenders to take any action against a debtor in a US bankruptcy case to collect their loans after that debtor files for US bankruptcy, including taking actions against any collateral or to accelerate the maturity of the loans. Since most guarantees provide that the guarantor is obligated to pay the guaranteed debt "when due", it is necessary that such debt be accelerated for a guarantee to be fully called upon prior to the final scheduled maturity of the guaranteed debt. The automatic acceleration provision is crucial since it removes any doubt as to whether the loans have been accelerated without violating the automatic stay applicable to the debtor (by avoiding the need for service of any acceleration notice), thereby enabling lenders to call on any guarantees of non-bankrupt guarantors. However, including a US-style automatic acceleration provision, whilst an important structural feature in a domestic US deal (due to the automatic stay applicable upon a US bankruptcy filing), may not result in the right outcome in the context of a non-US credit group. Such a provision could force certain non-US borrowers and guarantors into a local insolvency process which may be value-destructive and may derail the manner in which a senior secured creditor is trying to organise and control a restructuring process. Careful thought should therefore be given as to which non-US borrowers and guarantors are subject to automatic acceleration provisions (taking into account the fact that certain non-US entities can easily file for US bankruptcy protection).

Comparing guarantees and security in different jurisdictions

US and Canada

The value of security and guarantees from borrowers and guarantors located in the US in secured loan transactions is generally not a source of material concern for senior secured lenders. The UCC provides for a relatively simple and inexpensive means of taking security over substantially all of the non-real property of a US entity and taking security over real estate and IP assets is, generally, relatively straightforward and inexpensive. Furthermore, save for well understood fraudulent conveyance risks, upstream, cross-stream and downstream guarantees from US entities do not give rise to material value leakage concerns for senior secured lenders. A similar position applies in Canada.

Europe and Asia

In contrast, with the notable exception of the UK, there are very few European and Asian jurisdictions in which fully perfected security interests can be taken over substantially all of a debtor's non-real property assets with the ease or relative lack of expense afforded by the UCC. In addition, taking security over real estate and IP assets in these jurisdictions is generally less straightforward and can often be very expensive. Furthermore, the value of upstream and cross-stream guarantees that can be provided by companies in many European and Asian jurisdictions is frequently limited as a matter of law (and in some cases, may be prohibited altogether). This can often mean that value leakage is a material concern because lenders do not get the benefit of either a guarantee for the full amount of their debt or security in an amount equal to all or substantially all of the value of the assets of the relevant guarantor.

Some other factors which do not apply to US borrowers or guarantors also need to be taken into account for European and Asian borrowers and guarantors. Examples include: (1) in many jurisdictions, it is not practically possible to take security over certain types of assets, especially in favour of a syndicate of lenders which may change from time to time (if not from day to day) and general restrictions may exist for security that supports obligations owed to financial institutions outside the jurisdiction of incorporation of the relevant security provider; (2) in some jurisdictions, it is not possible to take both first-ranking and second-ranking security over the same asset (which, in financings with a second lien facility, necessitates that the first-ranking security is held as "common security" with the proceeds distributed in accordance with agreed intercreditor arrangements (although even this approach is not possible in certain jurisdictions); and (3) the US concept of excluding certain assets from the security package can cause legal issues for certain types of "floating" security available in some European and Asian jurisdictions where customary guarantee and security principles would more appropriately operate to reflect local market requirements (note, in this regard, that recent deals backed by strong global financial sponsors retain the US-style "Excluded Assets" concept and also include the European-style guarantee and security principles concept, which can often result in greater overall exclusion of assets from the security package in both the US and non-US jurisdictions).

In addition, to ensure that a European or Asian borrower group restructuring may be accomplished through the use of the relevant intercreditor provisions, it is important to determine an appropriate "single point of enforcement" in the group structure where a share pledge could be enforced quickly and efficiently, without interference by other creditors and stakeholders, in order to effect a sale of the entire business as a going concern. In this regard, the governing law of the share pledge and the jurisdiction of the relevant entity whose shares are to be sold should be carefully considered to ensure that the distressed disposal provisions in a European or Asian intercreditor agreement may be fully taken advantage of (if and when needed).

What happened to credit documentation in 2017?

A look back at trends emerging in 2017

Deals involving a credit group with operations based primarily in the US continued to adopt a traditional US approach to structuring and are drafted based on the expectation that any restructuring will be effected through a Chapter 11 process (or out-of-court using Chapter 11 principles). The credit documentation for these deals is governed by New York law.

Deals involving a credit group with operations predominantly located outside the US usually adopted a traditional European or Asian approach to structuring, based on the expectation that any restructuring would be effected through an out-of-court process relying on contractual tools set out an intercreditor agreement (as described above). The credit documentation for these deals is typically English law-governed (based substantially on LMA or APLMA form documentation). However, in 2017, European deal terms evolved rapidly, with a substantial increase in the volume of covenant-lite European Term Loan B issuance (which included terms that much more closely match, and in more recent deals, have even exceeded the flexibility more commonly seen in US Term Loan B deal terms) and in some cases, the governing law for the covenants (as opposed to the rest of the document) was New York law, even in deals that did not include any US dollar-denominated term loan tranche. The trend towards greater covenant flexibility was also observed in some Asian deals involving strong borrowers or international top tier sponsors.

Prior to 2017, Yankee Loan deals had typically been done using New York law credit documentation. But the latter half of 2017 saw the emergence of some Cross-Border Loan deals, where non-US borrowers tapped the US loan market for US dollar denominated term loan tranches, using LMA-style English law credit documentation. These Cross-Border Loan deals typically included US-style covenant terms, often in a separate schedule, governed separately by New York law. Further, as previously noted, the covenant packages in these Cross-Border Loan deals contained even more flexibility compared to the corresponding covenant packages seen during the same period in the US market. The initial rationale for the emergence of these Cross-Border Loans was due to the issuers' desire to align the covenant packages of their Term Loan B facilities with their simultaneously issued High Yield Bonds. However, this practice of using New York-style covenant packages, including in some cases those being governed by New York law for their interpretation, has gained momentum in the European market to the point that such terms are being accepted in deals where the capital structure does not include High Yield Bonds.

The rapid evolution in terms has been driven in large part by an imbalance across markets between supply and demand, giving rise to some of the most borrower-friendly terms seen in international debt capital markets since the early days of the financial crisis in 2007–2009.

Notwithstanding this, when including US-style covenant terms for credit groups which are predominately located in non-US jurisdictions, it remains very important to consider whether such terms are appropriate for credit groups where it would be much more likely for a restructuring to occur outside of Chapter 11. This is because US-style covenant packages were designed for, and gained acceptance in, the US market based on the presumption that for a traditional US-based borrower and guarantor group, US Chapter 11 principles, protections and processes would dictate the outcome of any restructuring. That may not be the case when the borrower and guarantors are primarily non-US entities and the flexibility permitted by such covenant packages (in particular, in regard to incurring additional debt, making future investments and acquisitions and certain intercompany transactions) may not be adequate to preserve the senior secured status of any Term Loan B tranche (and any *pari passu* revolving facility) absent the applicability of the Chapter 11 regime.

What's next in 2018 and beyond?

As US, European and Asian international capital markets continue to evolve and mature, it can be expected that credit documentation in different loan markets will continue to be impacted and that further convergence of terms between the US and European Term Loan B markets in particular, and between the bank and bond markets more generally, is likely to occur while benign market conditions continue. The continuing globalisation of the private equity and leveraged finance markets in 2018 and beyond will increasingly result in pressure for terms that become customary in one region to be adopted quickly in other regions. Lenders will need to consider carefully whether it is appropriate in all cases to import terms accepted in one region into deals featuring borrowers and guarantors in different regions (as a 'one size fits all' approach may well not be appropriate in all circumstances).

In Asia, it is notable that institutional investors (who typically require higher yields in exchange for lighter terms) are less prevalent than in the US and European markets because of the high level of liquidity available from local lenders. This means that it is unlikely that Asian issuers will need to tap the US capital markets in the near future by way of a true Yankee Loan. But local lenders are under increasing pressure to accept covenant-lite and covenant-loose terms in transactions involving international financial sponsors (and it is worth noting in this regard that the portion of global private equity capital being deployed in Asia has increased from approximately

15% five years ago to more than 25% at present). This, coupled with approximately $130 billion of private equity dry powder in Asia,[iv] make it fairly likely that Asian credit documentation terms will continue to converge with terms in the US and European markets on transactions with international financial sponsors.

In Australia, the first Australian dollar Term Loan B transaction governed by Australian law closed in September 2016, and 2017 saw a number of additional high-profile Australian dollar Term Loan B acquisition financing and dividend recap transactions involving domestic and international financial sponsors governed by Australian law (in a shift away from earlier transactions governed by New York law). The Australian market has been increasingly following the US and European markets, where non-bank and institutional players are playing an increasingly prominent role in owning leveraged loans, although the traditional bank market remains active. As a result of the rise of non-bank lenders and the ability of domestic and international financial sponsors to import loan terms from US or European credit documentation, covenant-lite Term Loan B structures have become more common and other documentary terms have loosened. The ability to denominate Term Loan B financings in Australian dollars also alleviates the need for US/Australian dollar currency hedging, which is particularly relevant when the majority of buyouts in the Australian market (outside the resources sector) are denominated in Australian dollars.

Comparison of Key Terms in US, and European and Asian Leveraged Finance Markets (and Related Credit Documentation) in Light of Key Structuring Considerations

When considering what changes should be made to credit documentation terms for a Yankee Loan or Cross-Border Loan, market participants should be aware of historical differences in drafting styles between New York law credit documentation and European and Asian LMA and APLMA credit documentation, based on the expected outcome under different applicable insolvency regimes.

US and European covenant-lite deals

US and European leveraged loan terms

The vast majority of leveraged loans issued in the US and a much larger portion of leveraged loans issued in Europe were done on a covenant-lite basis in 2017. In 2017, the value of covenant-lite loans issued in Europe stood at $96 billion, more than double the 2016 figure of $40.4 billion.[v]

In a covenant-lite deal, term loans do not benefit from any maintenance financial covenant. Only the revolving facility benefits from a single maintenance financial covenant, normally a leverage-based ratio test (and this only applies on a "springing" basis, i.e. at the end of a fiscal quarter, on a rolling LTM-basis, if utilisation exceeds a certain trigger percentage typically ranging between 30 and 40% of revolving capacity).

More importantly, the negative covenant package for "covenant-lite" loan facilities is either fully or partially incurrence-based in nature, similar to what would historically be found in a US high-yield unsecured bond covenant package, reflecting the rapid and continuing convergence between the Term Loan B and High Yield Bond markets in the US and Europe.

Whereas traditionally, European leveraged loans were structured with a suite of four maintenance financial covenants testing leverage, interest cover, cashflow cover and capex spend, followed in more recent times by a trend towards more "covenant-loose" deals (which include only leverage and interest cover protection), the volume of covenant-lite deals in Europe expanded much more rapidly in 2017 in comparison to prior years. Covenant-lite deals accounted for 78% of total leveraged lending in the market last year: considering the fact that there were zero covenant-lite deals between 2008 and 2011, the uptick has been substantial over time[vi] and is arguably one of the most significant changes to deal structures in the last decade.

Asian leveraged loan terms

Asian leveraged transactions are traditionally conducted out of the established hubs of Sydney (mainly for Australian domestic transactions), Singapore and Hong Kong, which will typically cover acquisitions of assets across the APAC region. Leveraged loans in Asia still often include at least a maintenance leverage covenant, with typical LMA or APLMA style covenant protections that are not incurrence-based in nature. This is particularly prevalent in deals involving local champion banks.

However, strong borrowers backed by international financial sponsors (and typically represented by international US or UK based legal counsel) continue to push for more "covenant-lite" or "covenant-loose" terms and achieve these in transactions when there is liquidity and competitive enthusiasm amongst the large domestic and international banks for the credit.

Issues to watch out for in covenant-lite Yankee Loan and Cross-Border Loan deals

Broadly, for a US-only credit group, the additional flexibility in covenant-lite transactions does not result in any material additional enforcement risk to senior secured lenders because enforcement will still occur normally through a US Chapter 11 process.

When agreeing to increased flexibility in negative covenant packages in the case of a credit group where material credit support will be provided by non-US borrowers and/or guarantors (or where there is no US credit support at all), senior secured lenders should continue to consider the impact of this additional flexibility carefully. Historically, the flexibility included in European or Asian credit documentation was much narrower (because of the very different way in which non-US borrowers and guarantors would be treated in a restructuring or insolvency process under local law compared to a Chapter 11 process) but 2017 saw a dramatic increase in flexibility included in European credit documentation, much more closely aligned with (and in some cases even going further than) US credit documentation. That is perhaps a little surprising in light of the Key Structuring Considerations highlighted earlier in this article, but these extremely borrower-friendly market conditions were driven by a high demand for leveraged loans in Europe throughout 2017.

Below is a summary of some recent developments and key issues in credit documentation terms in the different loan markets.

Limitations on debt incurrence for incremental/accordion debt, incremental equivalent debt, incurred acquisition debt and ratio debt

In New York law-governed leveraged loan deals, there is usually no hard cap on debt incurrence, i.e. an unlimited amount of additional debt can be raised subject to compliance with one or more different incurrence financial ratio tests.

Such debt may be equal ranking secured debt incurred pursuant to the credit agreement as incremental debt, typically by the existing borrower(s) only.

It may also be incremental equivalent debt (relying on incremental/accordion basket capacity), incurred acquisition debt or ratio debt, and such debt may be either senior secured debt (which can be in the form of senior secured notes or in some cases in the form of sidecar loans) or junior secured, unsecured or subordinated debt. In each case, such debt is incurred outside of the credit agreement, and usually can be incurred by any "restricted" subsidiary, usually subject to a non-guarantor cap. The same "MFN" pricing protection that applies to incremental/accordion debt usually also applies to incremental equivalent debt, incurred acquisition debt or ratio debt incurred in the form of *pari passu* secured term loans, although many deals now include a suite of carve-outs to the MFN protections (with many current top tier deals excluding some or all of the following incurrences of *pari passu* secured term loans from MFN protections: debt incurred under the fixed dollar prong of the incremental amount, debt incurred to finance acquisitions or investments, debt maturing a certain duration (usually two years or more) after the existing term loan maturity and, sometimes, an additional fixed dollar basket amount (with an EBITDA-based grower) for any type of debt).

Debt incurrence flexibility works well in deals that only involve US borrowers and guarantors, because there is generally no material concern about being able to deal with junior secured creditors or unsecured creditors in a restructuring or bankruptcy context where Chapter 11 principles apply and usually because of the additional protection afforded by customary caps on the amount of debt under such baskets that can be incurred by non-guarantors that would rank structurally ahead of senior secured creditors.

However, in deals that involve non-US borrowers and guarantors, if comparable debt incurrence flexibility is allowed, issues can arise due to the fact that guarantees provided by non-US entities may be subject to material legal limitations and/or prohibitions and because the scope of security provided by non-US entities may be subject to material legal and/or practical limitations resulting in security over significantly less than "all assets" of the relevant non-US entity. This could lead to some unexpected results for senior secured lenders in a Yankee Loan deal or Cross-Border Loan deal. Issues may also arise in relation to the equality of credit support between different senior secured debt tranches (in deals that feature CAM exchange or loss sharing protections).

Specifically, the claims of creditors of incremental equivalent debt, incurred acquisition debt or ratio debt, even if junior secured or unsecured, may rank equally, or in some cases structurally senior, to the guarantee claims of senior secured lenders who provided the original senior secured credit facilities.

Several factors can lead to this outcome. For example, incremental/accordion debt, incremental equivalent debt, or ratio debt not incurred for acquisition purposes would likely be subject to less stringent guarantee limitations or prohibitions in some jurisdictions than the guarantee limitations or prohibitions applicable to the original senior secured credit facilities incurred as acquisition debt to finance the initial LBO transaction. Also, in many jurisdictions the scope of security provided by the applicable non-US borrowers and guarantors is not fully comprehensive (for the reasons described in "Comparing guarantees and security in different jurisdictions" above), resulting in a larger pool of unsecured assets, the value of which will be shared equally among senior secured creditors, junior secured creditors and unsecured creditors with equal ranking debt claims.

Additionally, in the event of a restructuring accomplished by means of a distressed disposal and release of borrower and guarantor claims, providers of incremental debt, incremental equivalent debt, incurred acquisition debt or ratio debt may not be subject to the contractual enforcement standstill or release provisions provided under a customary European-style or Asian-style intercreditor agreement.

The solution to this is the inclusion of provisions that cap the amount of additional debt (especially junior secured debt, and in the case of non-US entities, importantly also unsecured debt) that can be incurred without the new creditors in respect of such additional debt entering into an intercreditor agreement with the existing senior secured lenders. In the European market, 2017 saw an increase in the number of lenders who are pushing to include for such intercreditor protection (but there still is no consistent approach on this issue in either the US or the European Term Loan B markets). We would continue to recommend that it makes sense in both US and European deals involving non-US borrowers or substantial non-US credit support to consider including such protections, and this should be negotiated on a deal-by-deal basis.

In the case of new first lien or senior secured debt, inclusion of an additional provision requiring the new creditors to become subject to any existing CAM exchange or loss sharing provisions between existing first lien or senior secured lenders should also be considered to mitigate the impact of unequal credit support between different senior secured tranches and loan facilities.

Investments and acquisitions

Permitted Acquisition cap: Consistent with High Yield Bond covenants, most US and some European Term Loan B deals now do not include a fixed cap on acquisitions and investments (although a limited number of mid-market deals in both markets retain a requirement for *pro forma* compliance with an incurrence ratio condition, sometimes above closing date levels, or, alternatively, subject to meeting a "no worse than" test).

Third Party Non-Guarantor Cap/Value leakage: In US deals, there are now many instances where there is no third-party non-guarantor investment cap, provided that acquired entities become restricted subsidiaries, consistent with the approach in High Yield Bond covenants (the logic being that lenders rely on the non-guarantor cap applicable to limitations on debt used to finance acquisitions). In Europe, some deals include a non-guarantor cap (or a guarantor coverage test requirement) but an increasing number of covenant-lite European Term Loan B deals do not include this protection (or, in cases where guarantor coverage tests are retained, the applicability of agreed guarantee and security principles that limit the requirements to provide guarantees based on local limitations, will likely result, in practice, in far less credit support than the corresponding position in a US deal).

While this is less of an issue in US domestic deals, in deals where a substantial portion of the credit group is or becomes non-US based, this could give rise to significant erosion in the value of credit support available to senior secured lenders over time because of the difference in the quality of credit support available in some non-US jurisdictions (either due to limitations on available guarantees or due to the scope of the available security package).

No cap on Intercompany transactions/J Crew issue: An additional instance in which the shift to High Yield Bond style covenant flexibility could lead to unintended consequences in Yankee Loans and Cross-Border Loans pertains to intercompany asset transfers and investments. Many US Term Loan B facilities issued in 2017 adopted the High Yield Bond approach of unlimited intercompany asset transfers and investments within the restricted group (i.e., free transfer between the borrower and all restricted subsidiaries – loan parties and non-loan parties alike). Here again, investors were expected to rely upon non-guarantor caps in the debt covenant carve-outs that in theory limit the amount of structurally senior debt that can be incurred in reliance on assets or value transferred from loan parties to non-loan party restricted subsidiaries. However, as noted, these protections may not be as effective outside of the US where guarantee limitations and the like impact the credit support available from certain guarantors.

Moreover, the now infamous J. Crew trapdoor provision that is included in a lot of existing precedents in the US market could lead to additional leakage via a seemingly innocuous provision allowing for non-guarantor restricted subsidiaries to make unlimited investments in unrestricted subsidiaries with proceeds of an initial permitted investment from the borrower or guarantor into the non-guarantor restricted subsidiary. The expansion in unlimited basket investment capacity also potentially gives rise to the same issue. However, investors in both the US and European markets continue to be focused on this issue in recent transactions and have been resisting the inclusion of the trapdoor in new issue US and European Term Loan B facilities (including Yankee Loans and Cross-Border Loans).

Available Amount (or "Builder") basket for third party investments, restricted payments and restricted debt repayments

In US and European deals, this basket builds with 50% of Consolidated Net Income (now frequently excluding the deduction for 100% of losses in top-tier deals in contrast to the corresponding provision in most High Yield Bond covenants) or the retained portion of Excess Cash Flow. In addition, the basket includes certain equity contributions and returns on investments made using the Available Amount basket. In European deals, the basket sometimes also builds with Permitted Financial Indebtedness capacity. The basket can be used for (among other things) third-party investments, restricted payments and restricted debt payments. Use of the basket was historically subject to a "no Default" condition but 2017 saw substantial diminution of this protection. Use of the basket was also historically subject to *pro forma* compliance with a leverage incurrence ratio, but 2017 saw significant erosion of this protection in US deals and some erosion of this protection in European deals based on leverage ratios set at 0.5x to 1.0x inside closing date levels.

Available Amount/Builder baskets are still rarely seen in the Asian loan market. However, given the fact that we have seen significant cross-pollination of terms across the Atlantic between the US and European markets, we would not be surprised if some of the borrower-friendly trends that have emerged in the US and Europe start to appear in the Asian market in the future in large top-tier sponsor deals.

Unlimited baskets for third party investments, distributions and junior debt repayments

In many US and European deals (including Yankee Loan and Cross-Border Loan deals), it is now common for there to be uncapped ability to make third party investments, pay distributions and to repay junior debt often, but not always, subject to a "no Event of Default" condition and *pro forma* compliance with an incurrence ratio condition. Historically, the ability to utilise this basket capacity required quite significant de-leveraging but in 2017, levels tightened materially and are now typically set at 0.25× to 0.75× inside closing date total net leverage for investments and 0.75× to 1.50× inside closing date total net leverage for restricted payments and restricted debt payments. Lenders need to be aware that the flexibility provided by such baskets can give rise to the value leakage and intercompany/J Crew issues identified above, especially if this basket flexibility is combined with a trapdoor feature.

This basket has generally not been adopted yet in deals sold in the local Asian market.

Asset Sales

In US deals, there is now commonly an unlimited asset sales basket, subject to an Event of Default blocker condition (although even this protection is now excluded in many deals), and provided that 75% of consideration is cash (plus a basket for designated non-cash consideration), the sale is for fair market value and the net sale proceeds are applied and/or reinvested in accordance with mandatory prepayment asset sale sweep provisions. In some more recent top-tier sponsor deals, the percentage of net sale proceeds that must be applied in prepayment steps down from 100% to lower percentage levels based on meeting a specified first lien net leverage or total net leverage financial ratio, following a trend that first emerged in the European Term Loan B market. In both US and European Term Loan B deals, we are also seeing the retained portion of asset sale proceeds (after the operation of any step down) being added as an additional component to the Available Amount or "builder" basket for investments, restricted payments and restricted debt payments.

For European deals, there is not yet conformity in the approach to the asset disposals covenant. It is not uncommon to still see some form of general disposals baskets with an annual or life-of-deal cap combined with a fairly extensive list of carve-outs for certain identified assets. However, increasingly, European Term Loan B deals (particularly where they are structured as a hybrid to incorporate certain High Yield Bond covenants) will adopt the US approach, and many European deals now include leverage-based step downs, as noted above.

In Asian deals, the more traditional European approach is still the norm (i.e. a lengthy list of carve-outs for identified assets, accompanied by a general basket).

The top-tier 2017 markets also saw considerable convergence across US and European deals in relation to asset sale sweep reinvestment rights, where the trend followed the US market approach of asset sale proceeds being subject to a reinvestment period and typically not requiring reinvestment in any particular types of assets.

Excess Cashflow Sweep

In the same vein as asset sale sweeps, excess cashflow sweep provisions in US and European deals are increasingly aligned, with both markets typically seeing 50% of excess cashflow required to be applied as prepayment with step downs based on a leverage test (usually first lien or senior secured). Deductions relating to voluntary prepayments of term loans, other *pari passu* debt (and sometimes even second lien loans originally incurred at closing), and debt buy back amounts, are seen in both markets, although a noteworthy recent trend in both US and European deals is to give dollar for dollar credit (i.e., deductions applied after the excess cashflow prepayment amount is calculated based on the applicable percentage) for all such amounts as opposed to the traditional approach that only gave such credit for voluntary prepayments of the original senior secured credit facilities.

The same phenomenon holds true for deductions for other expenditures such as amounts used for acquisitions, investments, capex and certain restricted payments. Whereas, historically, in US deals, these amounts were deducted from excess cashflow through the operation of the definition in the applicable credit documentation, before the calculation of the sweep amount based on the applicable percentage, a trend that appeared with increasing frequency in 2017 was to deduct these amounts after the excess cashflow payment amount is calculated, resulting in a far lower prepayment to lenders.

Assignments and transfers

Unlike other 2017 trends noted above with respect to Yankee Loans and Cross-Border Loans (where the European market has largely borrowed, and in some recent cases expanded on, borrower-friendly US-style terms), when it comes to assignments and transfers of loans, the opposite appears to be the case. Most English law-governed credit documentation that includes a Term Loan B tranche is being documented with European-style transferability provisions and restrictions, which are more restrictive on transferability of loans than the typical US market approach. So, the European approach of a permitted white list of lenders with the ability to remove a certain number of names on an annual basis after closing (as opposed to the US approach of a Disqualified Lender list, which typically cannot be updated after closing), a blanket prohibition on transfers to loan-to-own or distressed investors, and expansion of transfer limitations to apply not only to assignments but also to participations and sub-participations alike has been maintained in most European Term Loan B deals (including some Cross-Border Loans – notwithstanding the intent to syndicate the US dollar tranche in those deals to the US institutional market). We have noticed a recent push to try to expand these restrictions into traditional US Term Loan B deals (including Yankee Loans), but these attempts have so far not gained widespread acceptance from US investors. Based on US market reaction, we may well see deals in 2018 that include a bifurcated approach to transferability for different loan tranches, depending on the target market in which the tranche will be syndicated. It is therefore critical that underwriters, investors and other market participants understand the impact that these provisions may have on the overall liquidity of a particular tranche and the ability to freely enter into participations and similar transactions, in light of the intended syndication strategy for that tranche.

Endnotes

i. Leveraged Commentary & Data unit in Standard & Poor's Global Market Intelligence.

ii. Dealogic Loan Analytics, as of March 5, 2018.

iii. *Bluecrest Mercantile NV v Vietnam Shipbuilding Industry Group* [2013] EWHC 1146 (Comm).

iv. Source: McKinsey&Company – For A&O NY: https://www.mckinsey.com/industries/private-equity-and-principal-investors/our-insights/asian-private-equity-defying-expectations.

v. Leveraged Commentary & Data unit in Standard & Poor's Global Market Intelligence.

vi. Leveraged Commentary & Data unit in Standard & Poor's Global Market Intelligence.

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Debt Retirement in Leveraged Financings

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A company borrows money. It would like to avoid any requirements to mandatorily prepay the debt before its maturity, such as on the occurrence of some event or contingency, in order to retain the economic benefits of that arrangement and avoid the need to raise or deploy cash to meet a required prepayment. At the same time, it would like to maximise its flexibility to voluntarily prepay the debt before its maturity, such as to refinance at a cheaper cost of capital, or to obtain less restrictive terms.

An investor lends money. It would like to ensure that it can have the debt prepaid if an event or contingency affecting the credit occurs, such as an asset disposition or change of control. At the same time, it would like to protect itself against an unexpected prepayment of the debt at the company's election, forcing the investor to redeploy its capital and lose the benefit of its investment.

The interplay between these competing goals of a borrower and its creditors shapes the prepayment requirements and protections in financing agreements. These provisions further evolve over time with changes and developments in financing markets and products. This article will discuss prepayment requirements and protections in leveraged financing agreements, as well as prepayment and refinancing techniques employed by borrowers, focusing principally on custom and practice in the United States leveraged financing markets for large cap transactions.

Mandatory Prepayment Requirements[1]

Syndicated Term Loans. Traditionally, syndicated term loans in leveraged financings have had a number of mandatory prepayment requirements. Like other features, these requirements have evolved over the years as the syndicated term loan product and debt capital structures have changed and become more complex. The syndicated term loan market has changed fairly dramatically over the last three decades, moving from a market characterised by relatively modest sized loans made and held by commercial banks to one dominated by sizable loans arranged and sold to institutional investors. Given these changes, this article will focus principally on current market practice and recent developments with respect to common mandatory prepayment requirements for syndicated term loans.

Syndicated term loans typically require prepayment with the net proceeds of specified asset dispositions and recovery events with respect to property, commonly after a period during which the borrower is entitled to apply the proceeds to reinvest in its business or repair or replace property, and subject to monetary thresholds. In some more recent transactions, the portion of the net proceeds that is required to be applied varies based on a leverage-based financial ratio, commonly beginning with 100%, and declining with step-downs based on meeting agreed ratio levels. Over the years, the feature has evolved to provide the borrower with greater flexibility to reinvest in its business and to exclude various types of transactions from the prepayment requirement. Its basic purpose, however, remains the same: to protect the investor against substantial changes in the assets of the business that may negatively affect the credit.

Term loans also commonly require a percentage of "excess cash flow" to be applied to prepay the loans, with the percentage varying with a leverage-based financial ratio, commonly beginning with 50%, and declining to zero when an agreed ratio is met. Excess cash flow is calculated for each fiscal year and any prepayment is made annually. In some more recent transactions, the prepayment requirement is subject to meeting a monetary threshold before any prepayment must be made. The excess cash flow calculation can start either with net income and add back non-cash deductions, or with EBITDA and subtract non-cash additions. The former approach has become more common in recent years. The calculations have become increasingly complex, particularly for larger and more complex businesses. In some recent transactions, deductions for investments and capital expenditures have been shifted from the definition of excess cash flow and instead applied to reduce the amount of prepayment due after excess cash flow has been calculated and the applicable percentage applied, resulting in full rather than partial credit for those payments. In addition, excess cash flow calculations now commonly take into account and deduct not only prior prepayments during the measurement period on the term loans themselves, but also on other debt secured with equal priority by the same collateral package, further adding to the complexity of the calculation. The excess cash flow prepayment requirement allows an investor to share in the cash flow generated by the business's performance in a good year, as a hedge against performance in a bad year. For a borrower, on the other hand, the excess cash flow prepayment requirement presents potential risk: if the calculation formula has missed something significant, the borrower could be facing a prepayment requirement that it is not anticipating or prepared for. In addition, paying out cash after a good year may result in a leaner cushion if performance declines in a future period. A borrower thus has a substantial incentive to try to shape the excess cash flow formula in a way that minimises the amount calculated. Term loans traditionally have offered a countervailing incentive, by allowing the borrower to increase "basket" capacity to make dividends and investments and take other actions by the amount of excess cash flow retained by the borrower. More recently, term loans have evolved to increase basket capacity by other means – for example, a percentage of consolidated assets, or 12-month EBITDA – and in some instances have moved entirely away from the retained excess cash flow construct.

A third common prepayment requirement relates to the incurrence of debt: A borrower must prepay its term loans if it incurs debt other than debt that is permitted by the term loan credit agreement. The evolution of debt incurrence features in credit agreements in recent years, providing enhanced flexibility to incur debt, including adding additional secured debt to the same collateral package, has made this prepayment requirement in many cases largely meaningless, and as a practical matter merely a way of refinancing the term loans without resorting to the voluntary prepayment features.

Syndicated term loans commonly give the investor the option to decline mandatory prepayments from the proceeds of asset dispositions and recovery events, or from excess cash flow. If the investor is happy with the investment and comfortable with the continuing credit, it may want to keep the investment and decline the prepayment. If, on the other hand, the term loan is trading at a significant discount, the prospect of a prepayment at full principal amount can create an incentive for investors to closely scrutinise a borrower's calculation of amounts subject to mandatory prepayment and enhance the need for the borrower to exercise care in that calculation.

Although not structured as a prepayment provision, syndicated term loans effectively require prepayment on the occurrence of a change of control, which typically constitutes an event of default entitling the lenders to require prepayment. How a change of control is determined, and what constitutes a change of control, has evolved over the years. Some term loans deem the change of control default to be waived or otherwise not to occur if the borrower has offered to prepay the term loans and has done so for all term loans tendered for prepayment, a construct that in effect is similar to the option to decline prepayment from asset proceeds or excess cash flow.

High-Yield Bonds. Since the early days of the high-yield bond market, high-yield bonds have required the borrower to offer to prepay bonds from the proceeds of specified asset dispositions, typically after complying with any requirement to prepay any more senior debt, and after a period of time to reinvest the proceeds in the business. For high-yield bonds, the prepayment requirement is coupled with the covenant restriction on asset dispositions. This provision requires that, if a specified asset disposition occurs, the borrower must receive fair value, the consideration must largely consist (commonly, 75%) of cash or the equivalent, or other specified types of consideration, and the net proceeds must be applied to reinvest in the business or to prepay more senior debt, and after a period of time to make an offer to prepay the bonds. As with the similar requirement for syndicated term loans, the bond prepayment requirement has evolved over the years to take into account increased business complexities and to provide the borrower with greater flexibility to make changes in its business without being required to prepay debt. The range of transactions excluded from the asset disposition restriction, the items that count toward the consideration percentage requirement or are deducted in calculating net proceeds, and the time period in which the borrower can otherwise apply the net proceeds, have all expanded substantially over the years. The application of proceeds "waterfall" has become more complex to take into account the potential for multiple bond and other financings with similar application and prepayment requirements. In some instances, the cash consideration threshold requirement has moved away from a test applicable solely to the consideration received for an individual asset disposition or a series of related asset dispositions to a test for all consideration received in connection with all asset dispositions since the issue date, allowing potentially greater flexibility for individual transactions. In addition, a feature has begun to appear that is reminiscent of the early days of high-yield bonds, providing that under certain circumstances, the application of proceeds requirement does not apply to a specified portion of the net proceeds of an asset disposition. In the early days, the provision might only cover 80% of the net proceeds absent default. Under the modern construct, the percentage steps down from 100% to a lesser percentage or to zero if a financial ratio is met. This provision thus can effectively suspend the operation of the asset disposition covenant restriction and prepayment requirement so long as the borrower meets a specified ratio. In addition, the asset disposition provision, including the proceeds application and prepayment requirements, is often one of a number of high-yield bond covenant restrictions that are suspended upon achievement of investment grade ratings.

A second prepayment provision that has long been a feature of high-yield bonds requires the borrower to offer to prepay the bonds, typically with a 1% premium, if a change of control occurs. As with syndicated term loans, how a change of control is determined, what constitutes a change of control, and the range of permitted transactions and equity holders, have evolved considerably over the years, in part to account for the complexity of the "beneficial ownership" concepts under US federal securities laws that underlie the typical change of control test in high-yield bonds; increasingly, these change of control provisions lock in these references to the US federal securities laws as in effect on the issuance date in order to avoid unforeseen consequences that might result from future changes to these securities laws.[2] The so-called "portability" construct that has become common in European high-yield bonds, permitting an acquirer to assume the bonds if specified financial or other requirements are met, has not gained traction in the US market. However, some US high-yield bonds, particularly those that are higher rated, require that a ratings downgrade occur in addition to a change of control, before the prepayment offer is required to be made. While offering an additional measure of protection to the borrower, the additional ratings downgrade requirement does not necessarily make things easier for an acquirer: the downgrade often can occur during a period of time after the change of control and still trigger the prepayment offer requirement, which may complicate an acquirer's financing plans.[3]

Other Leveraged Financing Products. Other leveraged financing products include such financing types as second lien term loans, as well as so-called "mezzanine" debt, which may be subordinated contractually in right of payment to other senior debt, or subordinated structurally by having been borrowed by a parent of the borrower of other debt. These products generally will provide for prepayment requirements similar to those for syndicated term loans and high-yield bonds. Second lien term loan provisions commonly will parallel those applicable to the syndicated term loans having first lien priority. Mezzanine debt may follow either a term loan or bond construct or a mix of both.

Protections Against Voluntary Prepayment by Borrower

Syndicated Term Loans. Traditionally, syndicated term loans have generally been prepayable without premium, on relatively short notice. This relative lack of prepayment protection is coupled with the variable interest rate nature of this financing product, which provides the investor with a rate of return that continually adjusts to the current interest rate environment.

In recent years, the syndicated term loan market has evolved, with institutional investors dominating the buy side, and opportunistic repricings and refinancings becoming more common. Prepayment protections too have evolved, with a relatively modest premium (typically 1%) being payable in connection with refinancings and amendments aimed at achieving a lower interest rate and thus a cheaper cost of capital. This so-called "soft call" protection will commonly fall away after a period of time, giving the investor some period in which it has some assurance that it will realise the benefit of its investment, while at the same time preserving for the borrower the flexibility to refinance or reprice on better terms after the soft call expires.

High-Yield Bonds. Traditionally, debt securities such as bonds have provided investors with a substantially greater degree of prepayment protection, corresponding to the generally fixed interest rate nature of this financing product. The fixed rate provides the investor with a predictable rate of return over a period of time, and the prepayment protection provides a degree of assurance that the investor will continue to receive that return over time, or an enhanced return in the form of a premium payable on prepayment of the investor's bond investment.

Investment grade bonds commonly have relatively long maturities, few covenant restrictions, and if they are prepayable at all, are prepayable only at a premium calculated at a so-called "makewhole" formula that typically results in a very expensive, if not prohibitive, refinancing cost. The effectively permanent nature of this capital is acceptable to the borrower because the covenant restrictions on the operation of its business are few and relatively benign.

In contrast, below investment grade, or high-yield, bonds typically have a maturity not exceeding 10 years – eight years is very common in the current market – and a significantly broader array of covenant restrictions aimed at protecting the investor against a wider scope of possible changes to the business and its creditworthiness that may be of greater concern given the lower credit quality of the borrower. The greater potential for these covenant restrictions to interfere with the evolution of the borrower's business and its owners' goals for their investment give the borrower a greater interest in being able to prepay its high-yield bonds at a reasonable cost: the more restrictive the contract, the more the borrower is incentivised to have the flexibility to terminate the contract and free itself from those restrictions.

High-yield bond prepayment protections have evolved over the years. In the early days of the high-yield bond market, bonds commonly were not prepayable at all for a period of time, and thereafter would become prepayable at a fixed premium that declined to zero over time. That prepayment feature has remained a common term, but has undergone some changes. For many years, the so-called "call schedule" would begin at the midpoint of the life of the bond – for an eight-year bond, after four years; for a 10-year bond, after five years – and the initial "call" premium would be one-half the interest rate, scaling down ratably to zero for repayments made within two years of maturity. More recently, as the market has moved to an eight-year senior unsecured bond paradigm, the call schedule has moved to begin three years out instead of four, with an initial "call" premium that at first was set at three-quarters of the interest rate, but now may be seen beginning at one-half the interest rate as in the earlier call schedule construct.

New prepayment features have appeared over the years, principally aimed at mitigating the impact of the absolute prepayment, or "noncall", protection during the early life of the bond. First, high-yield bonds came to incorporate a provision permitting the borrower to prepay up to a specified percentage of the outstanding amount of bonds using proceeds of a new equity issuance received by the borrower at a premium lower than a makewhole-based premium, so long as a minimum amount of bonds remains outstanding to assure sufficient liquidity for secondary trading. Initially the feature was focused on public equity offerings, on the theory that going public and paying down debt would be a credit-enhancing event and accordingly one that merited allowing the borrower to make a partial prepayment at a lower premium than a makewhole. The feature now commonly applies to any equity issuance by or contribution to the borrower. Typically the so-called "equity claw" can only be exercised during the first three years of the life of the bond, at a premium equal to the interest rate – more expensive than the premium payable when the call schedule becomes available, but less expensive for most if not all of the first three years than the makewhole feature now common in high-yield bonds, as discussed below.[4] For many years, the equity claw typically was exercisable for up to 35% of the outstanding amount of bonds, so long as 65% remained outstanding thereafter. More recently, the feature increasingly has permitted up to 40% to be prepaid, so long as 50% or sometimes 60% remains outstanding.

A second prepayment feature that has become common permits prepayment during the "noncall period" at a premium calculated at a makewhole formula, similar to the feature found in investment grade bonds. Early versions of the provision were commonly limited to voluntary prepayment upon a change of control, but it evolved to permit prepayment at the makewhole premium without restriction. The refinancing cost using the makewhole feature, while still substantial, is less prohibitive than for an investment grade bond, initially because of the shorter maturity of a high-yield bond, and later because the makewhole formula became tied to the prepayment amount payable at the first date on the call schedule rather than at maturity; this significantly reduces the makewhole premium because the amount payable at that first call date is significantly less than what would be payable at that date using a makewhole formula.

A third prepayment feature that has gained some currency is typically seen only in a secured bond context. It permits the borrower to prepay up to 10% of the outstanding amount of bonds in any 12-month period at a 3% premium, and again typically can only be exercised during the first three years of the life of the bond. The feature is based on the theory that secured bonds are incurred as a substitute for secured term loans, which as previously noted are generally prepayable without any premium, and accordingly the borrower should have some enhanced flexibility to prepay this alternative type of secured debt.

A final prepayment feature that has appeared more recently permits the borrower to prepay any bonds remaining outstanding after a tender offer has been made for the bonds in which at least 90% of the bonds have been tendered for payment, at the same price as paid in the tender offer. Thus, if, for example, the borrower has made an offer for its bonds following a change of control as required by their terms, typically at a 1% premium, and at least 90% have been tendered, the borrower can prepay the remaining bonds at the same premium.

High-Yield Bonds: Impact of a Bankruptcy. Negotiating for redemption flexibility in bonds could have unforeseen consequences when tested in court in a bankruptcy or insolvency proceeding. The United States Court of Appeals for the Third Circuit has held in the Energy Future Holdings case[5] that the repayment of notes following their automatic acceleration resulting from a voluntary bankruptcy filing requires payment of the redemption premium that would otherwise be due on a voluntary redemption. The United States Court of Appeals for the Second Circuit, to the contrary, has held in a similar situation in the Momentive case[6] that the plain meaning of "redeem" is to repay "at or before maturity", that acceleration brought about by a bankruptcy filing changes the maturity of the accelerated notes to the date of the bankruptcy petition, and therefore that any repayment made in connection with a bankruptcy filing is made post-maturity and is not subject to payment of a redemption premium. One consequence of these conflicting court decisions is that filing for bankruptcy in the Second Circuit may lead to a preferred result for an issuer compared to filing in the Third Circuit.

Other Leveraged Financing Products. Prepayment protections for alternative lending products, such as second lien term loans and mezzanine debt, can vary to a greater extent than for syndicated term loans or high-yield bonds, but generally tend to be fairly modest in comparison to high-yield bond protections. These products often can be prepaid immediately or after a short period of time at modest premiums that decline fairly quickly to zero. The relatively benign prepayment cost involved makes these products attractive to borrowers.

Prepayment and Refinancing Techniques

The preceding section, in describing prepayment protections, also summarised a number of features permitting a borrower to voluntarily prepay its debt. This section will discuss the ways in which these provisions can be used by the borrower, as well as other features of the financing agreement and approaches external to the agreement that can be deployed to prepay, reprice, extend or otherwise retire debt.

Syndicated Term Loans. Syndicated term loans typically can be voluntarily prepaid on short notice, generally three business days in the case of loans bearing interest at a rate based on LIBOR. Traditionally, that notice was irrevocable, but when lending syndicates were relatively small and made up of commercial banks, it was generally feasible and accepted practice to obtain a so-called "payoff letter" that waived the notice requirement. In addition, in the case of a complete refinancing, the requirement to mandatorily prepay the term loans with the proceeds of a debt financing not otherwise permitted could be used to effectively sidestep the notice requirement. As term loans and lending syndicates became larger and the market moved to an institutional investor base, it became increasingly important to the borrower that it have the ability to revoke its prepayment notice if some contingency did not occur, such as the closing of a refinancing or of an acquisition of or by the borrower. It is now common for term loans to allow the borrower to give prepayment notice on a conditional basis, permitting the notice to be withdrawn if a given condition does not occur.

Modern syndicated term loans commonly provide a number of other options for prepaying, repricing, extending or otherwise retiring that debt, which have generally appeared over the last decade or so. One of the earliest features to appear is a set of provisions providing a fairly elaborate mechanic for the borrower to make an offer to prepay some or all of its term loans, open to all lenders, at a stated price or range of prices, similar to a tender offer for bonds or other securities. While this feature remains common in syndicated term loans, it has fallen into disuse as other debt retirement options have developed. In particular, syndicated term loans now often allow the borrower and its affiliates to acquire loans in open market purchases from individual lenders, without the need to make a prepayment offer to all lenders. Loans acquired by the borrower are generally required to be retired, while loans acquired by an affiliate such as a private equity sponsor are generally subject to certain restrictions, such as a limit on the amount of loans the affiliate can hold and on what voting rights the affiliate can exercise. The open market purchase option is generally faster, cheaper and more efficient than resorting to the prepayment offer mechanics.

Syndicated term loans now often allow for partial or full prepayment from a permitted refinancing facility created under the same term loan agreement. This feature will often impose a number of requirements that the permitted refinancing will have to meet. Perhaps in part as a result, the feature has not proven as popular in the context of a complete refinancing as another option, the uncommitted "incremental facility" feature. This provision allows the borrower to add new term loans under the existing term loan agreement subject to a monetary limit or compliance with a leverage-based financial ratio, the calculation of which will give *pro forma* effect not only to the incurrence of the new incremental term loans but also to the prepayment of the existing term loans with the proceeds. The new term loans often will be offered first to existing term lenders, and then to new investors. Some existing lenders for internal reasons may want to exchange their existing term loan for a new term loan, rather than fund cash and then be repaid, in a so-called "cashless rollover". The cashless rollover raised complications under some older term loans, but more recent term loans often expressly allow for it. The incremental refinancing may be used simply to "reprice" the borrower's term loans – that is, to obtain a lower interest rate but make little or no other changes – or it may be used to extend the maturity of the borrower's term loans and make other changes to the agreement.[7]

A simple term loan repricing can also be done by an amendment to the term loan agreement that just changes the interest rate. While such an amendment requires all lenders to consent, term loans today typically permit the borrower to require non-consenting lenders to assign their loans to another party once a majority of lenders have consented to the amendment – the so-called "yank a bank" mechanism – which will allow the borrower to obtain the necessary consent. Similarly, syndicated term loans commonly allow for an amendment to extend the maturity of the existing term loans, instead of incurring new debt with a longer maturity to refinance the old debt. The extension amendment can be effective for only a portion of the outstanding term loans. It can also make other changes to the agreement that would otherwise be permissible with necessary lender consent, and the "yank a bank" mechanism can be deployed once a majority of lenders have consented.

The amendment approach has tended to be disfavoured by financial institutions engaged by borrowers to assist in effecting the repricing or extension, because it can make arranging and allocating the repriced or extended loans to new investors more complicated in practice than an incremental refinancing to effect the same repricing or extension. However, more recently, principally to avoid the need for a new CUSIP number and the resulting potential for increased rating agency fees, arrangers and borrowers have reverted to the "yank a bank" approach, or have adopted an approach in which a new term loan is funded to pay off non-consenting lenders, with that new loan being deemed part of the repriced or extended loan and accordingly fungible with it as part of a single term loan. In some cases, the rating agencies have waived the higher fees, facilitating the use of the incremental loan approach.

High-Yield Bonds. As discussed in the previous section, high-yield bonds give the borrower a number of options to prepay, or "redeem", the bonds at varying costs depending on when and how the prepayment is made. Traditionally, notice of prepayment had to be given at least 30 days and not more than 60 days in advance, and once given was irrevocable. The inability to revoke the notice once given meant that many transactions, such as those financing an acquisition of the borrower and the repayment of the bonds, had to be structured in other ways, often to provide instead for a tender offer for the bonds, or for a "redemption and discharge", as discussed below. In the late 1990s, our firm introduced a "conditional redemption" feature to the high-yield bond market, giving the borrower the ability to give the notice of prepayment of the bonds but subject to the satisfaction of one or more conditions. The prepayment still had to be made not less than 30 days and not more than 60 days after notice, but the borrower had the flexibility to delay the prepayment within that 30-day period to permit the specified conditions to be met. This innovation allowed the borrower to effect the prepayment with a relatively simple notice, without the cost and complexity of a tender offer. This feature has become increasingly common in the high-yield bond market, as borrowers have come to appreciate its efficiency and cost-effectiveness. It has further evolved in recent years, allowing notice to be given as little as 10 or 15 days in advance, and for the prepayment date to be extended beyond the traditional 60-day limit as needed to satisfy the specified conditions, in a manner similar to how a tender offer can be conducted. The ability to extend beyond 60 days makes it unnecessary to revoke the notice and issue a new notice, starting the clock over.

The tender offer is the traditional alternative to the voluntary "redemption", or prepayment, of high-yield bonds. Because bonds are securities, the tender offer is subject to rules governing debt tender offers under the US federal securities laws. These rules among other things require the offer to be held open for 30 days, but as a matter of interpretation allow the party making the offer to begin to accept tendered bonds for payment after 15 days, facilitating completion of the prepayment of the bonds more quickly than the 30-day minimum for a traditional voluntary prepayment discussed above. The tender offer also can be extended as necessary for any specified condition to be met, and is not subject to a set maximum limit on extensions similar to the 60-day maximum for a traditional voluntary prepayment discussed above. Holders of the bonds are not obligated to participate in the tender offer. However, the tender offer is typically coupled with a solicitation of consents to eliminate, or "strip", essentially all the restrictive covenants with majority consent, as an inducement to participate in the tender offer. Once a majority have consented, the remaining investors must either tender or be left without covenant protections, and typically a very high percentage of the bonds wind up tendered. Pricing can be set, and later adjusted if need be, to achieve sufficient market acceptance. Equal treatment may be required contractually for consent payments, but tender offers can provide for differential consideration to different series of bonds based on differing bond values. The principal drawbacks to a tender offer are that the documentation is more complex and the costs greater for a tender offer than for a voluntary prepayment, making the modern "conditional redemption" feature discussed above an attractive alternative in many cases.

High-yield bonds commonly provide two other features that can be deployed in retiring that debt. First, high-yield bonds typically provide for the "satisfaction and discharge" of the bond agreement, or "indenture", on payment in full of the bonds. Many high-yield bonds also allow satisfaction and discharge if the bonds will mature or can be "redeemed", or prepaid, within the next year: the company simply deposits funds with the bond trustee to cover all future payments due through maturity or prepayment, together with a notice of prepayment if the bonds will be prepaid prior to maturity. The discharge is then effective, and all covenant restrictions under the bonds terminate. A satisfaction and discharge can be coupled with a voluntary prepayment, or "redemption". A "redemption and discharge" is fairly straightforward, and need not involve substantial out-of-pocket costs. But it may be more expensive than a simple redemption, because the company must deposit funds for a period of time prior to the redemption occurring, potentially increasing its interest expense or other cost of capital. In addition, the contractual conditions required to be met to effect the discharge need to be carefully assessed for practical concerns; for example, a requirement that no default exist could present an obstacle to a transaction should a default come to light at the last minute. Bonds called at a makewhole premium, or bearing interest at a variable or "floating" rate, may raise calculation issues with respect to determining the amount to be deposited, if the bonds have not expressly addressed that calculation in advance.

Second, high-yield bonds typically also provide for "defeasance" of bonds, by depositing funds with the trustee to cover all future payments through maturity or redemption. Defeasance is not limited to the one-year look forward limitation applicable to the discharge option – bonds can be defeased at any time. "Legal" defeasance terminates all substantive obligations, but is typically not possible as a practical matter because a common condition to legal defeasance requires delivery of a tax opinion that cannot be given under current US federal tax law. "Covenant" defeasance only terminates specified covenants and related defaults. It may be unattractive economically, and again the contractual conditions to covenant defeasance, such as absence of default, may pose practical concerns. Bonds called at a makewhole premium, or bearing interest at a "floating" rate, again may raise calculation issues with respect to determining the amount to be deposited.[8]

Endnotes

1. Financing products use differing terminology for similar things. A company that incurs debt as a term loan is a "borrower", but is an "issuer" if it incurs debt as a bond. A company "prepays" a term loan, but "redeems", "repurchases" or "calls" a bond. Term loans are "borrowed" under a "credit agreement", while bonds are "issued" under an "indenture". For simplicity and clarity, this article will generally use the same terms regardless of which product is being discussed.
2. See, e.g., Laurent Alpert and Robert Guszecki, *Indentures and the Brokaw Act*, Harvard Law School Forum on Corporate Governance and Financial Regulation (May 2, 2016), https://corpgov.law.harvard.edu/2016/05/02/indentures-and-the-brokaw-act/0.
3. The requirement to make a change of control prepayment offer has made some inroads in the investment grade bond market, responding to investor pressure for an option to exit in the event of a leveraged acquisition or similar credit-changing event.
4. For an eight-year bond that becomes prepayable after three years at half the interest rate (known as "8 noncall 3"), a makewhole prepayment may be less expensive during the final six months of the three-year period than an equity claw prepayment.
5. *In re Energy Future Holdings Corp.*, 842 F.3d 247 (3d. Cir. 2016).
6. *In re MPM Silicones, LLC*, 874 F.3d 787 (2d Cir. 2017).
7. One constraint on the incurrence of incremental term loans is that, to the extent that existing term loans remain outstanding and the effective interest rate on the new loans exceeds that on the old loans by more than a stated differential (commonly 0.5%, or 50 basis points), a "most favored nations" or MFN provision will typically require the old loans to be repriced to that differential. The MFN provision may be subject to a so-called "sunset", and expire after a period of time. It would not in any event apply in the case of an incremental financing in which the old loans are repaid in full.
8. Under case law, an issuer cannot impose "in substance" defeasance absent a provision permitting defeasance. See *Rievman v. Burlington Northern Railroad Company*, 618 F. Supp. 592 (S.D.N.Y. 1985).

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Debevoise is a premier law firm offering clients unsurpassed expertise on a global scale. The firm has extensive experience in U.S. and international leveraged and investment grade finance, including syndicated loans, asset-based loans, high yield issuance, investment grade issuance, acquisition finance, private equity finance, structured finance, and corporate debt finance. Debevoise also represents clients in credit derivatives, fund formation, mezzanine financing, restructuring and bankruptcy, and regulatory matters. In a market where cross-border transactions are commonplace, our clients benefit from the firm's footprint and capabilities.

Clients look to us to bring a distinctively high degree of quality, intensity and creativity to resolve legal challenges effectively and cost efficiently. Our deep partner commitment, industry expertise and a strategic approach enable us to bring clear commercial judgment to every matter. In fact, Debevoise was recently named the recipient of *Chambers USA*'s 2017 "Finance Client Service Award".

Analysis and Update on the Continuing Evolution of Terms in Private Credit Transactions

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For the past seven years, The Private Credit Group at Proskauer Rose LLP has tracked deal data for private credit transactions (our "data"). The data referred to in this article reflects trends and evolving terms in over 200 private credit transactions closed by The Private Credit Group at Proskauer Rose LLP in 2017 and may not be indicative of overall market trends. Our data reflects that, as the market has become more competitive, the middle market has continued to incorporate financing terms that were once only found in large cap financings. While middle market transactions have not fully incorporated the complete slate of large cap financing terms, the increasing competition for deal origination has resulted in the selective inclusion of certain large cap financing terms, albeit with a middle market orientation. While large cap terms assume a profitable and durable business model, as deal sizes get smaller and business models less able to withstand adverse economic results, middle market lenders have reacted to the introduction of large cap terms with additional conditionality and risk mitigants. Middle market lenders' appetite for certain of these large cap financing terms differ not only based on institutional biases, but also based on the size of the borrower's consolidated EBITDA. As a result, the evolution of these large cap financing terms can be traced, in certain respects, to the size of the borrower's consolidated EBITDA, resulting in the middle market becoming further divided into the "lower middle market", "traditional middle market" and the "upper middle market". This article will analyse the continuing evolution of certain key financing terms in the private credit middle market that is being driven by the blurring of once clear boundary lines with the large cap syndicated lending market as well as discuss the related market drivers and trends influencing such terms. The analysis will provide a description of the terms, proprietary data pertaining to the usage of such terms within the traditional middle market across various industries, and future changes to such terms in light of the continuing evolution of the private credit identity and market variables.

Overview of Proskauer Rose LLP Private Credit Transactions in 2017

The top five industries represented in middle market transactions, as shown in our data, include (a) business services, (b) consumer, (c) healthcare, (d) manufacturing, and (e) software and technology. These primary industries comprise 74% of our deals in 2017. Notably, healthcare deals have increased to represent more than a quarter of all of our deals in 2017, while manufacturing deals showed the biggest decline from 19% in 2016 to 10% in 2017. First lien and second lien transactions increased for the year; whereas mezzanine loan transactions continue to decline in popularity falling to 8% of all deals in 2017 compared to 13% in 2016. Closing leverage for middle market transactions in our data remains consistent with a slight drop from 5.10× to 5.00× with 80% of deals having a closing leverage between 4.00× and 6.99× consistent with 81% of deals in 2016. Interest rates across all deal types in our data trended slightly higher in 2017 compared to each of the previous two years, however, an increase in the LIBOR benchmark rate largely accounting for the higher all-in rates in 2017. For example, 52% of our deals had pricing under 9.5% compared to 63% of our deals in 2016, and 5.7% of our deals had pricing between 8.5%–8.99% up from 4.65% of our deals in 2016 in the same interest rate bracket. With respect to commitment fees, 51% of commitment fees or OID were between 2.0%–2.5% in 2017 which is consistent with the levels for 2016. In comparison to 2016, covenant lite deals in our data remained consistent in 2017 at 13% of our deals with EBITDA greater than $50MM, however, we have seen an increase in our data of transactions where the financial covenant cushions are equal to or greater than 40%. Although financial covenants generally include total leverage ratio tests, 41% of our deals also included a fixed charge coverage ratio test which is down 8% from 2016. Of the transactions with financial covenants, 70% of them had five or more covenant step-downs and of these transactions, 80% of them had EBITDA of less than $50MM. In transactions with EBITDA greater than $50MM, only 31% of them had a cap on general non-recurring expenses as an add-back to EBITDA; whereas in transactions with EBITDA that is less than $50MM, 72% of them had a cap on general non-recurring expenses.

It is worth noting that the loosening of parameters relating to the calculation of consolidated adjusted EBITDA in deal documentation in the traditional and upper middle market, including the increased prevalence of synergy-type addbacks and larger caps (or the absence of caps) on addbacks generally, may be directly affecting closing leverage multiples and resulting in more forgiving financial covenants. Additionally, in connection with the general trend towards borrower's counsel controlling the drafting process at both the commitment stage and the definitive deal documentation stage, an increasing percentage of our traditional middle market deals in 2017 were initially drafted by borrower's counsel, and in certain circumstances the borrower also identifies the precedent credit agreement to be used in a particular transaction which may not have been a transaction in which the lender participated. Due to the time sensitivity in certain transactions during the commitment stage, the lenders may sometimes find themselves agreeing to precedent credit agreements which could result in the lender accommodating terms that are more typically found in larger transactions.

Debt Incurrence

One of the most transformative structural changes to make its appearance in the middle market is the flexibility given to borrowers to incur additional debt either within or outside the applicable loan facility.

Incremental Facilities and Incremental Equivalent Facilities

Leading the way in providing greater flexibility to borrowers is the evolution of incremental and incremental equivalent loan facilities. An incremental facility (also commonly referred to as an "accordion") allows the borrower to incur additional term loans or revolving loan commitments under the existing credit agreement within certain limitations and subject to certain conditions, without the further consent of the existing lenders. Incremental equivalent debt has the same features of an incremental facility except that the debt is incurred as a separate facility outside the existing credit documentation either pursuant to a separate credit facility or through the issuance of notes (either issued in a public offering, Rule 144A or other private placement).

The migration of these additional debt facilities into the middle market can be summarised as follows: (a) the upper middle market will generally accommodate both incremental facilities and incremental equivalent facilities; (b) the traditional middle market is increasingly accommodating both incremental facilities and incremental equivalent facilities (subject however to stricter conditions, as discussed below) but remains stratified in approach depending on the consolidated EBITDA of the borrower and the leverage of the borrower; and (c) lower middle market deals generally do not provide for incremental or incremental equivalent facilities. Our data shows that 86% of traditional middle market deals include incremental facilities with 53% including both incremental facilities and incremental equivalent facilities.

Incremental Amount

- In large cap transactions, and increasingly in the upper middle market, the existing credit facility may limit the incremental facility to both a fixed amount (known as a "starter basket" or "free and clear basket") and an unlimited amount subject to compliance with one or more leverage ratios. The fixed amount will generally be no greater than 1.0× of consolidated EBITDA and may even have a "grower" component (see discussion on Grower Baskets below). Our data shows that 37.5% of traditional middle markets deals with incremental facilities contain a starter basket for the incremental facility equal to or greater than 1.0× of consolidated EBITDA. The unlimited amount will generally be subject to compliance with a leverage ratio and depending on whether the original transaction is structured as a first lien/second lien credit facility or senior/mezzanine credit facility and what type of incremental debt is being put in place (i.e. debt *pari passu* to the first lien or senior facility, debt that is subordinate to the first lien or senior facility but *pari passu* with the second lien/mezzanine facility, or unsecured debt), the type of leverage test will be different (i.e. first lien leverage test *vs.* secured leverage test *vs*. total leverage test). In these larger deals, the level of the ratios will often be set at the closing date leverage multiple or, in the case of unsecured debt, sometimes 0.25× to 0.50× outside the closing date leverage multiple. In larger deals, there may be an alternative test for the incurrence of incrementals to the extent the proceeds of such incrementals are utilised to fund permitted acquisitions. In such instances, the incurrence leverage ratio shall be the leverage ratio of the borrower immediately prior to giving effect to such permitted acquisition. The upper middle market often follows the larger deals in terms of how the incremental amount is limited except that, originally, the leverage ratio for the incurrence of the unlimited incremental amount would sometimes be set at the closing date leverage multiple less a setback (often 0.25× of EBITDA). Our data has shown, however, that setting back the closing date leverage multiple has become rare.
- We have seen a trend in the data in the traditional middle market to allow both the starter basket and the unlimited amount, with 62% of traditional middle market deals in 2017 permitting both components of incremental facilities. In the traditional middle market, it is common for the incremental amount to be unlimited but subject not only to an incurrence leverage test but also to *pro forma* compliance with the maintenance financial covenants. In instances in the traditional middle market where the incremental amount is subject to a fixed cap amount, our data also shows that its incurrence will also often be subject to an incurrence leverage test and *pro forma* compliance with the maintenance financial covenants.

  The use of different leverage tests creates significant flexibility to the borrowers in that it allows borrowers to incur multiple layers of debt in excess of the overall total leverage test originally used as the leverage multiple. For example, in computing total leverage, the indebtedness included in such a calculation would typically include all funded indebtedness of the applicable credit parties and those subsidiaries included in the financial metrics of the credit parties. The indebtedness included in calculating first lien leverage would only be funded indebtedness subject to a first lien on the assets of the credit parties. As a result, a borrower could first incur unsecured indebtedness up to the required total leverage ratio and still incur additional first lien indebtedness even though such additional debt would bust the total leverage ratio because the test applied for the first lien leverage ratio would not include the unsecured indebtedness incurred by the borrower. This flexibility, although provided in the upper middle market, is often rejected in the traditional middle market transactions. Traditional middle market deals will usually only apply a total leverage test for all types of incremental loans.
- In large cap and upper middle market transactions, borrowers will also seek the ability to (a) elect to use the ratio based unlimited incremental amount prior to the fixed amount, (b) reclassify (at their discretion or automatically) incremental debt which was originally incurred under the fixed amount as incurred under the ratio based unlimited amount (thereby reloading the fixed amount), and (c) in instances where an incremental loan is incurred based on both the fixed amount and the unlimited amount, not take the fixed amount into account when testing leverage. In the instances where a traditional middle market financing allows for both a fixed starter basket and a ratio based unlimited incremental amount, historically the middle market lender has required that the fixed amount be used first and reclassification would generally not be permitted but that protection is beginning to erode as the reclassification concept moves down market.
- In large cap and upper middle market transactions, the incremental amount may also be increased by an amount equal to: (a) in the case of an incremental facility that effectively replaces any existing revolving commitment terminated under the "yank-a-bank" provisions, an amount equal to the portion of such terminated revolving commitments; (b) in the case of an incremental facility that serves to effectively extend the maturity of the existing facility, an amount equal to the amount of loans and/or commitments, as applicable, under the existing facility to be replaced with such incremental facility; and (c) all voluntary prepayments of the existing term loans, previously incurred incremental term loans and refinancings of the existing term loans and voluntary commitment reductions of the revolving facilities (except to the extent funded with the proceeds from an incurrence of long-term indebtedness (other

than revolving indebtedness)). The incremental amount limitations will be the same for incremental equivalent facilities provided that the establishment of an incremental facility or the incurrence of incremental equivalent debt will result in a dollar for dollar reduction of the amount of indebtedness that may be incurred in the other facility. In this regard, the upper middle market is generally consistent with the larger deals. However, the traditional middle market will again differ in that if any additional amounts increase the incremental amount, it will be limited to the voluntary prepayments of indebtedness or commitment reductions of the revolving facilities.

Rate and maturity

- Generally, incremental term loans: (a) cannot have a final maturity date earlier than the existing term loan maturity date; (b) cannot have a weighted average life to maturity shorter than the weighted average life to maturity of the existing term loans; (c) rank *pari passu* with the existing loans or junior in right of payment and/or security or are unsecured; (d) are not secured by any additional collateral or guaranteed by any additional guarantors than collateral securing or guarantors guaranteeing the existing term loans; (e) participate *pro rata* or less than (but not greater than) *pro rata* with the existing term loans in mandatory prepayments; (f) have covenants and events of default substantially similar to, or no more favourable to the lenders providing such incremental term loans than those applicable to the existing term loans, except to the extent such terms apply only after the latest maturity date of the existing term loans or (sometimes) if the loan agreement is amended to add or conform to the more favourable terms for the benefit of the existing term lenders; and (g) if incremental equivalent debt is permitted, such incremental equivalent debt is subject to customary and satisfactory intercreditor arrangements. Some borrowers in larger deals have been successful in negotiating a carve-out from the maturity requirement which would allow the borrower to incur incremental term loans with earlier maturities, up to a maximum amount governed by a fixed dollar basket.

  These terms have generally been adopted in the upper middle market. The traditional middle market does not contain significant variations with an exception, as the traditional middle market sometimes allows only the incurrence of incremental debt that is *pari passu* debt. Although it seems that allowing the borrower to incur either lien subordinated or unsecured subordinated debt instead of *pari passu* debt would be beneficial to the lenders, the traditional middle market's resistance to allowing different types of debt stems from a desire to maintain a simpler capital structure especially in credit transactions where there are no other financings.

- The interest rate provisions applicable to incremental facilities customarily provide some form of pricing protection that ensures that the all-in yield of the existing credit facility would be increased to match (less 50 basis points) any new incremental facility whose all-in yield was greater than 50 basis points above the existing credit facility. These provisions are generally referred to as the "MFN (most favoured nations) provisions". In large cap and upper middle market transactions, the MFN provision is often no longer applicable after a period of 12 months to 18 months (some with sunset periods as short as six months). The sunset provision, however, may be eliminated altogether or flexed out, depending on market conditions. As the ability to designate incrementals with different payment and lien priorities (or as incremental equivalent debt) has become commonplace in large cap and upper middle market transactions, borrowers have been soliciting additional accommodations that have the effect of further eroding the MFN provisions, including (i) additional carveouts to the calculation of all-in yield for amounts that do not clearly constitute "one-time" fees (for example, OID and upfront fees), thereby making it easier to remain below the MFN trigger threshold, (ii) applying the MFN provisions only to incrementals (or incremental equivalent debt) that is *pari passu* in claim and lien priority to the existing credit facility, (iii) limiting the application of the MFN protection to the term loan facility originally issued under the credit facility and (iv) excluding from the MFN provisions incrementals (or incremental equivalent debt) that (A) are incurred in reliance on the started basket amount, (B) are utilised for specific purposes (e.g., for permitted acquisitions), (C) are structured as an issuance of notes (whether issued in a public offering, Rule 144A or other private placement) as opposed to loans, and (D) mature later than the latest maturity debt of any other term loans under the credit facility or which are bridge-financings. Without adding further protections, allowing the incurrence of an incremental loan based upon the starter basket amount to be free of the MFN protection has the potential of eliminating the MFN treatment altogether in deals where the borrower has the ability to redesignate starter amount incrementals as leveraged based incrementals because the borrowers are able to, in certain circumstances, reload the starter basket amount. Our data shows that 3% of traditional middle market deals with MFN provisions include a sunset period, which is consistent with the deals in 2016.

  The traditional middle market takes a somewhat consistent approach to the upper middle market's treatment of the MFN provision. For the most part, *pari passu* debt issued in reliance upon the incremental provisions is subject to the MFN provisions. However, middle market lenders may also require that the impact of the MFN provisions apply to all debt outstanding under the credit facility, including incremental loans previously funded. Traditional middle market lenders in single-lender or club deals have had some success maintaining the MFN provisions without a sunset with exceptions generally limited to first lien transactions and senior stretch transactions where the credit is intended to be syndicated.

Use of proceeds

- In large cap and upper middle market transactions, proceeds from the incurrence of incremental and incremental equivalent debt may generally be used for any purpose not otherwise prohibited by the original credit facility. In contrast, the traditional middle market restricts the use of proceeds to very specific purposes such as acquisitions or capital expenditures. Our data shows a clear migration of the large cap and upper middle market flexibility with respect to the use of incremental proceeds filtering down to the traditional middle market. Increasingly, middle market lenders are, in some deals, permitting incremental proceeds to be used for general purposes, including for restricted payments such as dividends and payment of junior debt but subject to stricter leverage tests.

Ratio Debt

In addition to the incremental and incremental equivalent facilities described above, large cap and upper middle market transactions often include additional debt incurrence capacity through the inclusion of so called "ratio debt" provisions, provisions that can be traced back to the high-yield bond market. Ratio debt allows the borrower to incur additional indebtedness so long as the borrower meets the applicable leverage or interest coverage ratio test, if based on leverage, typically set at the same level required for incurrence of incremental and incremental equivalent debt. In upper middle market transactions that include "ratio debt" provisions, the conditions for incurrence (other than the applicable leverage or interest coverage test) may differ from the conditions to incurrence of incremental and incremental equivalent debt, though lenders have had some success in standardising the conditions across the different types of permitted debt incurrence. To the extent ratio debt provisions appear in traditional middle market transactions, the incurrence of such debt is often conditioned on such debt being subordinated in right of payment to the credit facility (and is not otherwise permitted to be secured). Additionally, where the traditional middle market allows for ratio debt, it requires that any applicable MFN provisions be applied to any ratio debt that is *pari passu* to the credit facility obligations. Notably, this middle market term has migrated up market as upper middle market deals have increasingly adopted this protection in respect to ratio debt. Lower middle market transactions generally do not provide for ratio debt. Our data shows that 48% of traditional middle market deals permitted ratio debt.

Acquisition Indebtedness

Generally, credit agreements will allow the borrower to incur certain indebtedness in connection with a permitted acquisition or investment. Not surprisingly, the larger deals will commonly allow the borrowers the most flexible formulation and permit the incurrence of any acquisition indebtedness to the extent such indebtedness was not incurred in contemplation of such acquisition or investment and is only the obligation of the entity or its subsidiaries that are acquired. The upper middle market takes a similar approach to the large cap market but will sometimes place certain restrictions by providing that after giving effect to the acquisition indebtedness, the borrower must be in pro forma compliance with the financial covenants and/or meet a leverage test (i.e. closing date leverage). Although it is not uncommon for this type of indebtedness to be permitted in the lower middle market, it will be subject to additional limitations, including required subordination terms and dollar caps.

Limited Condition Transactions

One of the best known outcomes of the loosened credit markets in 2005 was the "certain funds provision" technology proposed by sellers who gave preference to those potential buyers who had financing locked down. Certain funds provisions (also commonly known as the SunGard provisions) provided that, except as expressly set forth in a conditions annex, there could be no conditions precedent in the definitive loan documentation to the close and funding of the credit facility, and it limited the representations required to be true at closing to material representations set forth in the acquisition agreement and a narrow set of additional "specified representations". It also limited the actions required to be taken by the borrower pre-closing to perfect security interests in the collateral. These limits were designed to assure buyers and sellers that so long as the conditions to closing under the acquisition agreement were met, the lenders would not have an additional "out" beyond the narrow set of conditions in the conditions annex.

Acquisition financings in general, regardless of the market, have generally adopted the SunGard provisions which require that the only representations at closing that are conditions to funding are specified representations and the representations set forth in the acquisition agreement. All other representations and warranties in the credit agreement are made at closing, but are not conditions to close, so even if such representations and warranties are not true, the lender will still be required to close the financing with a default immediately following the closing. In most highly competitive deals, the borrower will seek to limit the representations and warranties made only to the specified representations and the acquisition agreement representations so that even if the other representations are not true, the borrower will not have a default post-closing. The upper middle market has generally followed the larger deals in this respect but not without objection especially in first lien and second lien financing transactions where the second lien lenders will not benefit from a regular bring down of the representations through advances made under a revolver. The traditional middle market, for the most part, continues to resist the requirement that only specified representations and acquisition agreement representations should be made at close.

As borrowers continued to push for greater flexibility in credit documents, the certain funds provisions continued to evolve, widening its applicability to include future acquisitions (and in larger deals, paydown of indebtedness that requires irrevocable advance notice) contemplated by the borrower financed from the proceeds of incremental loan facilities or "ratio debt". Through the broader applicability of the certain funds provisions, the limited condition acquisition provisions were developed where borrowers have limited conditionality for incremental debt incurred primarily to finance an acquisition, thereby diminishing financing risk for follow-on acquisitions. In larger deals, borrowers have been successful in extending this "limited condition acquisition" protection to all acquisitions using an incremental facility, regardless of whether there is a financing condition in the underlying acquisition documentation.

Customarily, as noted above, conditions to incremental debt and "ratio debt" incurrence have included material accuracy of representations and warranties, absence of default or event of default, and in certain areas of the market, either a *pro forma* compliance with the existing financial covenant (if any) or meeting a specific leverage test, each tested at the time of incurrence of the incremental debt. The limited condition acquisition provisions debuted in the larger deals enabling the borrower to elect the effective date of the acquisition agreement ("acquisition agreement test date") as the relevant date for meeting the required conditions. As a result, if the borrower made such an election then the combined conditions to accessing the incremental loans and making a permitted acquisition (which may have included accuracy of representations and warranties, no events of default, and leverage tests) would be tested at the time the acquisition agreement is executed and the borrower would have the ability to include the financial metrics of the target entity (i.e. EBITDA) at the time of such testing. Although the traditional middle market has largely incorporated the limited condition acquisition protections, some lenders have required the relevant acquisition to close within a specified time frame from execution of the purchase agreement (usually not longer than 120 days) otherwise, the limited condition acquisition protections fall away. As a result, in the event the acquisition does not close within the agreed upon time frame, the limited conditionality is eliminated and the borrower would have to comply with all the conditions at the time of the incurrence of the incremental loan. The lower middle market has generally not incorporated the limited condition acquisition provisions.

The limited conditionality provision permits a borrower to elect the effective date of the acquisition agreement (instead of the closing date) as the date of determination for purposes of calculating leverage ratios in order to test ratio-based incremental debt capacity. Testing of the leverage ratio at signing eliminates the risk of a decline in EBITDA of the borrower and the target between signing and closing (the period between execution of the acquisition agreement and closing date referred to as the "Intervening Period"), when the ratio otherwise would be tested. This risk is of special concern in deals involving a lengthy delay between signing and closing due to regulatory approvals.

As the leverage test is intended to include the financials of the acquisition target on a *pro forma* basis, borrowers have further requested that any other incurrence based leverage test (required in connection with any other investment, incurrence of debt, restricted payment, etc.) that is tested during the Intervening Period include the financials of the acquisition target on a *pro forma* basis. Generally, the markets have responded to this request in three different ways:

- *Most Borrower Favorable*: In large deals, any leverage test required during the Intervening Period will be tested after giving *pro forma* effect to the acquisition. In the event the acquisition does not close, any leverage test applied during the Intervening Period will be deemed to be valid regardless of whether the borrower would have failed to meet the leverage test without giving effect to the acquisition target's EBITDA. The upper middle market has not yet fully embraced this calculation of the leverage test, although we are seeing this construct more frequently.
- *Most Lender Favorable*: Any leverage test required during the Intervening Period will be tested on a stand-alone basis. The traditional middle market and the upper middle market (but less frequently) will generally take this approach.
- *Compromise*: The maintenance financial covenant and any incurrence leverage test pertaining to the payment of restricted payments are tested on a stand-alone basis but the remaining incurrence leverage tests are tested giving *pro forma* effect to the acquisition. Another compromise is to test all maintenance financial covenants and incurrence leverage tests on both a *pro forma* and stand-alone basis. This application of the leverage test is often seen in the upper middle market.

Available Basket Amount

Once the leveraged financing markets revived following the down turn of the financial markets in 2009, the concept of builder baskets or the "available basket amount" seen in high-yield bond deals migrated into, and became prevalent in, the middle market. It is worth noting, however, that the lower middle market has not fully embraced the inclusion of available basket amounts. An available basket amount is also commonly referred to as a "cumulative amount" or a "builder basket". The purpose of an available basket amount is to give the borrower the ability to increase certain baskets in the negative covenants (i.e. investments, dividends and payment of junior indebtedness) without asking for a consent from the lender. The rationale behind lenders conceding to an increase in certain baskets in the negative covenants was an attempt to recognise and reward an increase in the borrower's profitability by permitting the borrower to not only deleverage its debt, but also to permit the borrower the ability to increase baskets in the negative covenants that generally restrict cash outflow. Our data shows that 81% of traditional middle market deals include the available basket amount concept.

The available basket amount will be generally constructed to be the sum of the following:

- *Starter Basket Amount*: a starting amount (commonly referred to as a "starter basket amount") which, unlike the incremental starter amount, is not necessarily based on a percentage of the borrower's EBITDA but is, instead, generally determined on a case-by-case basis (which amount may be further increased by a grower basket in the larger deals). Upper middle market deals and traditional middle market transactions (but less frequently) will often include a starter basket amount. A frequent compromise position we see in the traditional middle market is to allow for the available basket amount but eliminate the starter basket amount or set it at a *de minimis* amount so that the borrower has to show revenue growth (or receive an equity contribution) prior to any permitted use of the available basket amount. Our data shows that 94% of traditional middle market deals with the available basket amount include a starter basket amount.
- *Retained Excess Cash Flow or a Percentage of Consolidated Net Income*: typically in larger deals, the available basket amount will include a percentage of consolidated net income over the retained excess cash flow because the borrower will have quicker access to the consolidated net income especially in those transactions that close in the first half of a fiscal year since the borrower will not be able to build retained excess cash flow until the end of the following fiscal year. Upper middle market transactions will often use either retained excess cash flow or a percentage of consolidated net income. In contrast, the traditional middle market deals will more often include retained excess cash flow which, in addition to having limited accessibility, will most likely be defined in a manner that results in as little actual excess cash flow as possible since the borrower will be required to make a mandatory prepayment in an amount equal to a percentage of such excess cash flow. As a result, the borrower is incentivised to minimise the amount of excess cash flow generated.
- *Contributed Equity*: if the available basket amount is included in the financing, then having it increased by the amount of equity contributions will be common regardless of the size of the deal. It is also commonly accepted that equity contributions made in connection with equity cures will be excluded from the available basket amount.
- *ROI on Investments Made With the Available Basket Amount*: larger deals and upper middle market deals will commonly increase the available basket amount by the amount of returns in cash, cash equivalents (including dividends, interest, distributions, returns of principal, profits on sale, repayments, income and similar amounts) or investments. However, not all traditional middle market deals will include returns in cash, cash equivalents or investments in the available basket amount. If included, they will only be permitted to the extent such investments were initially made using the available basket amount and in an amount not to exceed the original investment.
- *Declined Proceeds*: declined proceeds from mandatory prepayments required to be made by the borrower will commonly be included in the calculation of the available basket amount regardless of the size of the deal.
- *Debt Exchanged for Equity*: in larger deals, to the extent that any debt owed by the borrower is converted into equity, such amount will be included in the available basket amount. The upper middle market will often adopt this formulation while the traditional middle market has not fully accepted the addition of debt exchanged for equity in the calculation of the available basket amount.
- *Redesignation or Sale of Unrestricted Subsidiaries*: in larger deals and often in the upper middle market transactions, in the event an unrestricted subsidiary is (i) redesignated as a restricted subsidiary, or (ii) the subject to of a disposition, the fair market value (generally determined in good faith by the borrower) of the investments in such unrestricted subsidiary at the time of such redesignation (in the case of clause (i)) or the net proceeds of such sale actually received by a restricted subsidiary or the borrower in excess of the original investment in such unrestricted subsidiary (in the case of clause (ii)), will increase the available basket amount. The traditional middle market has not fully accepted this component of the available basket amount.

The conditions around the usage of the available basket amount vary greatly and the traditional middle market takes a very different approach than the upper middle market. As noted, the purpose of the available basket amount was to increase the baskets pertaining to cash leakage such as investments, dividends and junior debt payments. The upper middle market deals often place few conditions around the usage of the available basket amount. Such conditions may be further distinguished as follows. In most upper middle market transactions conditions for accessing the available basket amount will usually apply in respect to a dividend or junior debt payment and such conditions may include no payment or bankruptcy events of default as well as a specific leverage test set within the closing date leverage level (by 0.50× to 1.0×). In some cases, the specific leverage test will apply only to the extent the component of the available basket amount being accessed pertains to retained excess cash flow or a percentage of consolidated net income. In the more conservative upper middle transactions and the traditional middle market deals, the approach will be to place conditions for the usage of the available basket amount for all investments, dividends and junior debt payments irrespective of which component of the available basket amount is being accessed. For the most part, these conditions may include a *pro forma* leverage ratio test as well as a no events of default condition. In the traditional middle market, it is also not uncommon for the available basket amount permitted to be used to be subject to an additional capped amount. Additionally, in respect to the payment of dividends or junior debt, there will be an additional leverage ratio test that will be well within the closing date leverage (by as much as 1.0× to 2.0×).

Grower Baskets

Akin to the available basket amount, the "grower basket" is intended to provide the borrower with the flexibility of automatically increasing certain basket amounts based on the growth of the borrower's EBITDA or total assets. While the upper middle market and, to a lesser extent, the traditional middle market have generally adopted the grower basket provisions (in certain circumstances, excluding baskets related to restricted payments and junior debt payments), the lower middle market has generally not accommodated the inclusion of grower baskets or the available basket amounts. Our data shows that 63% of traditional middle market deals include grower baskets in some form.

Grower baskets are intended to be utilised at any time a hard capped amount is implemented by formulating it as being the greater of a capped amount and a percentage of either the total assets or EBITDA of the borrower. As such, grower baskets will be used in connection with the free and clear amount in incremental debt provisions, the starter basket amount in the computation of an available basket amount and other amounts set out as exceptions to negative covenants. In the upper middle market and traditional middle markets certain transactions have incorporated exclusions with respect to baskets relating to restricted payments and junior debt payments from the grower basket concept, while still providing flexibility on baskets that are deemed to be accretive to the underlying business.

Unlike the available basket amount, which represents an additional level of flexibility within the investments and restricted payment covenants by providing for an additional performance-based covenant exception, a grower basket is the addition of a growth component based on a percentage of EBITDA or total assets that corresponds to the growth of company. Utilisation of the grower basket will not be subject to any conditions such as there being no events of default or a leverage ratio test unless the exception for which the hard capped amount relates originally included any such condition.

Choosing between EBITDA or total assets is not exclusively beneficial to either the lender or the borrower. While EBITDA is better to measure the performance of companies that are not asset rich but are instead cash flow-centric, the downsides are that it can be volatile and, depending on the industry, very cyclical. Total assets, on the other hand, are better suited for companies that are asset rich. However, the downside is that there may be certain assets that are difficult to value such as intellectual property and goodwill.

Unlike the available amount basket, which will uniformly build with a percentage of consolidated net income or retained excess cash flow, there is no established rate by which particular grower baskets are set. Instead, the parties will negotiate the hard-capped amount and set the percentage of either the closing date EBITDA or total assets to the equivalent hard-capped amount.

Unlike the calculation of the available basket amount which once increased would only decrease to the extent utilised, because grower baskets are formulated based on a "greater of" concept, if the growth component fluctuates in size, the quantum of the basket will also fluctuate (but limited down to the hard capped amount). Note, however, that since grower baskets are generally included in incurrence based exceptions utilisation, if a grower reduces in size, any prior usage of the basket at the higher level will not trigger an event of default.

Looking Ahead

With each passing year, The Private Credit Group data has shown that the terms relating to debt incurrence, limited condition transactions, available basket amounts and grower baskets as adopted in the middle market have continuously evolved as lenders adapt to the inclusion of what were once considered large cap terms. Constantly evolving markets, the entrance of new capital and institutions into the middle market, the economy and access to debt markets should, in certain instances, impact the continued migration of large cap terms into middle market transactions. However, as a particular new concept or provision is adopted in the middle market, the middle market lenders' ability to unwind such change is, for the most part, limited. As noted above, the growing use by borrowers and middle market lenders of credit documents for a prior transactions or a precedent selected by the borrower as the basis for the documentation of a new transaction should continue to solidify certain new concepts and provisions. Larger changes in the market will most likely still impact the dividing lines of where these issues fall in either the lower middle market, traditional middle market or upper middle market.

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Proskauer

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The Private Credit Group is a unique middle market finance practice. The breadth and diversity of our practice is unmatched in the industry. The group was the first to dedicate its practice solely to representing providers of private credit. We represent over 50 clients, including private debt funds, business development companies, asset managers, finance companies and family offices. These lenders provide financings for transactions ranging from $10 million to more than $1 billion across a myriad of product types and industries.

Know Your Client: Adopting a Holistic Approach to Law Firm Representation


Kelli Keenan


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Introduction

In an ever-competitive landscape for the provision of external legal services to financial institutions, in-house counsel departments are constantly seeking to reduce external legal costs through a variety of methods, while retaining competent and effective counsel. Some institutions look to "in-source" certain types of legal work while others may seek to reduce costs by limiting the number of approved law firms (and thereby channelling a larger volume of legal work to fewer firms to justify volume discounts) or negotiating for fixed or flat rates on certain matters with panel law firms, and some institutions may employ a combination of these tactics.

In this environment, it is of paramount importance that law firms continually and consistently deliver excellence and forge stronger partnerships with their clients. For law firms, doing so effectively hinges on a profound knowledge of a client's business, legal and regulatory challenges and institutional sensitivities. In the context of complex cross-border financing transactions, a law firm's understanding of the objectives of, and challenges faced by, each participating financial institution, whether in the capacity of an underwriter, arranger, syndication agent, administrative agent or lender in the credit facility, can provide such firm with an opportunity to demonstrate its capabilities beyond that of merely competent deal counsel. A law firm's ability to step back from the transaction documentation and identify potential legal or regulatory issues posed by a particular transaction or impacting a particular client or client group within the transaction may resonate with more lasting effect on clients than simply getting the deal done in a timely manner.

Undoubtedly, the importance of developing close partnerships with clients and having a strong and current understanding of a client as noted herein is imperative for law firms in today's lending environment. Today, many financial institutions are evaluating cross-border lending and entering into cross-border lending transactions, some for the first time. Cross-border lending transactions have significantly increased over the years as companies have become more global and so have their financing needs. With the increase of cross-border lending, it has become a very exciting time to be both in-house counsel and external counsel working on complex cross-border loans. With such excitement, however, comes a number of unique legal issues and challenges for a financial institution and its counsel that go beyond the applicable governing law of the deal documentation.

What Are Some Considerations for Law Firms Looking to Increase Their Knowledge and Understanding of Their Clients' Businesses?

To be an effective external legal advisor, a law firm must first gain a client's trust. This can occur by knowing the client and the client's businesses remarkably well. In particular, a deep understanding of a client's legal structure, operational capabilities, industry footprint and business objectives is likely to pay dividends to a legal service provider. Learning about an organisation from a law firm's associate who is on secondment with a particular client, frequent communication with individuals responsible for key functions throughout an organisation and staying abreast of the deal market generally (with particular attention given to which financial institutions are leading or participating in which deals) are some ways that law firms may gain this intimate familiarity with their financial institution clients. For these external lawyers, for instance, knowledge about whether a multinational financial institution is organised as one bank with various branch offices (and, therefore, operates on a single balance sheet) or a confederation of distinct banks is a critical piece of knowledge that will allow the law firm to identify applicable legal and regulatory challenges facing its client and to provide advice on how best to overcome or structure around those hurdles. As an example, a global financial enterprise that is capable of lending on multiple balance sheets may choose to book large loan underwrites on various balance sheets to comply with regulatory lending limits or it may choose to use a specific balance sheet to comply with licensing requirements under local law. Law firms that are sensitive to and aware of these points can be particularly helpful to clients seeking advice on structuring a financing early in the deal's lifecycle.

Moreover, knowledge about a client's internal legal risk management process can be invaluable. Some financial institutions may lack full-time legal staff who have the relevant product expertise to provide comprehensive advice to banking teams on specific transactions. In such cases, external deal counsel can add meaningful value to the financial institution client's risk management by helping to identify legal and regulatory issues and involving internal counsel on the matter as soon as possible.

Furthermore, understanding a bank's industry position, recent deal history and growth strategy can enable law firms to provide targeted and effective advice to clients. Full-service, multinational law firms that represent various financial institutions often have a client-base that originates and executes transactions in a wide variety of industry sectors or regions. Accordingly, these law firms are ideally situated to provide meaningful advice to banks looking to break-in to a certain geographic area, make headway with new and existing clients, grow a product platform or become a bigger player in a given industry sector. Financial institutions, in such case, can benefit immensely from the prior deal experience of the law firm with knowledge and expertise on topics such as (i) relevant legal or regulatory risks or regulatory restrictions or limitations associated with lending to a specific borrower, (ii) taking security located in a specific country, (iii) how to effectively allocate legal and credit risk during negotiations with a client with whom the financial institution has little previous experience, and (iv) an understanding of unique deal or market terms associated with a borrower of a certain size or which operates in a specific industry that may assist the financial institution to get a better result for its client when syndicating the deal. The ultimate goal of the bank is, after all, to provide the best service possible to the borrower while protecting itself and ultimately getting the loan paid back. These themes are often the subject of law firm teach-ins for bank clients and a law firm that is attentive to such topics can be successful in integrating itself in both a client's business strategy and legal risk management framework. Both are extremely important. Garnering the support from a financial institution client's business people and its in-house counsel alike can give a law firm a marked advantage in a financial institution's deal counsel selection process.

What Are Some Ways External Counsel Can Establish Itself as a Value-Add Advisor to Financial Institution Clients?

In cross-border lending transactions, the governing law of the credit agreement is important for a number of reasons, including for a financial institution to determine and engage from its approved list of law firms the most appropriate, knowledgeable counsel in the relevant governing law jurisdiction. A financial institution will rely on external counsel with solid experience and knowledge in the relevant jurisdiction to ensure that the loan agreement is valid and enforceable. From a governing law perspective, a financial institution and its in-house counsel will expect the firm to raise and address material legal risks relating to such governing law and how to enforce an agreement governed by that law. With that said, it is the ability to provide more than legal counselling on the governing law that consistently distinguishes a law firm in the eyes of the financial institution and its in-house counsel. High-quality external counsel does not just advise on general governing law issues and risks. Genuine value is provided when international and local external counsel (i) directly work with its client and, as appropriate, the in-house legal team to structure and vet the transaction from a client's perspective with a strong understanding of the client's internal and external legal and regulatory environments, and (ii) advise on potential future risks, such as political risk, or legal reforms in the relevant jurisdiction(s) that may impact the credit facility or its client's ability to enforce or get repaid. These issues cannot be examined simply with respect to the loan's governing law jurisdiction; rather, all jurisdictions that touch on the parties involved can have an impact during the term of the credit facility. Proactive external counsel can quickly become an invaluable asset to a financial institution when entering into cross-border lending transactions.

Accordingly, external counsel should take a more holistic view of the transaction and its client, analysing potential risks to a client under the laws and regulations applicable to the specific client and to the specific transaction. Active engagement and discussion with in-house counsel, including a client's regulatory attorneys, on a regular basis is an effective and productive way to learn of, understand and appreciate a specific financial institution's regulatory and legal concerns, which more often than not go beyond the governing law of a loan agreement.

What Are Some Examples of How External Counsel Can Advise its Financial Institution Clients Beyond a Transaction's Governing Law?

In today's market, we have seen a number of US lenders become comfortable entering into cross-border lending transactions governed by English law. Approved law firm lists at US financial institutions typically include a number of high-quality English law firms capable of offering competent counsel from an English law perspective. In such an environment, what may, but must not, be overlooked in a lending transaction in which a firm is representing a US lender is an analysis of non-English laws or regulations of other jurisdictions applicable or of sensitivity to such US lender.

For example, Regulation W, which implements Sections 23A and 23B of the Federal Reserve Act, restricts the amount of transactions that a US bank has with its affiliates and the terms on which those transactions are conducted. Regulation W is a regulatory concern for US banks and US banks must ensure Regulation W compliance. In the cross-border lending context with US lenders, the governing law of the underlying loan agreement does not determine the applicability of Regulation W. If a financial institution in a cross-border loan is a US bank, then Regulation W may be applicable depending on the transaction and whether and to what extent such US bank's affiliate is involved in the transaction, without regard to the credit facility's governing law.

A similar example is the margin regulations in the United States. Regulation U, 12 C.F.R. § 22.1 *et seq*., is a US regulation applicable to US banks and US non-broker-dealer lenders with the general purpose of limiting the amount of credit, including loans, that can be extended to buy or carry publicly-traded equity securities and certain other securities when such securities are also the collateral securing the credit. In the context of lending, Regulation U (subject to certain specific exemptions) imposes certain requirements on US banks and non-broker-dealer lenders making such credit extensions and further prohibits such banks and lenders from making a loan so a borrower can buy or carry margin stock if the loan is directly or indirectly secured by margin stock in an amount exceeding the maximum loan value of the collateral securing the loan. Margin stock includes, with specific limited exceptions, any equity security trading on a US national securities exchange, an over-the-counter security trading in the national market system, warrants and debt convertible into publicly-traded equity securities. It is worth noting that foreign equity securities traded in the US through American Depositary Shares that are listed on a national securities exchange also constitute margin stock under Regulation U. Despite the potential significant consequences such as regulatory enforcement and criminal liability for non-compliance with Regulation U, margin lending risks are often not foremost concerns of external counsel when representing a US lender, especially in a cross-border lending context.

An additional example of a regulatory matter impacting US and non-US banks alike is the possibility of triggering local law licensing requirements when lending to a borrower located or organised in certain jurisdictions. Specifically, for example, countries like France and Japan have strict requirements (subject to limited exemptions) that financial institutions must be licensed in such country or, as with France, duly passported under the European Passport Directive, to lend to a borrower located in, or organised under, the laws of such country. A violation of these licensing requirements could result in potential criminal liability and significant regulatory fines for financial institutions. Therefore, the need for financial institutions to be aware of and correctly address these requirements and this risk is imperative. External counsel questioning and diligencing whether there are applicable local law licensing or authority issues or restrictions early on in a transaction can save its client time, expense and potential legal and reputational issues later on.

Of course, in-house counsel at US banks can issue spot Regulation W, margin lending concerns, potential licensing requirements and other similar legal and regulatory risks as these are regulatory matters of significance to many financial institutions, and the potential penalties for non-compliance are at the forefront for such financial institutions. In-house counsel involvement in transactions, however, varies based on a number of factors, including the specific deal and its complexity, in-house work volume, priorities and the institution's legal coverage model. Though it is perhaps unfair to expect primary external deal counsel to have a working knowledge of all laws and regulations applicable to every member of the loan syndicate, such counsel should, at a minimum, be sensitive to the fact that, in addition to the governing law of the transaction, other material laws and regulations likely apply to its client. It is therefore essential for a law firm to understand its client's legal, regulatory and compliance sensitivities, and know when and how to escalate to the client and its in-house counsel. When external counsel is representing a financial institution on cross-border transactions, proactively issue spotting potential legal and regulatory risks beyond the governing law and escalating them to its client will distinguish a firm from the many sophisticated deal closers in the legal world.

Similarly, in the context of sanctions and anti-bribery and corruption, external counsel can deliver a valuable impact in cross-border financings by investing the time to learn a client's sanctions and anti-bribery and corruption requirements and concerns and ensuring those are implemented and addressed in the loan documents. Going even a step further and counselling a client on the potential sanctions and anti-bribery risks posed in the borrower's jurisdiction and where the borrower does business is a way for a law firm to provide critical legal support and to become a real partner with its client in mitigating risk. External counsel is pivotal in ensuring the loan documents adequately protect a financial institution from sanctions and anti-bribery and corruption risks in all relevant jurisdictions and that the documentation includes representations and covenants aligned with the client's sanctions and anti-bribery and corruption requirements.

What Are Some Additional Considerations for a Law Firm Seeking to Benefit its Clients Beyond Identifying Legal Risks or Providing Deal-Specific Advice in the Cross-Border Lending Context?

Clients will invariably appreciate external counsel raising time and expense concerns during the early stages of evaluating a potential deal. In US lending transactions, for example, most secured loans are secured by all or substantially all of the assets of a borrower. This gives a lender comfort from a credit risk perspective and in the US it is reasonably easy and generally inexpensive for a lender to obtain and perfect its security interest. We know this is not the case in all jurisdictions. In some jurisdictions, the perfection of a security interest is administratively burdensome and very costly. In other jurisdictions, the legal system or the court system make enforceability or collectability on the pledged assets significantly challenging. External counsel who raises to a client such practical and cost considerations and who can assist a client in analysing the value of the collateral compared to the time, cost and potential risks and limitations on enforcement and collectability is a vital resource in cross-border transactions. External counsel discussing these matters with its client very early in the evaluation of a cross-border transaction allows the client to effectively evaluate and structure a transaction with a full appreciation of costs and potential limitations.

Closing Thoughts

It is undoubtedly a competitive landscape for financial institutions and legal service providers alike. As financial institutions seek to navigate this competitive landscape and be more prevalent in new and different markets and geographic territories, they face increased business, regulatory and legal challenges. With the demands on financial institutions lending into such new markets and countries being ever greater, so too are the expectations of their external law firms representing them on cross-border financings. Such environment presents significant opportunities for law firms acting as deal counsel to also serve as a trusted advisor to the financial institutions they represent. Surely this can help a law firm develop deeper relationships with its clients and win future mandates.

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Law of Astana International Financial Centre: Key Considerations

Colby Jenkins

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I. Introduction[1]

Kazakhstan has sought to position itself as the "Dubai of Central Asia" since the advent of the so-called "Dubai model" over a decade ago, with its capital Astana figuring as a global financial hub connecting Western Europe with Eastern Asia and serving as a gateway to China.

In May 2015, President Nursultan Nazarbayev issued a decree pursuant to the "100 Concrete Steps Plan" (a national development plan intended to achieve the country's admission to the top 30 developed countries by 2050) that established the Astana International Financial Centre (the "AIFC") free economic zone for the purposes of cultivating foreign direct investment, developing the local capital markets and facilitating their integration into the international markets, and developing the local banking, insurance, and Islamic financing sectors.

The AIFC has entered into cooperation agreements with Visa, NASDAQ, and the Shanghai Stock Exchange in order to deploy state-of-the-art technology infrastructure that enables capital market, asset management, private banking, green finance, Islamic finance, and FinTech transactions. The AIFC will have its own stock exchange, which is intended to serve as the privatisation platform for state-owned enterprises held by the Kazakh sovereign wealth fund, Samruk Kazyna, and the national holding company, Baiterek, with auctioned companies including Kazakhstan's national oil & gas company (KazMunaiGas), national energy company (Samruk-Energo), national atomic energy company (Kazatomprom), national railroad company (Kazakhstan Temir Zholy), and national postal company (KazPost).

The AIFC is intended to serve as a gateway to the Eurasian Economic Union (comprised of Armenia, Belarus, Kazakhstan, Kyrgyzstan, and Russia), as well as the first port of call for China's "Belt and Road Initiative" (the "BRI"), a multi-trillion dollar development project which aims to integrate the infrastructure and economies of Eurasia. Foreign investment appetite for local assets has been substantially whetted by the fact that Kazakhstan lies directly in the BRI's geographic scope and investment mandate, with the country positioned as a major beneficiary of, and transportation hub for, inbound and outbound Chinese commerce.

The Kazakh government and the National Bank of Kazakhstan have jointly adopted a development strategy for the AIFC which initially attracts the financial and technological expertise necessary to support the later phases of positioning the AIFC as a regional, and then an international, financial centre of choice by 2021.

The AIFC is located in the premises constructed for the EXPO-2017 International Specialized Exhibition, which was held in Astana from June to September 2017. The AIFC is scheduled to enter into operation in January 2018.

II. Overview of the AIFC Legal Framework

On December 7, 2015, the Constitutional Law "On Astana International Financial Centre" (the "AIFC Law") was adopted, which defines the AIFC as a territory within the city of Astana, with limited borders and a special legal regime. The AIFC Law sets forth an independent legal framework based on the law of England and Wales and is drafted to complement the regulations of the Dubai International Financial Centre (the "DIFC").

Pursuant to Article 9 of the AIFC Law, the AIFC will have four principal bodies:

(i) the AIFC Management Council (top executive body), headed by the President of Kazakhstan;
(ii) the AIFC Authority (governing and operational body);
(iii) the Astana Financial Services Authority (financial services regulator); and
(iv) the AIFC Court.

According to Article 13 of the AIFC Law, the AIFC Court will be independent and separate from the judicial system of Kazakhstan and have exclusive jurisdiction over civil, employment, and financial disputes (though not over criminal or administrative offenses) arising between AIFC participants and/or the AIFC bodies. The AIFC Court will consist of the courts of first instance and the appellate courts. The decisions of the appellate courts will be final and binding with no right of appeal to the regular Kazakh courts.

The AIFC Court will have the exclusive right of interpretation of AIFC law, and its courts' judicial determinations will be guided by AIFC Court precedent, the law of England and Wales, and the norms and standards of the leading global financial centres. The AIFC Court will maintain sitting courts on-site at the AIFC facilities, and its benches of English law-trained judges will conduct proceedings in English.

The AIFC will also host the International Arbitration Centre. Where AIFC participants contractually elect to resolve disputes extrajudicially pursuant to arbitration, AIFC International Arbitration Centre arbitrators will adjudicate the cases. Arbitral awards granted by the AIFC International Arbitration Centre will be recognised and enforced in accordance with Kazakh law. The AIFC International Arbitration Centre will be modelled on the DIFC-LCIA Arbitration Centre and will seek to incorporate international best practices.

III. Benefits of AIFC Participants

The AIFC free economic zone will offer a number of financial and administrative inducements to its participants and their owners and employees, including:

- 50-year corporate tax holiday (until January 1, 2066) on income from financial and professional services provided in the AIFC;
- 50-year tax holiday (until January 1, 2066) on capital gains from sales of securities traded on the AIFC's stock exchange;
- 50-year individual income tax holiday (until January 1, 2066) on dividend income from sales of securities traded on the AIFC's stock exchange and from sales of shares in the AIFC participants;
- 30-day visa-free entry to Kazakhstan for citizens of 35 OECD country-members (including the US, UK, Canada, France, Germany, Switzerland, and the Netherlands) and citizens of the UAE, Malaysia, Singapore, Monaco, and other countries specified from time to time by Kazakhstan;
- five-year entry visa for foreign employees (and their family members) of the AIFC and AIFC participants;
- work permit exemption for foreign employees of the AIFC and AIFC participants;
- "one-stop shop" facility within the AIFC for visa issuance and registration of AIFC participants;
- exemption from property and land taxes for AIFC participants;
- the AIFC Court will be separate and independent from the court system of Kazakhstan and operate on the basis of the law of England and Wales;
- the AIFC will have its own arbitration centre in the form of the AIFC International Arbitration Centre;
- AIFC participants may conduct and settle their transactions in any currency they choose without regard to the FX restrictions set forth in the Kazakh domestic currency law;
- English will be used as the working language of the AIFC;
- AIFC participants may enter into transactions in the English, Kazakh, and/or Russian languages; and
- the proceedings in the AIFC Court will be conducted in English, unless the parties choose Russian or Kazakh as the language of their court proceeding.

As of today, the rules regarding the formation and registration of AIFC participants and the broader compliance requirements of AIFC participation remain subject to finalisation and adoption. It is anticipated that these elements of the AIFC framework will be based on those of the DIFC and other international financial centres to ensure efficiency and familiarity for international stakeholders.

IV. Conclusion

Establishment of the AIFC represents a substantial step toward realising Kazakhstan's "100 Concrete Steps Plan" of long-term socio-economic development and the gradual diversification of the economy away from oil and gas wealth. The AIFC is designed to be a technological and cultural catalyst for transforming Astana into an international financial hub that delivers a wide range of financial services to market participants throughout Eurasia and globally.

By effectively reducing market risk by importing internationally recognised commercial law precedent and best practices under the AIFC Court and International Arbitration Centre, Kazakhstan is simultaneously attempting to attract foreign direct investment, accelerate integration of the Kazakh markets into the global financial system, deploy enabling best-in-class financial technology platforms, achieve knowledge transfers sufficient to build up its skilled labour base, and capitalise on its geographic proximity to Chinese demand.

Central Asia is currently home to no other Dubai-equivalent financial centre: Kazakhstan has a first-mover advantage. As such, the animating principles and underlying rationale of the AIFC appear to be sound, and the ultimate success or failure of the project likely will depend on a few key variables: the degree of sustained political will in-country to implement in practice what the AIFC promises in theory; the BRI's ultimate unifying effect on the infrastructure and economies of Eurasia and degree to which Astana becomes the Chinese stepping-off point; and the eventual materialisation of demand for a Central Asian financial hub that better permits the global markets to follow the sun.

Endnote

1. The views provided herein are for general discussion and education purposes only and not attributable to any particular situation, individual, client, or otherwise.

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Moore & Van Allen PLLC

Moore & Van Allen PLLC is a full-service law firm and one of the largest and most preeminent law firms in the Southeast United States, with nearly 300 attorneys and offices in Charlotte and Research Triangle, North Carolina, and Charleston, South Carolina. Founded in 1949, MVA has a long history of civic service and noted international and national clients, including 110 Fortune 500 companies. MVA's business and corporate work is organised into more than 20 practice groups, including Bankruptcy & Financial Restructuring, Finance, Corporate, Litigation, Intellectual Property, and Real Estate. Moore & Van Allen is the only Charlotte-based law firm identified in the prestigious "Am Law 200" list. U.S. News & World Report and Best Lawyers recognised Moore & Van Allen in their 2017 "Best Law Firms" rankings, both regionally and nationally.

Unicase Law Firm

Unicase Law Firm provides a full range of legal services to local Kazakh and international clients. Our lawyers have contributed to the development of more than 90 national laws and regulations. Our clientele includes large national companies and international corporations in Kazakhstan. International financial institutions such as the EBRD, the World Bank, the International Finance Corporation, the Development Bank of China, and many more have repeatedly engaged Unicase to support their operations in Kazakhstan.

Trade Finance on the Blockchain: 2018 Update

Holland & Knight LLP

Josias Dewey

1. Traditional Trade Finance

The Primary Driver of Global Economic Growth

We have updated last year's discussion of blockchain and trade finance to address several new pilot projects, joint ventures and other significant advances made toward digitising the global trade engine. Also, where relevant, we have included new thoughts on matters of policy and trade that gained traction during the last year.[i] With approximately 80–90% of global trade reliant on trade finance, it is estimated that the industry is worth nearly $10 trillion a year. The evolution in trade finance is being driven by greater efficiencies and novel capabilities resulting from advancements in the underlying logistics of the global supply chain, all of which are being made possible by the combination of three powerful technologies: (1) blockchain and distributed ledger technology; (2) the Internet of Things ("IoT"); and (3) powerful machine learning capable cognitive tools (e.g., IBM's Watson) that are capable of analysing vast amounts of data that humans simply cannot do.

The transformation occurring in supply chain management and trade finance is not simply about converting from paper documents, such as letters of credit and bills of lading, to electronic documents. To the contrary, as we will discuss in detail, the changes that are occurring are about new ways that participants in supply chains can share information in a very granular and controlled manner, utilising novel technology that allows economic participants to trust the outcome of transactions without any need to trust the actual counterparties to a transaction. Equally important is the ability of distributed ledgers to accomplish the foregoing without the need for a trusted third party to act as an intermediary for the transaction – disintermediation has become a key theme of distributed ledger technology, and supply chains and the trade financing vehicles that keep them operating are not exempt from this phenomenon.

What is Trade Finance – Basic Mechanics

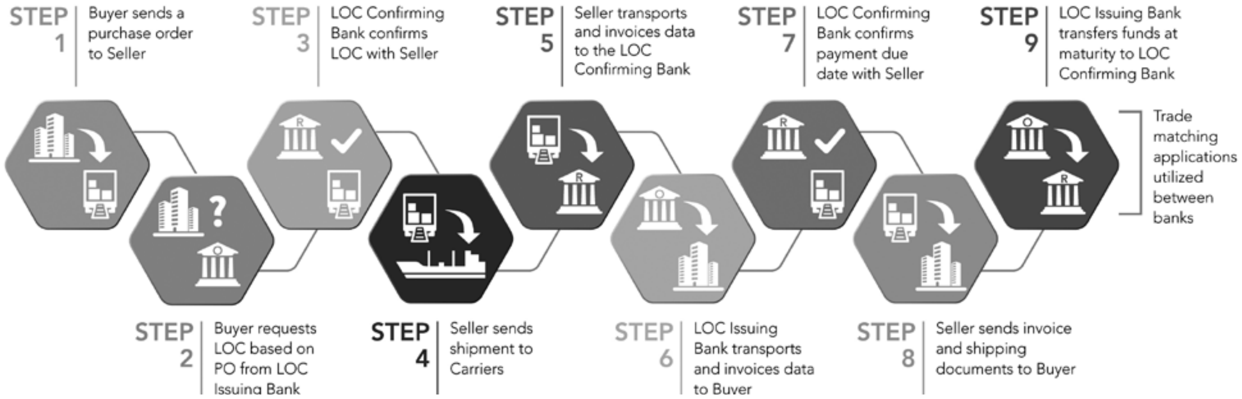
Before discussing the future of trade finance, it's important to understand the current mechanisms used to facilitate the movement of goods and commodities across the globe – much of which has remained static over the last few hundred years. It did not take human civilization long to discover the benefits of specialisation and trading resources that might be prevalent in one geographic region for other goods which are scarce in the same region. In the beginning, bartering ruled most forms of trade and even after stores of value, such as gold, allowed for the acquisition of goods for money, marketplaces were often static in terms of point of sale – thus requiring trading groups and companies to venture across long and often dangerous trading routes. With the advent of oceanic shipping, however, it became far easier to move large quantities of goods and commodities from one port to another far more efficiently.

While a superior approach in terms of economic efficiency, "chicken and egg" situations soon arose when sellers did not want to place their goods on a ship for delivery to the purchaser without payment; and likewise, buyers did not want to pay for goods that they had not received – enter trade financing solutions. In its most simple form, trade financing addresses the "chicken and egg" dilemma by effectively creating an intermediary, such as a bank who issues a merchant letter of credit, who can assure the seller of payment if the seller performs and protect the buyer from ever paying for undelivered or non-conforming goods. In most circumstances, this is accomplished by the buyer causing its bank to issue to the seller a merchant letter of credit in the amount of the purchase price for the goods. The bank who issues the merchant letter of credit generally requires that the seller present, together with the merchant letter of credit, documentary proof that conforming goods were delivered to the buyer and that the seller has met the conditions of payment. One of those conditions will be the delivery of a properly-executed bill of lading (a document of title) to the buyer, who with that and an opportunity to inspect to goods to ensure conformance, is never at risk of losing his or her capital in the event of the seller's non-performance.

It should be apparent that in many respect, the "finance" transaction described above has less to do with loaning money and extending credit and more to do with facilitating a transaction that might otherwise introduce too much risk for the buyer, seller or both. There are plenty of trade finance transactions that are akin to more traditional extensions of credit. For example, a farmer may need trade finance to acquire seeds and fertilizer and is unable to repay such financing until the farmer harvests his crop. In that case, the transaction could be solely driven by credit considerations. In some cases, trade finance serves both as a transaction facilitator and an extension of credit necessary to provide a farmer or manufacturer with inputs necessary to generate the profits necessary to repay the extension of credit. In the case of the farmer, the seeds and fertilizer may be shipped from a foreign producer, such that the trade finance solution serves both purposes – the role of an intermediary with respect to the exchange between the farmer and the foreign producer and that of an extension of credit because the farmer lacks the liquidity to purchase the inputs necessary to grow his crop.

Trade Finance – Traditional Lifecycle

While there are several forms of trade finance, we have chosen to further illustrate, via graphical illustration (which the author admits is an oversimplification with respect to many transactions), the mechanics of this industry through one of the most conventional types of trade finance facilities – a merchant letter of credit:



As entire books are frequently written on trade finance, we cannot analyse the above transaction from every participant's perspective in a single chapter. So, we will look at some of the most common pain points and areas of "friction" from the perspective of a bank or other financial institution providing trade financing in a transaction following the lifecycle depicted above. In any secured transaction, a trade finance lender will want to ensure that its position:

(i) is adequately collateralised (i.e., the seller has the goods it purports to have or will have when it is required to tender and the value of such goods is consistent with the assumptions made by the lender in underwriting the credit);

(ii) consists of a first-priority security interest (unless providing subordinate financing); and

(iii) is consistent with its understanding of risks posed by acts of god, casualty or other *force majeure* events, and that such risks have been mitigated by insurance or other means to the extent available.

To achieve the above three objectives, lenders often employ the following "controls":

(i) implementing relevant financial controls throughout the trade transaction lifecycle;

(ii) monitoring all material aspects of the transaction; and

(iii) ensuring that the collateral (i.e. the trade goods) are properly stored and transferred.

Using the Bill of Lading example illustrated above, implementing these controls can be a cumbersome and fragmented process for lenders, which often lead to the following "pain points":

(i) Fraud. Current methods of documentation, and documentation transfer, do not protect against the risk of parties, including lenders, relying on falsified documentation.

(ii) Tracking and Reconciliation Costs. Current fragmented trade lifecycles, which require human involvement and interaction throughout, require constant tracking and reconciliation by lenders and often require that such be done amongst several different platforms.

(iii) Authenticity of Goods. A lack of uniform tracking mechanisms from "source to sale" provides susceptibility for counterfeit goods to enter the trade lifecycle.

(iv) Confidentiality. The current necessity to (humanly) verify and reconcile points throughout the trade cycle make it difficult to ensure the confidentiality of the trading parties and terms.

It should come as no surprise that the above complexities often leave bank customers less than satisfied with the overall experience of obtaining the credit. To make matters worse, there has been a steady increase in transaction costs, in part, due to the increasingly difficult regulatory environment. Fortunately, all participants may soon be receiving relief from all of the above.

Trade Finance – Increasing Number of Stakeholders Means Growing Complexity

It is also worth noting that some of the additional friction in the market today is due to an increase in the overall number of persons involved in the process, including trade finance credit insurers, customs personnel and certification organisations – who depending on the existence of friendly trade arrangements – may be required to hold the goods at port or other locations for extended periods of time. This increase in participants has led to a corresponding level of complexity. Simply put, supply chain management and trade finance have become more complicated, while innovation was non-existent. Seemingly overnight, the paper documents that remained in use for decades are on the verge of extinction.

2. Emerging Technologies – Blockchain Technology

Blockchain technology is commonly defined as a decentralised peer-to-peer network that maintains a public, or private, ledger of transactions that utilises cryptographic tools to maintain the integrity of transactions and some method of protocol-wide consensus to maintain the integrity of the ledger itself. The term "ledger" should be thought of in its most simple terms; imagine a simple database (like an Excel spreadsheet) that can store all sorts of information (e.g., someone's name, age, address, date of birth). As you can write an entire book on the topic of blockchain technology and the law (I know because I did), set forth below is a very cursory review of the underlying technology. If you are not comfortable with the technology itself after reading the below, there are no less than a couple of hundred good descriptions available on the Internet (or you can find my book).

Blockchains tracking the transfer of virtual currency, such as Bitcoin, essentially maintain a ledger that tracks the transfer of Bitcoin from a transferor to a transferee. Perhaps most importantly, such ledgers are considered decentralised because transactions are stored on several thousand computers connected to a common network via the Internet. These computers are known as "nodes". Each node contains a complete history of every transaction completed on a blockchain beginning with the first transaction that was processed into the first block on that blockchain. This network of nodes is connected via the Internet, but in a completely decentralised manner (i.e., there is no single server to which all the nodes are connected). So, when we refer to the network, this describes all the peer-to-peer nodes operating under the same set of rules (commonly referred to as a "protocol"), which are embodied in computer code under which all participants in such blockchain operate. Thus, at the heart of every blockchain is an agreed upon protocol that ensures that only information upon which the network reaches consensus will be included in the blockchain. In other words, a network of computers, all running a common software application, must come to agreement upon whether a change to the blockchain (again, think "ledger") should be made, and if so, what that change should be.

As a proposed transaction propagates throughout this peer-to-peer network, there is still one last step left to consummate the transaction – the transaction needs to be memorialised into a block on the given blockchain ledger. "Blocks" are simply a convenient way of aggregating transactions into larger groups (or batches) for processing purposes. The perceived immutable nature of the ledger is rooted in the aggregation of time-stamped transactions into linear sequenced blocks. It is the aggregation into blocks that permits us to create links between transactions – the proverbial "chain" in the blockchain. Each block contains a reference to the block before it. This resulting relationship between all the blocks makes it exponentially more difficult to alter a prior entry in the ledger. Recently, certain protocols have been developed which have all the character of a blockchain, but without the block structures – hence the reason all blockchains are distributed ledgers while not all distributed ledgers are blockchains (e.g., R3's Corda platform is not a blockchain). For the time being, the terms distributed ledger technology and blockchain are generally used interchangeably – the reader should recall the distinction, however, in dealing with the implementation of a distributed ledger system that requires a blockchain style ledger.

While Bitcoin was the first implementation of blockchain technology (and the only implementation for several years), with the advent of the Ethereum protocol and the subsequent "Blockchain 2.0" protocols, the capability of the technology skyrocketed – as did the potential use cases. The reference to "Blockchain 2.0" generally refers to the development of smart contracts, which is executable computer code that is broadcast to all of the nodes connected to a distributed ledger – the resulting computation being what determines any changes to the ledger. While the term "smart contract" does not necessarily refer to a legally binding contract (but rather any snippet of code), some smart contracts do constitute legally binding agreements. The advent of smart contracts is critically important to its adoption for trade finance – without it, we would not be able to model the functionality and provisions of a letter of credit or bill of lading.

Another recent development that was necessary for distributed ledgers to play an active role in trade finance was the ability for parties to include all the details of a trade in the transmission of a transaction to a distributed ledger – but limit who can see which details with very fine control. For example, if a seller of crops experiences a liquidity crisis and must sell a portion of his crop for below market prices, the seller will want neither his competitors nor other buyers in the market to know the price for those crops. In this example, it is possible to broadcast the transaction with only the buyer and seller seeing the price and needing to validate the terms to the contract. Any other consensus on the network will be limited to the existence of the transaction itself (and most likely a time stamp as well).

While there are no less than a dozen protocols in regular use today, the two most public blockchains are Bitcoin and Ethereum. Anyone is free to connect to either of those protocols. Unlike public blockchains, most financial institutions and other enterprise users are not comfortable using public blockchains because of data security and privacy concerns, among others reasons. Instead, these institutions have or intend to deploy permissioned and/or private distributed ledgers, where each member of the distributed ledger knows with whom it is transacting. Again, there are many more protocols that are listed herein, but some of the more popular permissioned protocols are: (1) R3CEV's Corda platform; (2) Hyperledger Fabric (also hosted on IBM's cloud as its native blockchain solution); (3) Monax (formerly known as Eris); (4) Ethereum (permissioned version, Quorum, developed by JPMorgan); and (5) Ripple.

3. Emerging Technologies – The Internet of Things ("IoT")

Even alone, distributed ledgers would have a significant impact on supply chains and trade finance, but when coupled with two other technologies – IoT and Cognitive Analytics (including machine learning) – the impact will be nothing short of a paradigm shift. The Internet of Things (IoT) is one of the other technological advances that will have a major impact on the financial industries. IoT refers to the simple concept that more and more physical devices are becoming connected to the Internet (i.e., networked). Today, the types of devices being connected to the Internet is growing exponentially – both in terms of consumer and industrial products. For example, in January of 2018, Maersk and IBM announced the intention to establish a joint venture to provide more efficient and secure methods for conducting global trade using blockchain technology and IoT devices. The new venture aims at bringing the shipping industry together on an open global trade digitisation platform that offers a suite of digital products and integration services like transportation tracking systems.[ii]

This trend is expected to continue over the next several years, such that virtually all physical objects in the world will be (or at least have the capability to be) connected to the Internet. These connections will work both ways. Physical objects will transmit information about their internal state and/or information about environmental factors (e.g., temperature, humidity). Many objects will also have physical actuators (i.e., things that interact with physical world such as motors, locks, LEDs). Together with sensors, this means that many physical objects will be able to transmit real-time information over the Internet (whether by ZigBee meshes, cellular or satellite transmissions) to applications that can analyse that data and send commands back to physical devices to interact with the physical world. For example, if a Maersk storage container's internal temperature is too hot, that data will trigger an application monitoring that information over the Internet to send a signal back to the container's internal fans to cool it down again.

Blockchain technology will augment IoT in several positive ways. First, blockchains built in cryptocurrency payment protocols are perfect for interacting with automated payment systems, especially in the context of complex trade cycles that do not necessarily require human interaction. Second, and probably more importantly, the blockchain can add a level of security that no other existing technology can. The distributed ledger is perfect for ensuring that use and ownership rights are adequately tracked. For example, the generation of public/private keys is perfect for ensuring that only an authorised user can authorise the dispatch or delivery of goods.

4. Emerging Technologies – Artificial Intelligence and Cognitive Analytics

Artificial intelligence and cognitive analytics, including applications leveraging machine learning, are the final ingredients needed to radically transform supply chains and trade finance. By combining distributed ledger technology with IoT devices, such as sensors, real-time data is available to the parties to the transaction and can be recorded on an immutable, tamper-proof ledger. This capability alone significantly improves the overall supply chain and trade finance process, but what about data from one or more business processes that requires intensive calculations or analytics that the human brain cannot do? Artificial intelligence, especially the subsets known as machine learning and natural language processing have made significant advancements in just the last couple of years. These tools can receive the raw data from the IoT devices, process the data and format it into useful structured data that can be used to monitor contract compliance matters. These tools remove any limitation on human cognition and traditional computing devices that impair our ability to process complicated and voluminous data sets. For example, Oaken Innovations and the Toyota Research Institute partnered to create a blockchain ecosystem of IoT devices that will support the future of autonomous cars. The infrastructure will accommodate voluminous, frequent, heterogeneous transactions like toll payments, peer-to-peer ride and car sharing arrangements and immediate insurance claims.[iii]

In addition to real-time compliance oversight, artificial intelligence is also helping sellers and purchasers with business decisions that impact their entire enterprise, especially with respect to supply chain management. For example, price discovery is made possible so that a purchaser can unleash sophisticated algorithmic tools on massive amounts of data available online or through private network data feeds. Price discovery, however, is just the tip of the iceberg – a purchaser's entire inventory management process can be run by artificially intelligent machines, which can contract for supplies when appropriate without any human interaction. Machine learning capabilities are particularly useful because as these systems are used and provide feedback on the decisions they make, its performance or percentage of accurate decisions increases until it performs its function far better than its former human counterpart.

Of course, the real-time data feeds monitoring in-route products and the price discovery and inventory management are ultimately all part of one operation – to ensure the smooth and optimal purchase order and inventory life cycle. We must also keep in mind that these machine capabilities will continue to grow at a rapid pace, especially given the fact that Moore's Law appears to still have some run left in it before humans are no longer capable of fitting more transistors on smaller and smaller pieces of silicon. This assumes, however, that we do not discover entirely new ways to supply ever increasing computational power (e.g., quantum computing).

5. Trade Finance 2.0: Applying Emerging Technologies and Paradigm Shift

Any lawyer or professional who has practice transactional law for any length of time, knows that the more stakeholders involved in a transaction or series of related transactions, the more difficult it becomes and the more "friction" is involved in the form of higher transactional costs and lost efficiency and output. Often, trade finance and supply chain transactions involve several stakeholders, especially when there is a cross-border aspect to the transaction. The number of participants can grow fast. Possible participants include the buyer, the seller, a letter of credit issuer (i.e., a bank), one or more correspondent banks, customs and revenue (tariff) officials, warehouse owner, logistics companies and a host of other possible involved participants. It is for this reason, that distributed ledgers when combined with IoT devices and cognitive analytics prove to be one of the most powerful uses of distributed ledger technology. The cost savings and reduction in transactional costs and friction in many cases are extreme. For example, the ability to model a merchant letter of credit in the form of computer code (e.g., Solidity, Java, Go); and more importantly, the ability of that code to execute on a distributed ledger using self-implementing conditions to, in the case of a letter of credit, release funds programmatically to the seller without any need for the seller to present a paper letter of credit to anyone. Consider the reduction in friction afforded by this mechanism. Rather than a paper letter of credit needing to work its way through a series of correspondent banks, each of which must be paid a fee, a digital letter of credit that is self-implementing executes automatically when the conditions to payment are met – resulting in a significant reduction of expenses. Recently, BBVA applied blockchain technology to a letter of credit transaction between two offices in Mexico and Spain. Based on the trial, BBVA observed that the time taken to submit, verify and authorise an international letter of credit trade transaction was reduced from seven to 10 days, to just 2.5 hours.[iv]

The inverse is also true, and no less important – meaning that the bill of lading, which evidences the transfer of ownership to the goods to the purchaser, is also transformed into computer code where it resides on a distributed ledger until payment is released to the seller. Upon payment, the bill of lading will automatically be released to the purchaser in digital form. This removes any issues with respect to fraudulently procured or produced documents of title, such as a bill of lading. In Q4 of 2017, ZIM, an Israeli container shipping company, announced it completed a pilot that used blockchain technology to carry out a paperless bills-of-lading. During the trial, all participants issued, transferred and received original electronic documents using blockchain technology, which managed the ownership of documents in order to eliminate disputes, forgeries and unnecessary risks.[v]

In addition to payments and documents of title, many more aspects (in fact, virtually all of them) can be converted to self-implementing code broadcast to a distributed ledger, together with corresponding, real-time contract administration and monitoring, including casualty insurance covering the goods during transit, foreign trade credit insurance and the coordination of any other logistics companies (e.g., last mile carriers).

In addition to what I will refer to as "core logistics", there are a host of other significant benefits to virtually all participants in the lifecycle of an average transaction, including integrity and providence matters. For the consumer, there is certainty that the product is what it says it is, whether that is assurances that a luxury brand is not a cheap counterfeit good, or that a non-GMO food product is in fact not made from genetically altered DNA. For governments, both taxation and import requirements are far easier to enforce when all of the data for products and manufactured goods flowing into and out of a country are monitored in real-time and stored in a tamper-proof, immutable ledger. Governments and regulators can easily require a "master key" with respect to goods and products over which they have some jurisdictional interest. For example, Walmart recently engaged in a pilot programme to ensure the safety of produce sent to the U.S. from a foreign producer. It is for these reasons and many others that so much investment has been spent in supply chain and trade finance. The benefits gained by the number of parties involved in the supply chain far exceeds the potential cost to implement.

It is important to appreciate that the concepts described in this chapter are not mere academic discussions or the thoughts of a futurist. To the contrary, everything has been implemented in real world pilot programmes, and some aspects are already in deployed, production systems. In fact, of all the potential use cases generally discussed as appropriate for distributed ledger technology, there is no other use case likely to reach critical mass in deployed, production-ready distributed ledgers. The world's largest participants in all aspects of trade finance and supply chain management are actively pursuing pilots and otherwise moving full speed ahead – these companies include Walmart, BNY Mellon, IBM, HSBC, Bank of America, Microsoft and Barclays, just to name a few. To be fair, the transition to Trade Finance 2.0 is not remotely finished and ninety-some percent of supply management and trade finance are accomplished in the same manner as described in the very beginning of this chapter. The feedback, however, received from all the companies involved in pilot or prototype programmes has been unanimous – distributed ledger technology (as augmented by IoT and AI) will soon result in a complete paradigm shift.

While the promised land is in sight, there are still obstacles that must be overcome before all the world's trade is completed on distributed ledgers. Payment rails for the distributed systems currently under investigation are still not perfect. More specifically, unlike Bitcoin and Ethereum, Hyperledger Fabric (IBM Blockchain) and R3's Corda do not include a native cryptocurrency, and even if one were added (it's easy to model digital cash on either platform), there is no existing system to process the volume of exchanges of fiat currency and digital currency that would be generated by global trade. As such, it is more likely that payments made will be triggered by messages from the distributed ledger that instruct the payment from a traditional fiat account (e.g., messaging with SWIFT codes to release funds from the purchaser's account or its letter of credit issuer).

Maybe a more systemic hurdle to overcome is the lack of uniformity in the different distributed ledgers that are currently under active development. As discussed earlier, there are several different distributed ledger protocols under active development. These different ledgers cannot currently communicate with each other, but this may, however, be a temporary impediment. Several development shops are working on interfaces and other strategies to achieve interoperability between these different ledgers. In addition, systems are being developed to ensure backwards compatibility for each new distributed system with existing legacy systems since it's not possible to transition the world's information technology systems all at one time. Furthermore, given the rather nascent nature of the technology, many companies prefer to overlay their distributed systems atop their legacy system to maintain a level of redundancy (what I refer to as the "training wheels" approach, which I believe to be a prudent approach).

While no one is certain of the exact timing, based on the current pace of advancement, it seems likely that there will be several deployed, production systems in operation within five years. Be skeptical of anyone who suggests these systems are 15 or 20 years away from production. In fact, if these systems are not in production before 10 years, that means they are likely never going into production and a newer, better system has surfaced (e.g., quantum computing). The reason for such a statement is that the potential benefits are so fundamental and so enormous when scaled on a global basis, that most major players in every industry imaginable are in a sprint towards implementation. The growing number of pilot programmes and proof of concepts appearing in the general news and economic journals is only further testament to the investment being made around the globe.

This rapid pace of development is likely to continue or even accelerate as industries reach critical mass – which triggers another key benefit of distributed ledgers, which is the mutualisation of the cost to implement new systems. Because distributed systems allow all participants to access a common truth, only one distributed ledger system needs to be designed and engineered to a common set of specifications and standards. Today, every participant maintains its own centralised database that is the subject of costly reconciliations with other counterparty records. For example, rather than 10,000 manufacturers in a province of China maintaining their own central database – as they do today – only one decentralised system must be operational; thus, resulting in each company paying 1/10,000th of the costs of such decentralised system. It is tempting to think distributed ledger technology is an area limited to the world's megabanks or largest retailers, like Walmart. The headlines certainly reinforce this perception.

For small to midsize banks, suppliers, manufactures and others involved in supply chain management and trade finance (or any other industry for that matter), distributed ledger technology is an opportunity to level the playing field and eliminate certain competitive advantages held by their larger competitors, especially with respect to the banking industry in the United States. Anti-money laundering (AML), OFAC and other compliance costs represent a disproportionate amount of expenses for small and midsize banks. Distributed ledger technology also can permit banks to mutualise the cost of compliance, and in doing so, improve the effectiveness of their overall programmes. This is just one of the many potential benefits (others include participation trading platforms) available to small and midsize banks. The choice seems simple. For those institutions willing to be innovative and to take some risk, there is an opportunity to be a trailblazer with potentially market-changing innovative solutions. For those who remain complacent and willing to allow the world's largest banks to maintain a monopoly on the future, their own future does not seem bright.

Perhaps the one force that can derail the implementation of distributed ledger technology across the globe is regulations or other policy enforcement that is too restrictive, and ultimately smothers out the innovation needed to reform our existing and inefficient processes. Fortunately, many jurisdictions, including the United States, already have existing legislation that, while passed years before distributed ledger technology existed, is broad enough in scope because of their origins out of the original Internet revolution. So, electronic or digital signatures, including public key infrastructure, are already accepted practice. While there will almost certainly be a need to tweak commercial laws here and there, especially in the cross-border context, those efforts should be easy to accomplish given the mutual benefits for all involved, including governments. The policy decisions that will impede distributed ledger technology are those too myopic on counterbalancing issues, such as consumer protection. Any policy that says no to any risk, is a policy that will shutter innovation. Going forward, it is important that the regulators and policymakers both in the United States, the U.K., continental Europe, China and the rest of the world's global trade powers, implement regulations and rules that foster innovation and encourage institutions to take chances to achieve potentially game changing results. That is not to say that financial institutions need a licence to engage in reckless activities, but rather enough flexibility to innovate by take calculated chances and risk. There is a balance that can be found where consumer safety and the soundness of the economic environment is maintained, while innovation fosters much needed economic growth and employment growth around the globe.

Endnotes

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Joe Dewey is a financial services and real estate partner in Holland & Knight's Miami office and is considered a thought leader on blockchain technology. Mr. Dewey regularly represents banks and other financial institutions across the entire spectrum as measured by assets and scale, from community to global money center banks. Mr. Dewey spends a considerable amount of time at the convergence of human prose legal contracts, as well as computational contracts, based primarily on computer code. This includes smart contracts that can be implemented on Hyperledger Fabric (or IBM's Blockchain service), Ethereum (both public and permissioned versions) and R3's Corda platform. Dewey spends a considerable amount of his practice in this space assisting clients in identifying optimal distributed ledger use cases and developing proof of concept applications. He can assist in the transition from proof of concepts (PoCs) to production systems built by our clients' primary technology solutions providers.

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Trends in the Expanding Global Private Credit Market: What to Expect for 2018 and Beyond


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Introduction

It has been called alternative credit, private credit, direct lending, shadow banking and other names, but as it approaches $1 trillion in assets under management, private credit has become a significant force in financial markets. What was initially described as bank financing without the bank has become much more complex. In recent years, there has been significant growth for private credit across a variety of debt products at all market levels, but the growth in middle market lending has been the most dramatic. We will look at the evolution of private credit globally, as well as the trends we see going forward.

Recent Growth and Expansion

Private credit started as an alternative to bank lending. It was generally used for the smaller deals or riskier credits that the banks passed on as not fitting their investment profile. Rather than posing competition to traditional banking, private credit filled a gap in the market for businesses in need of financing which could not access customary commercial financing sources or needed an additional layer of debt beyond what those sources would fund. Initially, private credit transactions tended to be smaller in size, higher in coupon and shorter in maturity than traditional bank lending. Private credit developed in multiple areas of the market including SBIC investments, middle market lending, asset-based lending, infrastructure, real estate finance, trade finance and other products. While some asset managers focus on niche or specialised areas, many employ multi-class investment strategies.

Following the financial crisis and the tightening of bank credit generally, private credit expanded in all markets with the US and Europe seeing the greatest increase in deal activity. The combination of restrictions on sub-investment grade credits on banks' balance sheets, the consolidation of financial institutions, the limits imposed on balance sheet lending among banks, the general shying away from the middle market and the strategic shift to focus on fee-generating business by banks during this period all created the opportunity for private credit to step in and pick up the slack. In the middle market, private credit rapidly expanded to fill the void left by banks, evolving from single lender financing arrangements into a source of liquidity for syndication, to acting as anchor investors for club deals, to acting as primary lender and lead arranger and competing with traditional banks for mandates. The evolution and growth in private credit was fuelled by a combination of (i) an influx of capital from institutional investors in private and publicly traded credit vehicles, (ii) borrowers being increasingly receptive to private credit as a primary source of funds, and (iii) changes in the regulation of banks in the US and globally.

Increased capital

Several factors drove the influx of capital into the private credit market. A primary driver has been institutional investors seeking to diversify from private equity and hedge funds. The low default rates and relative stability of the debt markets combined with more predictable returns not correlated with public market equity returns made private credit investments an attractive portfolio alternative for institutional investors. Recognising the burgeoning institutional appetite for private credit products, private equity managers started offering private credit fund alternatives. With the necessary fund raising infrastructure already in place, these firms capitalised on their scale, fund raising prowess and synergies between debt and equity fund products to generate substantial amounts of capital for investments in the private credit market.

As more money came under management, new entrants to the market drove investment deeper and broader in the market to join the already established players in the private credit market such as Antares Capital, Apollo Global Management, Ares Management, Cerberus Capital Management and KKR Credit. Illustrative of the continued investment in the private credit market are the January 2018 closing of the KKR Private Credit Opportunities II – a $2.24 billion global fund that will seek to invest in privately negotiated debt securities, mezzanine investments and asset-backed and specialty finance investments – and the December 2017 closing of the Ares Management LP $3.4 billion junior capital direct lending fund, which raised $900 million in excess of its target. Additionally, in 2017, Oaktree Capital Management, L.P., acquired certain assets from Fifth Street Management LLC for $320 million and became the investment adviser to two business development companies previously managed by Fifth Street Management. The Carlyle Group has also focused on the private credit market – from 2016 through 2017, they have raised over $30 billion for their private credit business.

Increased capital is not only being infused into the established private credit managers – capital raising by private credit managers that traditionally fall outside of the top 10 of assets under management are experiencing faster growth than those at the top. Owl Rock Capital launched two years ago and, through 2017, it has raised nearly $5 billion for its debt fund that focuses on middle market lending. This is a significant shift from just a few years ago when there was a large concentration of invested capital amongst a select group of leading private credit managers.

Over the last 10 years, assets under management with private credit managers tripled from approximately $200 billion in 2007 to over $600 billion at the end of 2017. During this period, private credit was the third-largest class for fund raising year-on-year with private equity and real estate-focused funds taking the top two spots. This influx of capital has expanded the scope and depth of private credit investment at all levels of the debt markets with private direct lending accounting for just over half of all the funds raised for debt strategies. The ample supply of dry powder for investing has also made private credit managers more competitive for mandates, particularly in the middle market lending and sponsor-based acquisition finance markets. The growth rate for the industry does not show any signs of slowing and assets under management for private credit are expected to exceed $1 trillion by 2020.

Borrower perspective

On the demand side, private credit has become an attractive alternative to traditional bank financing for a number of reasons – with the primary themes favouring private credit being faster credit approval, the flexibility to accommodate complex structures, the ability to provide financing at multiple levels of the balance sheet and, increasingly, borrower-favourable terms.

Unlike the traditional bank credit committee process, private credit vehicles are usually structured to be more nimble. Further, the buy and hold strategy of many funds limits syndication and flex risk and makes adjusting to significant transaction changes faster and more fluid.

The flexibility of private credit also extends to the ability to offer borrowers one-stop shopping with a variety of types of structures and financings at all levels of the balance sheet. This is an attractive feature of private credit, as it can provide the borrower with a litany of financing options to meet its specific needs. Although senior secured financing is the most prevalent structure in private credit, financings are also frequently structured as unitranche, second lien, payment in kind, or PIK instruments, mezzanine and other junior financing investments. Based on responses from the survey participants in the Alternative Credit Council report, nearly 60% of the survey participants utilise unitranche structures, mezzanine and other junior structures.

As competition among private credit managers and banks increased, the terms of private credit transactions have relaxed and become more borrower-friendly over the last several years. By way of example, a recent survey of 60 participants in the private credit market representing more than $500 billion in assets under management conducted by the Alternative Credit Council in collaboration with Dechert LLP, demonstrated that nearly half of the survey participants are incorporating less onerous covenants into their private credit transactions in comparison to the prior three-year period, while only 14% believe that covenants have become more onerous over that same time period. Further, the private credit market is moving towards covenant-lite and Term Loan B structures, which traditionally has been reserved for larger syndications with institutional investors and high-yield bonds. The flexibility is not just limited to covenants either – in that same study, nearly half of the survey participants have confirmed that pricing terms are more borrower-friendly than was the case three years ago.

Lastly, as with any other growing industry, borrower demand is increasing due to a virtuous circle of repeat business. As many borrowers and sponsors are exposed to the flexibility and attractive pricing of private lenders and become more familiar with it, they tend to return to such lending partners for their next round of financing.

Regulation

Moving beyond investor enthusiasm and the increasing demand from borrowers, the growth of private credit can also be attributed to a key advantage it maintains over traditional lending institutions – for the time being, private credit is relatively free of regulation for the deployment of funds.

In the wake of the financial crisis, the Federal Reserve, Federal Deposit Insurance Corporation and the Office of the Comptroller of the Currency announced guidelines in 2013 that recommended banks forego extending credit to borrowers with a leverage ratio that was greater than six times or that were otherwise determined to be unlikely to pay down debt quickly.

In addition to the Leveraged Lending Guidelines and similar regulations in Europe and other markets, traditional banks are subject to additional regulatory requirements and ongoing supervision such as US oversight through the Office of the Comptroller of the Currency with respect to liquidity requirements, concentration limits and capital limits. For the moment, the private credit market is not subject to the Leverage Lending Guidelines or any of the additional regulatory requirements that apply to traditional banks in the US and globally. Rather, private credit managers are free to structure debt for highly leveraged borrowers, subject only to the investment strategies of each private credit manager and any restrictions related to the leveraging of their capital.

Trends Forward

With the continued evolution and expansion of the private credit market, we note some key trends to watch in 2018:

- North America, with the largest global debt markets, remains the largest market for private credit. North American-focused funds accounted for more than 60% of the over $100 billion in new money raised globally by debt funds in 2017, reclaiming the top spot after UK- and Europe-focused funds finished first in 2016. For the middle market, the number of US and Canadian deals were close to five times the number closed in the UK and Europe. With the majority of institutional investors globally based in North America, this market should continue to grow and lead in funds raised and invested.
- So far, Brexit has not had an impact on deal volumes in Europe, with the UK remaining the largest market for private credit transactions followed by France and Germany. In Germany, the market share of private credit for middle market buyout financing grew to 30%, with deal volume triple the amount for 2016. Overall, the last several years have been robust in Europe for private credit fundraising with Alcentra, Ares, Bain, Barings, BlackRock, BlueBay, CVC, Hayfin, HPS, ICG and others adding to their dry powder for investment. Note, however, that growth in European Union private credit capital formation is hindered, to some extent, by the application of the AIFM Directive which directs marketing efforts toward attracting investors in private credit funds managed by non-EU alternative asset managers.
- Asia growth will be on a region-by-region basis due to the differences and conflicts in debt investment law and regulation. For example, in certain Asian jurisdictions such as Malaysia, Singapore and other various Indian states, private credit managers, as unlicensed money lenders, are prohibited from making loans to third parties absent an exemption or receiving a money lender's licence. In Indonesia, Bank Indonesia requires that any external debt that is available in a currency other than the Rupiah must maintain a hedging

ratio, a minimum forex liquidity ratio and a minimum credit rating. These types of restrictions will present private credit managers with challenges expanding to these markets. Investments of capital coming from within Asia to other regions of the world is an entirely different story as we have seen significant interest from Korean, Japanese and Chinese investors in US direct lending funds.

- Private credit deals are expanding beyond the middle market in both directions. As noted in the Alternative Credit Council report, the survey participants responded that borrowers who have less than $25 million of EBITDA represent 43% of the total market share. Deals are also moving upmarket, with borrowers with EBITDA in excess of $75 million making up about 20% of the market. While borrowers with EBITDA of between $25 and $75 million still comprise approximately 40% of the private credit market, this is a sharp decline from what has been previously reported in similar reports in prior years. Private credit transactions in Asia, Australia and New Zealand tend to involve borrowers in the $50 million plus EBITDA range. As increased capital continues to be raised, we would expect deal sizes to continue to trend upward and for the continued expansion beyond the middle market.
- An increasing number of private credit managers are seeking financings with longer maturities. Per the Alternative Credit Council report, 20% of the survey participants have a preferred target term of six years or greater – a percentage that is significantly up from the 8% of survey participants indicating a preference for such longer maturities in the 2015 edition of the Alternative Credit Council report.
- More private credit managers are taking the lead arranger role in transactions both as sole underwriter and as leader of a club syndicate. The structure, terms and syndication of these deals are becoming indistinguishable from those with a traditional bank lead. From a documentation perspective, the lines are blurring between private credit and traditional banking. This convergence will continue and be strongest in the middle market sponsor-based acquisition financing and refinancing context.
- Unitranche and PIK structures remain a staple in the private credit market. However, more and more deals, particularly sponsor-backed financing, are using a Term Loan B model. Although lending arrangements with sponsor-backed borrowers remain popular (more than half of the deals last year in the US, UK and Europe were sponsor-backed), there is increasing activity with sponsorless lending. We anticipate this trend to continue as it is an obvious growth area for private credit managers. Despite the fact that sponsorless deals may require more due diligence at inception and there is added risk that no sponsor with committed capital is present to support a credit during difficult periods, private credit managers view the potential growth in this sector as outweighing the risks.
- Terms are becoming more borrower-favourable. Note, however, that given the buy and hold strategy that is prevalent in the private credit market, there is less opportunity for a non-syndicated transaction to push the envelope on borrower-friendly terms with an agreement to "flex back" if the terms do not clear. It is likely that the expansion of borrower-friendly terms will continue to be at the upper end of the market for the better syndicated credits and first tier sponsors, and then trickle down from there. It is the trickle down into the middle market and the need to stay competitive that is trending private credit transactions in the direction of more borrower-favourable terms. For private credit transactions, covenant-lite and covenant loose deals are more prevalent the higher the EBITDA of the borrower.
- Banks still outpace even the largest private credit funds in their ability to do deals over $1 billion. Even with increased fundraising success by private credit managers, we do not expect this to change. While the bulge bracket part of the market will continue to be the province of the banks, private credit is becoming more influential at the high end of the market through collaboration with banks and participation in club deals and syndicates.
- Due to their access to government liquidity arrangements, banks continue to hold an advantage in being able to offer lower interest rates than private credit lenders, and this advantage is particularly significant for larger transactions. Recently, however, the gap has narrowed, and we would expect that trend to continue. In 2017, the all-in spreads in the US and Europe for middle market private credit transactions were approximately 2% higher than widely syndicated bank credits in those markets: a drop of about 1% from five years ago. The drop in spreads has also lead to compressed pricing to junior debt, particularly for second lien and mezzanine instruments. This compression may not be sustainable (particularly if default rates rise) and places pressure on private credit, particularly new and less established entrants, to achieve expected returns.
- Banks hold an advantage in being able to offer products beyond term debt, including revolvers, letters of credit, treasury management and hedging. However, more and more private credit managers are teaming up with banks to provide these services on their transactions.
- Overall, club deals, syndication and collaboration among banks and private credit managers are increasing and will continue to grow. Private credit managers are no longer just relying on existing relationships and networks that they have established within their particular industries to originate deals. Private credit managers are now in the position of being able to refinance existing deals with borrowers and are looking to traditional banks, private equity managers and other industry advisors to source deals.
- With assets under management increasing in the US and globally, there will be some pressure on private credit lenders to relax credit standards, particularly among asset managers seeking to deploy newly raised funds quickly. The competition for deals will also be a factor in relaxing credit terms. This will likely be more pronounced in the UK and Europe where the competition is chasing a smaller universe of deals. However, with over $200 billion of dry powder held by private credit managers globally at the start of 2018, we would expect an impact in all markets.
- Some institutional investors, such as pension funds and insurance companies, are setting up their own direct lending operations. Given costs involved in ramping up direct lending operations (and the existing competition in the field), we expect most institutional investors to continue to access the direct lending market through established asset managers.
- Thus far, the private credit industry has grown during a period of low default rates and some of the more common lending structures, such as unitranche, have not been tested in insolvency proceedings. The recent RadioShack bankruptcy involved two unitranche financings with split collateral packages, but settled prior to the court determining any key issues, including whether the agreement among lenders and the waterfall provisions contained therein qualified as a subordination agreement under the Bankruptcy Code. How private credit structures and returns fair in contested bankruptcies is an area that will need to be closely monitored to see if any changes should be made from current practice.
- The regulatory landscape in the US and globally is constantly changing. There is a chance that some of the competitive advantages private credit holds in this regard could change as well. In late 2017, after months of consideration, the US Government Accountability Office declared that the Leveraged Lending Guidelines amount to a formal rule that Congress can review, therefore potentially paving the way for the guidelines to be modified or overturned.

Conclusion

While the influx of capital, attractiveness to borrowers and lack of regulation all interacted and combined to drive the growth and evolution of the private credit industry, these factors effectively drove a fourth factor: the migration of bankers to private credit managers, which has furthered the convergence and mainstreaming of private credit. The bankers are becoming the shadow bankers.

Today, with over $600 billion in assets under management, private credit managers are acting more and more like banks but without the restrictions of bank regulation and are effectively competing for mainstream mandates across a variety of transaction types and sectors. The distinction between traditional banking and private credit will continue to blur, particularly for sponsor-based acquisition term loan funding where the private credit structures and syndicates are becoming indistinguishable from the traditional bank models.

Absent a downturn in markets or a shift in the regulatory landscape, the private credit industry will continue to grow and be increasingly competitive in global markets. 2017 was a banner year for private credit globally and with over 300 private credit managers looking for additional funds for investment, there are no signs yet of it slowing down in 2018.

For further reading: Financing the Economy 2017, the role of private credit managers in supporting economic growth, Dechert/ Alternative Credit Council (2017).

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Replacing LIBOR: the Countdown to 2022

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Four years from now, the scandal-plagued London interbank offered rate, or LIBOR, may no longer exist. With the July 2017 announcement of the U.K. Financial Conduct Authority (FCA) that panel banks will not be compelled to submit LIBOR rate information after 2021 because there are insufficient actual transactions to support submissions, it is likely that LIBOR will be phased out due to the absence of FCA backing. Although publication of LIBOR may not completely end in 2021, global financial markets need to be prepared for a transition from LIBOR to limit disruption if LIBOR ceases to be an accepted reference rate for financial contracts.

First published in 1986 by the British Bankers Association (BBA), an unregulated British banking lobby group, LIBOR began as a standardised benchmark to assist banks with setting interest rates on corporate loans. LIBOR refers to the London-based unsecured wholesale market rate for deposits between major banks denominated in certain currencies. These deposits can be available either on an overnight basis or for varying durations, such as one, two, three, six or 12 months. Traditionally, this market has been a source of liquidity for banks and the rates paid for these deposits have served as the basis for LIBOR interest rates.

What began as an interest rate used in syndicated loans became ubiquitous in the financial markets when institutions began using it in the 1990s to set the floating leg in derivatives contracts and the Chicago Mercantile Exchange adopted LIBOR to calculate the value of its Eurodollar futures contract in 1997.[1] Today, LIBOR serves as the reference rate for an estimated $350 trillion of financial contracts, including commercial and retail loans, floating rate notes, derivatives, mortgages and securitised loans. The notional value of all outstanding financial products referencing USD LIBOR is estimated to be approximately $200 trillion.[2]

How LIBOR Works

Historically, LIBOR for a particular interest period was determined by averaging quotes of several reference banks as of approximately 11:00 a.m. London time. Today, LIBOR is determined by reference to a screen quote from a customary market quotation service, such as Reuters or Bloomberg, with reference bank quotes used only as a fallback if the screen quote is unavailable.

The LIBOR quotation service uses rates compiled and published by ICE Benchmark Administration Limited (IBA), a U.K. subsidiary of global exchange operator Intercontinental Exchange (ICE). As IBA explains on its website,[3] IBA provides an indication of the average rate at which a panel bank can obtain unsecured funding in the London interbank market for a designated period in certain specified currencies. Producing a total of 35 rates on each business day, IBA determines LIBOR for five currencies (U.S. Dollars, Euros, Japanese Yen, Pound Sterling and Swiss Francs) with seven maturities, ranging from overnight to 12 months. IBA obtains quotes from a reference panel currently numbering between 11 and 16 banks for each currency for which LIBOR rates are determined. After discarding the top and bottom quartiles, IBA averages the remaining quotes to determine the rate, now known as ICE LIBOR.

The LIBOR Scandal

Beginning in 2012, an international investigation into LIBOR revealed a widespread plot among multiple large banks to manipulate LIBOR rates for profit starting as far back as 2003. During the global economic upswing of 2005 to 2007, Barclays and other banks reportedly manipulated LIBOR so that their traders would make profits on swaps. According to *The New York Times*, "swaps traders often asked the Barclays employees who submitted the rates to provide figures that would benefit the traders, instead of submitting the rates the bank would actually pay to borrow money".[4]

Following the onset of the financial crisis in 2008, LIBOR came under scrutiny with claims that banks were underreporting rates to avoid perceptions that they were being charged higher rates due to their weakened financial condition. The market for interbank lending had dried up, and, with no regulatory supervision, bankers were essentially making up numbers. Although the BBA denied it, government investigations soon showed not only that rate manipulation was pervasive, but also that government officials and central bankers had known about LIBOR's deficiencies for years but had failed to act.[5] In 2012, regulators discovered extensive manipulation of LIBOR by banks to benefit themselves and their traders' positions. Allegations of LIBOR manipulation led to lawsuits, criminal prosecutions and billions of dollars in fines and settlements paid by some of the world's largest banks. By the end of 2016, a dozen banks had paid regulators about $10 billion in penalties.

As a result of the LIBOR investigations, the U.K. government began considering reforms to LIBOR, and in 2012 the U.K. Parliament passed legislation to strengthen financial regulation and reform the LIBOR system.[6] That legislation created the FCA as a new government agency with expanded powers to investigate and regulate financial markets, including LIBOR.

In September 2012, a report on LIBOR was published based on an independent review led by U.K. financier Martin Wheatley, who became the first head of the FCA.[7] *The Wheatley Review* caused several reforms to be implemented in 2013 and the replacement of the BBA with IBA as the LIBOR administrator in 2014. As administrator, IBA has formalised the submissions process and made significant improvements to LIBOR. Still, trust in the integrity of LIBOR continued to erode due to concerns about manipulation and a decrease in the level of interbank borrowing activity serving as the basis for actual LIBOR quotes.

The FCA Announcement

On July 27, 2017, Andrew Bailey, the FCA's Chief Executive, announced that, after 2021, the FCA would no longer exercise its authority to compel panel banks to submit quotes used to determine LIBOR. In his speech, Mr. Bailey emphasised that there are insufficient underlying interbank transactions to continue to rely on LIBOR as a benchmark, noting that it is unsustainable "for market participants to rely indefinitely on reference rates that do not have active underlying markets to support them".[8] Because there currently is a very low volume of transactions on which banks can base their LIBOR submissions, banks rely on their "expert judgment" to form many of their submissions, and even those submissions that are transaction-based may be based on few actual trades. A key concern is the element of subjective judgment inherent in the LIBOR rate, which, in the FCA's view, leads to a "greater vulnerability to manipulation". Although the use of expert judgment allows daily publication of LIBOR, many banks understandably are uncomfortable with providing judgment on transactions with such a minimal level of activity.

Mr. Bailey noted that while LIBOR could remain viable past 2021, market participants cannot safely assume that it will and central bankers and regulators need to develop a robust alternative set of rates before then to protect against financial market disruption if LIBOR is no longer published. The FCA has obtained agreements with panel banks to continue submitting rates until the end of 2021, at which time a new benchmark is expected to replace LIBOR. Emphasising that the transition from LIBOR should be "planned and orderly rather than unexpected and rushed" in order to mitigate risks, Mr. Bailey stated that a transition period will enable the markets utilising LIBOR to develop and implement alternative rates in a coordinated manner that avoids major disruption.

While the public's understanding of the risk of LIBOR's unreliability increased significantly with the FCA announcement, the official sector has been concerned about it for years. In 2013 and 2014, both the LIBOR manipulation scandal and regulators' concerns as to the reliability and robustness of bank submissions prompted the undertaking by regulators of reviews of major financial benchmarks.

In the U.K., in June 2013 the FSB established an Official Sector Steering Group (OSSG) of central banks and regulators that it tasked with coordinating reviews of LIBOR and other interbank offered rates (IBORs),[9] and guiding the work of a Market Participants Group, which in turn was asked to examine the viability of adopting additional reference rates.[10] Drawing upon reviews of benchmark administrators by the International Organization of Securities Commissions (IOSCO)[11] and the work of the Market Participants Group, in 2014 the FSB published a report that prioritised as key objectives the transition to rates that are anchored in actual transactions and the development of alternative nearly risk-free reference rates (RFRs).[12] In the U.S., the Financial Stability Oversight Council (FSOC) in its 2014 annual report also reported concerns over the integrity of LIBOR and recommended that U.S. regulators identify alternative interest rate benchmarks based on observable transactions and develop an adoption plan for a transition to new benchmarks.[13]

Since these reports were issued, regulators have done substantial work on reforming global benchmarks in accordance with principles developed by IOSCO as set forth in its 2013 *Principles for Financial Benchmarks* report.[14] In the European Union, the EU Benchmarks Regulation, a regulation entered into force in June 2016 that became fully effective on January 1, 2018, introduces a regulatory framework for benchmarks across the EU and establishes, among other things, a requirement for the authorisation of administrators of financial benchmarks used in the EU.[15]

In the U.S., in November 2014, the Federal Reserve, in cooperation with the Treasury Department and the Commodity Futures Trading Commission (CFTC), convened the Alternative Reference Rates Committee (ARRC) to identify a robust reference rate to replace USD LIBOR.[16] The ARRC is a public-private sector initiative comprised of major banks, which are also interest rate derivatives dealers, and regulators, including the CFTC, the Federal Reserve Bank of New York (FRBNY), and the Treasury Department. The ARRC was tasked with identifying a set of alternative reference interest rates that are more firmly based on transactions from a robust underlying market and that comply with emerging standards such as the IOSCO *Principles for Financial Benchmarks*. Although the ARRC considers LIBOR an unreliable benchmark for all financial contracts, the ARRC so far has focused primarily on identifying a replacement rate for USD LIBOR for interest rate derivatives, where the exposure to LIBOR vastly exceeds other sectors.

Similar initiatives to identify and transition to alternative RFRs are progressing in the U.K. by the Working Group on Sterling Risk Free Reference Rates under the guidance of the Bank of England (BoE),[17] in Japan by the Study Group on Risk-Free Rates under the guidance of the Bank of Japan,[18] and in Switzerland by the National Working Group on CHF Reference Rates under the guidance of the Swiss National Bank.[19]

The Development of Risk-Free Reference Rates

In June 2017, the ARRC announced its selection of a Broad Treasury Financing Rate (BTFR), based on secured transactions in the overnight U.S. treasury repo market, as its proposed replacement for USD LIBOR.[20] In July 2017, the CME Group announced that it will develop futures and options contracts based on BTFR.[21] In August 2017, the Federal Reserve requested public comment on this proposed repo rate (among other rates), which it referred to as the "Secured Overnight Financing Rate" (SOFR).[22] SOFR will be based on about $660 billion in actual daily repurchase transactions between banks, hedge funds, money market funds and others, and does not require expert judgment.

On November 2, 2017, the ARRC hosted a roundtable at the FRBNY to present the ARRC's work, including its recommendation of SOFR as an alternative rate and details of its paced transition plan. The FRBNY, in coordination with the Treasury Department's Office of Financial Research, expects to begin publishing SOFR daily in mid-2018.[23] To commence the transition, ARRC members are expected to put into place the infrastructure for futures and/or Overnight Index Swap (OIS) trading in SOFR by the second half of 2018. The ARRC projects trading in futures and/or a bilateral OIS referencing SOFR to begin by the end of 2018. A term reference rate will be created once sufficient liquidity in the SOFR derivatives markets has developed to produce a robust rate, expected by the end of 2021.[24]

Representatives of both ARRC and non-ARRC member firms discussed how the risks surrounding LIBOR may impact not only the interest rate derivatives market, but also a wide range of other financial products and markets. Federal Reserve Governor (now Chair) Jerome Powell stated (in introductory read remarks) that the ARRC so far had focused its work on derivative products because that is where the largest exposures to LIBOR are, but noted "…[n]ow, however, market participants have realized that they may need to more seriously consider transitioning other products away from LIBOR".[25] Corporate loans are one of the cash products that will be considered by the ARRC going forward, along with floating rate notes, mortgages, securitisations, CLOs and consumer loans.

Chairman Powell's statement reflects concerns expressed by market participants that fundamental differences between SOFR and LIBOR require consideration by the ARRC in order to avoid the potential for disruption of a number of cash product markets. Whereas LIBOR is a forward-looking unsecured term rate that takes into account rate differences resulting from the credit risk of interbank lending and changes in pricing of that credit risk over time (term risk), SOFR is a backward-looking RFR representing the cost of overnight funding through a repurchase transaction secured by government debt.[26] As a secured overnight rate that reflects neither credit nor term risk, SOFR is much lower than LIBOR and there is a substantial concern that a value transfer would occur for existing transactions upon switching from LIBOR to SOFR. To address these significant distinctions between the two benchmarks, the Loan Syndications and Trading Association (LSTA), which has taken a leading role in channelling concerns of the $4.3 trillion U.S. syndicated loan market, requested in its comment letter to the Federal Reserve that term fixings for SOFR and a bank credit risk spread be published.[27] To further a transition to SOFR for cash products, the ARRC's membership recently was reconstituted to include buy-side end users of cash products.[28]

Despite the push by policymakers for a transition from LIBOR to an alternative rate, many U.S. investors would like to see LIBOR remain available. Nearly 80% of respondents to a Bank of America Merrill Lynch survey believe that LIBOR should continue to be quoted with a "more robust methodology".[29] In his speech, Mr. Bailey left open the possibility that LIBOR may continue to be quoted after 2021. In fact, IBA has announced plans to continue publishing LIBOR after 2021, which would require panel banks being willing to continue making submissions without FCA compulsion.[30] However, the FRBNY seems to favour pressuring market participants into SOFR in order to prevent creation of a bifurcated market.

In the U.K., the Working Group on Sterling Risk Free Reference Rates has proposed the Sterling Overnight Index Average (SONIA) as a near risk-free alternative to GBP LIBOR for use in sterling derivatives and other relevant financial contracts. Currently in the process of reforming the benchmark, the BoE expects SONIA to serve as the new benchmark rate commencing in April 2018.[31] In November 2017, the BoE announced that a key near-term priority will be for the working group to make recommendations on the development of term SONIA rates.[32]

The European Central Bank reportedly plans to publish a new overnight rate for interbank unsecured lending among euro-area banks and has called on market participants to provide comments on the high-level features of a new unsecured overnight interest rate.[33] In Japan, an RFR based on actual transactions in the overnight unsecured market has been developed for Yen (the Tokyo Overnight Average Rate, or TONAR). The National Working Group on CHF Reference Rates has recommended the Swiss Average Rate Overnight, or SARON, an overnight secured rate administered by the Swiss National Bank, as the alternative RFR for Swiss Franc LIBOR.[34]

What Happens Next?

While substantial progress has been made on identifying RFRs for derivatives, work on alternative reference rates for loans and other debt contracts is just beginning. The ARRC proposes the eventual creation of term reference rates intended to approximate LIBOR for different tenors based on derivatives contracts referencing SOFR after those products achieve liquidity. But uncertainty exists as to what extent overnight rates can be used to create forward-looking term reference rates, who will calculate and publish those rates, and whether those rates will be commercially satisfactory to LIBOR users under debt agreements. The development of term reference rates is projected to take several years, and the lack of clarity surrounding the process presents a challenge to parties drafting debt agreements during the transition period.

If new rates are not adopted consistently across various types of financial instruments, one of the many issues of concern is a potential economic mismatch between benchmarks used in loans and floating rate notes and those referenced in interest rate derivatives intended to hedge that exposure. Another issue is that LIBOR is published for five currencies and, absent global coordination on a replacement benchmark, the determination of reference rates for these currencies may use disparate approaches, resulting in different pricing for different currencies under multicurrency facilities utilised by corporate borrowers.[35]

What happens during the transition to loan agreements and debt securities referencing LIBOR? Assuming LIBOR's demise, conversion of debt agreements that reference LIBOR with maturities beyond 2021 to an alternative reference rate will be critical for market stability. As discussions on a replacement rate for these contracts are just starting, current transactions likely will continue referencing LIBOR until an alternative rate has gained debt market acceptance. In the U.S., debt market participants have been evaluating customary LIBOR fallback provisions in agreements and focusing on whether greater flexibility can be built in to select a replacement rate for LIBOR with a limited consent process. While many LIBOR-tied debt instruments provide mechanisms to determine a fallback rate if LIBOR is not available, these mechanisms generally are not sufficiently robust or intended to be utilised in the long term. With no alternative rate yet accepted in the debt markets, including workable procedures for selecting a successor rate upon LIBOR discontinuance is the most prudent course of action that parties can take during the transition period.

Syndicated Loans

Legacy credit agreements in the U.S. syndicated loan market typically have fallback mechanisms in the event that LIBOR is temporarily unavailable. Although variations exist, the LIBOR definition may provide that if the screen rate is unavailable, the rate is determined by interpolating between LIBOR rates of other specified durations, or by the rate offered to the agent bank by major banks for U.S. dollar deposits in the London interbank market for delivery on the first day of the interest period in the approximate amount of the loans. But these fallbacks are inadequate if LIBOR no longer exists. Similarly, market disruption clauses addressing a temporary unavailability of LIBOR or other trigger event by establishing fallback pricing at an alternative base rate are not a solution because borrowers would be dissatisfied with more expensive base rate pricing on a permanent basis if LIBOR disappears.

In anticipation of the LIBOR sunset, parties to new U.S. syndicated loan agreements with maturities extending past 2021 have begun including mechanisms for selection of a successor interest rate without requiring the consent of all affected lenders (which typically is required for any interest rate reduction), with triggers such as agent determination that LIBOR unavailability is unlikely to be temporary, regulatory announcement that LIBOR will no longer be published, or LIBOR still being reported but no longer being the prevalent rate in the leveraged loan market. No market consensus on these provisions has yet developed and a variety of approaches have appeared in documentation.

At one end of the range, some provisions allow the agent alone to select a comparable or successor rate and apply it in a manner consistent with market practice. Others allow the agent and the borrower to choose a successor rate, with many (but not all) of these provisions giving the majority lenders consent rights, either by affirmative consent or negative consent (usually a five-business day period to object), to the successor rate amendment. Many of these mechanisms require the successor rate to be selected in a manner giving due consideration to the then prevailing market convention for determining an alternative interest rate for U.S. dollar denominated syndicated loans at the time. Although many of these replacement rate provisions expressly override the syndicated loan market convention that changes to interest rate provisions require the consent of the majority lenders and any interest rate reduction require the consent of all affected lenders, other provisions don't expressly override these voting requirements, resulting in ambiguity.

Some replacement rate provisions are drafted narrowly to refer to a successor reference rate or index rate, suggesting that only a new benchmark can be selected without making other changes. But replacing LIBOR with SOFR would require a spread adjustment to preserve pricing. Toward that end, some broader provisions expressly permit a successor rate amendment to make appropriate adjustments to the loan agreement to preserve pricing. It is expected that these alternative rate provisions will evolve over time when there is further clarity on an alternative rate that is accepted in the U.S. loan market. For legacy loans, modifying the fallback provisions to implement greater flexibility to amend probably will be undertaken on a case-by-case basis because many legacy loans will be amended or refinanced before the end of 2021.

In Europe, since 2014 the Loan Market Association (LMA) template loan documentation has included an optional "Replacement of Screen Rate" clause that permits replacement of a benchmark rate that becomes unavailable with the consent of the borrower group and the majority lenders. Absent inclusion of the LMA optional provision in the loan agreement, an amendment to replace the benchmark likely would require the consent of all lenders.

Collateralised Loan Obligations

Many indentures in the U.S. $470 billion CLO market contain a fallback provision if the LIBOR screen rate is unavailable on the interest determination date. In that case, the calculation agent would request quotes from reference banks in the London interbank market and determine the rate based on the mean of the quotes provided. If an insufficient number of quotes are obtained, LIBOR for the subject interest period will be LIBOR as calculated on the prior interest determination date. Since reference banks no longer will be providing quotes if LIBOR becomes permanently unavailable, this mechanism effectively would turn floating rate obligations into those of a fixed rate instrument, which is not what investors bargained for. Also, this fallback mechanism risks creating a mismatch between the interest rates on the CLO securities and on the CLO's underlying loans if those loans reference a successor benchmark.

Amending fallback provisions in legacy CLO indentures typically requires the consent of 100% of the noteholders of each class and a portion of the equity so it may not be feasible. Given this high consent threshold, most CLOs likely will address the discontinuance of LIBOR by winding down the CLO and redeeming the notes after the no-call period.

It is anticipated that when the loan market accepts an alternative benchmark, CLO market acceptance quickly will follow. Until that occurs, the CLO market is focused on achieving a consensus on robust and consistent fallback methodologies for LIBOR replacement. Some new CLO indentures permit an amendment to provide an alternative rate with majority consent from the controlling class of noteholders and ratings confirmation. Possible alternative rates appearing in some recent CLO indentures include (i) the quarterly pay reference rate acknowledged as being the industry standard for leveraged loans by the ARRC or the LSTA, or (ii) the quarterly pay reference rate used in calculating the interest rate of at least 50% in principal amount of either (x) the CLO's underlying loans, or (y) floating rate securities issued in the new issue CLO market since a specified recent date bearing interest based on an alternative benchmark. If the requisite consents to amend are not obtained, a fallback mechanism may either require or permit the collateral manager, in its commercially reasonable discretion, to select an alternative reference rate that may be one of the above replacement rates. The ultimate fallback remains the same as that in existing CLOs: if no amendment has been adopted and the collateral manager has not selected a new rate, LIBOR will be the rate determined on the prior interest determination date.

Floating Rate Notes

Typically, indentures in the U.S. market for floating rate debt securities tied to LIBOR provide for the calculation agent to determine a fallback rate if no LIBOR screen rate is available on an interest determination date. In such event, the calculation agent would source rate quotes from reference banks in the London interbank market that such banks would offer to prime banks for U.S. dollar deposits for a designated amount for the relevant interest period and, if at least two quotes are obtained, use the arithmetic mean of such quotes. If London banks do not provide sufficient quotes, frequently the calculation agent may source quotes from major New York City banks for loans to leading European banks. When sufficient rate quotes are not obtained, the rate for the preceding interest period continues in effect. Given that reference banks are highly unlikely to voluntarily offer similar rate quotes after LIBOR's demise, this fallback methodology risks applying the rate in effect at the end of 2021 as fixed for the remainder of the term – clearly not a desirable outcome. Further, conversion to a fallback rate that could differ significantly from a new benchmark accepted in the market, such as SOFR, would risk creating inconsistencies in the debt capital markets and general dissatisfaction among noteholders.

If a fallback mechanism is not included in the indenture or form of notes, any indenture amendment that would reduce the interest rate would require the consent of all noteholders, which would be potentially costly and difficult to obtain. Alternative interpretations concerning the consent required for this type of amendment would be, when read most expansively, that no consent is required because the amendment would be effected to cure an ambiguity, omission, mistake or similar defect and the amendment does not materially adversely affect the interests of security holders. However, due to the potential economic impact on security holders, it is difficult to argue that changing the benchmark for a floating rate security is a ministerial change. Another interpretation would be that the consent of the holders of a majority in outstanding principal amount of the notes would be sufficient to effect the amendment if no interest rate reduction were to result. However, the possibility that an amendment could decrease the rate is likely to drive the parties to conclude that, pursuant to the terms of the indenture as well as Section 316(b) of the Trust Indenture Act of 1939,[36] a unanimous approval is required.

Given the interrelationship between LIBOR-based debt securities and the derivatives markets, it is expected that the debt capital markets will be guided by the guidelines on fallback provisions that are being developed by working groups established by the International Swaps and Derivatives Association, Inc. (ISDA). For the time being, most LIBOR-tied debt securities issued since the FCA announcement still rely on the standard fallback mechanisms described above. However, a limited number of recent indentures authorise the calculation agent (in some cases in consultation with the issuer), if LIBOR has been permanently discontinued, to substitute the alternative reference rate selected by the central bank, reserve bank, monetary authority or similar institution (including any committee or working group thereof) in the relevant jurisdiction and to make other necessary or desirable amendments to facilitate that change, in each case consistent with market practice.

Disclosure documents for recently issued LIBOR-tied debt securities, for the most part, contain a risk factor discussion of the implications of the FCA announcement, the uncertainty surrounding the discontinuance or reform of LIBOR and a transition to alternative reference rates, and the potential adverse effect of a replacement benchmark on the level of interest payments and the value and liquidity of the securities. This discussion could be expanded, if appropriate under the circumstances, to cover the lack of robust fallback provisions in existing documentation, the potential that application of the ultimate fallback effectively could result in a fixed rate, the possible need to amend existing indentures to specify an alternative rate through a consent solicitation, and whether requisite consents could be obtained at an acceptable cost or at all.

Interest Rate Derivatives

With the support of the FSB, in 2016 ISDA began an initiative of consultation with market participants on the implementation of alternative RFRs and the development of robust fallbacks for LIBOR and other key IBORs. The objectives of various working groups established by ISDA include:

- identification of triggers for fallback rates;
- identification of alternative RFRs designated by the applicable RFR working group or OSSG;
- development of possible methodologies for application of credit spread and term structures for fallback application (seeking to eliminate or minimise the potential for manipulation and value transfer when the fallback is applied);
- amendment of the 2006 ISDA Definitions to incorporate the fallbacks into new trades (changes would not automatically apply to legacy transactions); and
- development of a plan for amendment of legacy contracts to include the amended definitions, including a protocol to incorporate the fallbacks into legacy trades.[37]

Although the ISDA work is primarily relevant to interest rate derivatives, it potentially could be adopted for other financial instruments, particularly when hedged by an interest rate swap, but that would need to be addressed on a market-by-market basis.

In addition, ISDA has begun a comprehensive analysis of potential issues and solutions relating to a transition to RFRs, which will include a targeted global survey of buy- and sell-side firms to identify the means by which market participants can effectively implement benchmark transitions and highlight potential challenges.[38] According to ISDA, the report will explore, among other topics, potential adjustment required to transition from IBORs to RFRs for new and legacy contacts, including documentation issues, the potential for value transfer, threats to market liquidity, the requirement for term fixings and differences in credit spreads between existing and new rates. On February 1, 2018, ISDA, together with the Association of Financial Markets in Europe (AFME), International Capital Market Association (ICMA) and the Securities Industry and Financial Markets Association (SIFMA) and its asset management group (SIFMA AMG), published a roadmap that highlights key challenges involved in transitioning financial market contracts from IBORs to RFRs.[39] The roadmap aggregates and summarises existing information published by regulators and the various RFR working groups in order to provide a single point of reference on the work conducted so far to select alternative RFRs and plan for transition.

Conclusion

Substantial progress has been made by regulators and policymakers towards replacing LIBOR in 2021, with SOFR currently anticipated to be the replacement rate for most U.S. dollar-denominated instruments. Still, it is too early to form any clear views on what rate or methodology will replace LIBOR in debt agreements, and what impact the transition from LIBOR will have on the financial markets that rely on this benchmark. Although the FCA announcement contemplates a planned and orderly transition period over the next several years, uncertainty exists as to whether a longer transition period will be needed and to what extent market disruption can be minimised in connection with the transition.

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Investment Grade Acquisition Financing Commitments

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The investment grade bridge loan commitment is an important component of middle and large cap merger and acquisition transactions involving investment grade acquirors[1] (also referred to in this article as borrowers). The bridge loan commitment provides assurance to the acquiror and seller that the acquiror will be able to fund the cash portion of the purchase price at closing, whether or not the acquiror has suffered a material adverse change and whether or not the funds can be raised in the capital markets. Examples of transactions announced in 2017 with an investment grade bridge loan commitment include: CVS / Aetna ($49.0 billion); Gilead / Kita Pharma ($9.0 billion); Amazon / Whole Foods ($13.7 billion); and Thermo Fisher / Patheon ($7.3 billion). This article provides an overview of bridge loan commitments for investment grade companies in the U.S. bank market.

Investment grade bridge commitments are often provided in the U.S. by large banks, and provide a commitment to lend a short-term bank loan (typically, the maturity is 364 days) to fund the cash purchase price of an acquisition in the event long-term or "permanent" (i.e., more than one-year maturity) financing is not available. While the bulk of the permanent debt financing will have a maturity of more than one year, there are exceptions. This permanent financing is generally in the form of a combination of notes issued in the capital markets and bank term loans, with notes providing the majority of the financing. The banks offering the commitments must have sufficient capital available to hold these commitments through the sometimes lengthy executory periods of merger and acquisition transactions (although, as is discussed below, the commitments are syndicated after signing). To the extent a financing package includes a mix of bridge loans and bank term loans, the bank term loan component adds flexibility to the borrower's capital structure since bank debt has more liberal prepayment provisions than notes issued in the capital markets (*in lieu* of or to refinance bridge loans). The balance of the funds required might be obtained from cash on the balance sheet of the borrower, commercial paper and sometimes, the target company's cash on hand.

The terms of the bridge loan typically include a 364-day maturity, no prepayment penalty/call protection, and floating interest rates. Unlike in a below investment grade leveraged buyout bridge commitment, there is no provision to convert the bridge into longer term debt after a year at the option of the lenders. Expenses including ticking fees, funding fees, duration fees and increasing interest rate terms make the bridge loan more expensive financing than is expected for the permanent financing. Instead of incurring the bridge loans, the borrower expects to fund the acquisition with the proceeds of permanent debt and sometimes, equity financing. Only if the borrower is unable to raise permanent financing to fund the acquisition (or is unable to do so on attractive terms) will it draw down the bridge commitment to close the transaction.

Advantages of Bridge Financing Commitments

Sellers to investment grade companies typically expect that the obligation of the buyer to close the acquisition will not have a financing contingency. In addition, the seller will want to know the general sources of the cash portion of the purchase price. The bridge commitment fills the gap on the financing, without requiring the borrower to have the cash on hand at time of the signing of the acquisition agreement.

Additionally, while an investment grade company is generally able to access the capital markets on short notice on favourable pricing terms, in an acquisition there is often an extended period between signing and closing while regulatory and shareholder approvals are obtained. Raising the permanent financing immediately upon signing might lock the borrower into funding it may not eventually need, require an expensive escrow arrangement for notes with expensive call premiums, and/or require the borrower to incur bank term loans. In each such case, the closing of the financing would require the immediate payment of financing fees and the ongoing added interest expense during the executory period with no guarantee that the acquisition will close. Consequently, a bridge commitment allows the borrower to defer incurring the expense of raising permanent financing until it has better visibility on the likelihood of closing.

Once the conditions to closing are satisfied, the borrower will be obligated to close promptly. If at that time, the market for permanent financing is unavailable to the borrower, the borrower might not be able to raise the financing required on favourable terms, or at all. As a result, it reduces risk on both the borrower and the seller to obtain a bridge financing commitment. It also makes a potential buyer's bid more competitive, since a competing bid would arguably also need a bridge commitment to be credible and the competitor might find that banks are unwilling or not able to issue large commitments to multiple bidders.

Documentation

The initial documentation for a bridge facility commitment will include a commitment letter, together with a term sheet setting forth the terms and conditions of the bridge loan. There will also be a fee letter documenting the fee arrangements with the lead arrangers. In addition, there will be an engagement letter for the notes component of the permanent financing to be issued in the capital markets (as opposed to term loans). The financing letters will be signed concurrently with the acquisition agreement.

The process of negotiating the bridge facility commitment may require substantial time, depending on how many lead arrangers compete for the assignment or the level of detail specified in the term sheet. The borrower may seek proposals from multiple banks and conduct parallel negotiations with each in an effort to identify competitive terms. Alternately, the borrower may elect to work initially with only one or two institutions in order to avoid bringing additional parties that could complicate the confidential acquisition process.

The commitment letter and fee letter do not include many of the detailed provisions which are set forth in the credit agreement. However, the letters are meant to cover all key economic terms and are thus highly negotiated.

If the borrower has an existing credit facility prior to announcement of the acquisition, the credit agreement for such facility will often be agreed by the parties as the documentation precedent for the bridge loan. Among other things, any financial maintenance covenants in the bridge facility will typically track the financial covenants in the borrower's existing credit facility. However, as is discussed below, the closing conditions in the bridge credit agreement will be more limited than in the borrower's existing bank credit facilities. In particular, the occurrence of most events of default (except as to bankruptcy or specified representations and warranties) are typically not a closing condition.

Conditions

The conditions precedent to funding the bridge facility are a key component of the commitment letter. In general, the conditions to funding the bridge loan are very limited, especially as compared to a bank commitment letter in certain other acquisition scenarios. Acquisition bridge commitments adhere to the principal of "limited conditionality", which provides for a narrow set of conditions, the satisfaction of which is largely in the borrower's control.[2]

For the lenders, the basic conditionality requirements are twofold. Mainly, if the seller fails to satisfy the conditions to closing in the acquisition agreement, the lenders are not required to fund. Second, the borrower must comply with basic documentary formalities, and provide its historical financial statements, and depending on the significance of the transaction, those of the target, in order to facilitate placing the permanent financing. Specific components of these conditions are further summarised as follows.

Information-related conditions

Depending on the significance of the acquisition, financial statements of the acquired company and *pro forma* financial statements might be required by the SEC to market the permanent financing in a public offering. Consequently, the borrower may need to require delivery of additional financial information from the seller beyond what the target company has historically prepared in order to satisfy the bridge financing conditions. This is most likely to become an issue for negotiation if the target company does not already have audited financial statements, which could occur if the target company is a division of another company. It is also customary for the acquisition agreement to contain a covenant in which the target company agrees to cooperate with the borrower's financing process.

However, it is not customary in an investment grade bridge commitment to have, as a condition to funding the bridge, a specific minimum "marketing period" for the marketing of a notes offering, during which the requisite financial information was available. Such marketing periods are typically seen in below investment grade bridge loan commitments.

Acquisition-related conditions

Certain conditions to the bridge financing have the effect of ensuring that the acquisition proceeds in a manner not materially different from what was agreed by the borrower and the seller at the time of the bridge commitment.

Prior to making the bridge facility commitment, the lead arrangers will have been afforded the opportunity to review the acquisition agreement, as well as conduct due diligence on the seller and the target company. As a result, the scope of the representations and covenants in the acquisition agreement will have been satisfactory to the lead arrangers at the time of signing. The bridge facility will then include certain conditions directly tied to the acquisition agreement.

First, there will customarily be a condition that the acquisition agreement will not have been amended, modified or waived after the signing date in a manner that would be materially adverse to the lenders. Second, lenders will require that there be a condition that no "Target Material Adverse Effect" (as such term is defined in the acquisition agreement) shall have occurred during the period between the signing of the commitment and closing. Third, the lenders' requirement to fund the bridge loans will be conditioned upon the representations and warranties in the acquisition agreement with respect to the target company that are material to the interests of the lenders being true and correct in all material respects at closing, to the extent that, as a result of such breach of representations and warranties, the borrower has the right to terminate the acquisition agreement.

In each case, the acquisition-related conditions in the bridge commitment letter should track the corresponding conditions in the acquisition agreement. The conformity of the conditions is important to the buyer (and seller) so that, once the conditions to the acquisition are satisfied and the parties are in a position to close the acquisition, there is certainty of funds and they know that the conditions to the bridge loan financing will also be satisfied.

Other conditions

In addition to the description above, the conditions to funding the bridge will include (i) the accuracy in all material respects of certain fundamental or "specified" representations as to the borrower under the bridge loan credit agreement, (ii) the delivery of customary certificates and legal opinions, (iii) the delivery of "know your customer" information required by law with respect to the borrower, (iv) payment of fees and expenses, and (v) absence of bankruptcy defaults as to the borrower.

Syndication

The initial bridge commitment is often provided by only one or two lenders acting as lead arrangers, who then seek to syndicate a substantial portion of their commitments to a group of financial institutions. The syndication process is planned in advance by the lead arrangers and the borrower with pre-identified potential syndicate lenders, who are often (but not required to be) the borrower's existing relationship banks.

As part of the syndication process, the lead arrangers and the borrower will host a conference call or bank meeting to provide information (on a confidential basis) to the potential syndicate lenders regarding the acquisition and the terms and conditions of the bridge financing. The syndicate lenders will then commit to their respective allocations of the bridge facility, either through a joinder agreement to the commitment letter or by entering into a bridge loan credit agreement with the borrower and the lead arrangers. Upon entering into such joinder agreement or credit agreement, the syndicate lenders will generally be contractually committed to fund the bridge in their respective syndication amounts, and the lead arrangers will thereafter only retain a contractual commitment to fund in respect of the non-syndicated amount.

Concurrent with their commitments under the bridge facility, the syndicate lenders will be engaged for a proportionate role in the permanent debt or equity financing to fund the acquisition. For the syndicate lenders (like the lead arrangers), they are willing to commit capital to back the bridge commitment, so that in addition to sharing in the bridge fees, they are afforded the opportunity to earn fees associated with the future debt or equity offerings of the borrower *in lieu* of or to refinance borrowings under the bridge facility.

If the lead arrangers are unable to complete the intended syndication with the pre-identified group of lenders, they may expand the syndicate to additional institutions subject to certain limitations. Any additional institutions will at least be subject to consultation with the borrower (and will typically require the borrower's reasonable consent), and the commitment letter may specify that all syndicate lenders be institutions with investment grade credit ratings.

If the intended syndication is not achievable because banks are unwilling to take on a portion of the commitments on the agreed terms, the lead arrangers may exercise their "flex" rights to make the terms of the bridge facility more favourable to the lenders. The "flex" for an investment grade bridge facility will typically be limited to an ability to increase pricing by up to a certain negotiated amount, but can include other changes to the terms of the bridge facility.

Prior to funding of the bridge, any assignment by the syndicate lenders of their commitments will be subject to consultation with the borrower, or its consent. In many financings, borrower consent is not required for assignments to existing syndicate lenders or their affiliates. In addition, the borrower may be able to designate "disqualified" institutions, consisting of competitors of the borrower and other institutions identified by the borrower prior to the initial commitment date, which may not become lenders without the borrower's consent in its sole discretion, either before or after funding of the bridge.

In order to avoid interference with the syndication, the commitment letter will typically include a "clear market" provision. The clear market prohibits competing financings, with exceptions for the anticipated permanent financings, refinancings of existing debt and other ordinary course financings. Other exceptions to the clear market provision are often requested by borrowers to address specific situations or needs of the borrower and are often highly negotiated. Another consideration in negotiating the "clear market" is whether it will apply only to the buyer or to the target business as well (and whether the seller will agree in the acquisition agreement to comply). To facilitate syndication, the commitment letter will contain a covenant in which the borrower agrees to cooperate with the arrangers, and to use commercially reasonable efforts to cause the seller to also cooperate. However, compliance by the borrower with the cooperation covenant would usually not be included as a condition to the lenders' obligation to fund the bridge loans.

Commitment Reductions and Permanent Financing

During the period between signing and closing of the acquisition, the banks will require that the proceeds of any significant capital raise not required for a specified purpose be applied to pay the acquisition consideration. As such, lenders will ask to include in the commitment letter that the bridge facility commitment be reduced on a dollar-for-dollar basis with the net proceeds of debt and equity issuances and non-ordinary course asset sales, subject to certain negotiated exceptions.

The permanent financing to reduce the bridge facility may comprise the proceeds of debt, in the form of bonds or term loans, and/or the proceeds of an equity offering. The composition of the permanent financing will be based on factors including market conditions, desire to maintain a certain credit rating and other capital structure considerations.

Exceptions to the commitment reduction requirement are intended to anticipate other capital needs of the borrower during the period between signing and closing of the acquisition. For example, if there is a need to raise funds to refinance existing debt during the commitment period but prior to closing, or to make a separate investment or acquisition that may take place during such period, then such amounts should be excluded from the mandatory commitment reduction requirement. One point that is often negotiated is whether this exception to raise money to refinance existing debt should apply only to debt maturing during the commitment period or also to debt maturing within a limited time period after the commitment period terminates (i.e. through one year after the termination date of the commitments). In addition, amounts borrowed under existing credit lines will typically not be required to reduce the bridge. Furthermore, it is customary to set a "*de minimis*" threshold, below which proceeds of debt and asset sales will not be required to reduce the bridge facility commitment. A "*de minimis*" threshold for equity proceeds is less common.

Fees and Pricing

The economics for lenders in a bridge facility commitment include several types of payments which are scheduled to be made at different times during the period of the commitment.

First, the lead arrangers and any other lender that provides a commitment may be paid a commitment fee for their initial commitments at signing of the acquisition agreement. The amount of this fee is not publicly disclosed.

Second, the lenders will be compensated for maintaining the commitment for an extended period of time by a "ticking fee", the terms of which are generally set forth in the term sheet. There is often a second commitment fee paid on the outstanding amount of the bridge commitments as of a specified date after signing, also related to the commitment being maintained for an extended period. These fees will be paid on a *pro rata* basis to all lenders in the syndicate at such time. The dates on which the ticking fee commences and any additional commitment fee is paid are points for negotiation, and may vary across deals based on transaction-specific circumstances and market conditions.

Third, the lenders will be compensated for funding the bridge commitment paid as a one-time funding fee payable on a *pro rata* basis to the bridge lenders. In addition, the lenders might be entitled to a "duration fee" at 90, 180 and 270 days after funding. The most typical structure of the duration fee is 0.50% after 90 days, 0.75% after 180 days and 1.00% after 270 days. The purpose of the "duration fee" is to encourage the borrower to refinance a funded bridge loan with permanent financing as expeditiously as possible after the closing date.

Fourth, the initial interest rate margins on the bridge facility will increase following funding of the bridge. The most typical rate of increase for interest rate margins is 0.25% on each of the 90^{th}, 180^{th} and 270^{th} days after funding.

To address potential changes in the business prospects of the borrower between signing and closing (and after funding), the interest rate margins for the bridge loan will typically be based on a ratings-based grid. Pricing will therefore adjust higher or lower in order to reflect the credit ratings of the borrower at any given time. The ticking fee rate may also be ratings-based, though a flat ticking fee is not unusual.

In addition to the fees set forth above, all of which are directly connected to the bridge commitment and the bridge facility, the lead arrangers and the other lenders will also earn customary negotiated fees in connection with debt and equity offerings for the permanent financing.

The commitment letter, fee letter and/or engagement letter, as the case may be, will usually provide that the committing lenders are entitled to some or all of the fees payable in connection with the bridge commitment or the permanent financing, if the borrower pursues an alternate transaction in which other lenders are engaged to provide financing for the acquisition. The specific terms of what type of transaction and/or alternate financing would require payment of the alternate transaction fee, as well as which fees and what percentage of those fees would be payable, are highly negotiated and may differ from deal to deal.

Market Trends

Documentation. The documentation for investment grade bridge facilities has tended to become less burdensome. Traditional market practice had been for the borrower to enter into a credit agreement with the lenders upon completion of syndication, with the credit agreement superseding the commitment letter provided at signing. Increasingly, syndication of the bridge commitments is documented through the commitment letter, rather than a credit agreement. In such cases, the parties will negotiate a bridge loan credit agreement only in the event that funding of the bridge facility appears likely to occur. By foregoing a credit agreement at the outset, the borrower is able to avoid a costly and potentially time-consuming negotiation process for an agreement that the parties do not expect to be needed for funding.

Committed financing. Interest rate margins and duration fees for bridge facility commitments have remained stable and competitive through year end 2017, aligning with continued strength in the bank debt market and capital markets generally during that period. Yet, those strong market conditions have generally not caused borrowers to forego bridge commitments to fund acquisitions, even though bridge facilities come at significant expense and companies have been able to access the capital markets without difficulty. There are exceptions, including for high investment grade companies and acquirors with sufficient capacity under an existing debt facility, or sufficient cash on hand, to fund the acquisition consideration. Under such circumstances, parties are more likely to conclude that a bridge facility backstop is not needed. Otherwise, however, acquirors and sellers continue to value a bridge facility as a backstop against market disruption or the acquiror suffering a material adverse change during the term of the acquisition agreement and to ensure available funds to close the transaction. It remains to be seen if a rising interest rate environment would affect the investment grade bridge loan market.

Non-bank lenders. We have not seen a trend of non-bank lenders taking lead arranger roles in the investment grade bridge market. This is in contrast to the below investment grade market where non-bank credit fund managers are moving up the league tables with larger market shares.

Conclusion

Bridge financing commitments in very large sums are available to investment grade companies. The closing conditions generally are limited, and within the control of the borrower or mirror those in the acquisition agreement so that the borrower does not find itself in a situation in which it is required to close the acquisition but does not have the funds to pay the purchase price. While the overall process is highly negotiated, certain conditions to funding, interest rate margins and duration fees have started to become more standardised across the market.

Endnotes

1. Investment grade companies are those that have "investment grade" credit ratings from the major rating agencies. This means, in the case of Standard & Poor's, a rating of BBB- or better, and in the case of Moody's, a rating of Baa3 or better.
2. The commitment letter typically will limit the borrower's damages if the lender fails to fund to direct damages. For a related recent case, see Weisfelner v. Blavatnik (In re Lyondell Chemical Co.), No 17 cv4375 (DLC), 2018 BL 24643, (S.D.N.Y. Jan. 24, 2018) (upholding damages limitation in credit agreement when lender refused to fund a draw under a revolving credit agreement).

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Chapter 23

Acquisition Finance in Latin America: Navigating Diverse Legal Complexities in the Region

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The continued demand by private equity and sophisticated strategic investors for loans with "certain funds" or "SunGard" limited conditionality to finance their M&A activity in Latin America warrants exploring the impact of certain legal complexities in the region on such acquisition finance structures. M&A activity in Latin America appears poised for growth, accompanied by other local trends that suggest increased opportunities for international lenders financing M&A activity in the region, presenting opportunities for investors and lenders. For any given acquisition finance transaction in Latin America, the parties will need to consider country-specific concerns, including guaranty limitations and security steps and timing, applicable withholding tax regimes and exchange control regulations, to determine the optimal structure and lender syndicate composition for such transaction.[1]

M&A in Latin America

Latin American M&A in 2017 included 583 announced deals for a total of US$80.1 billion of value, which was an increase in value of 3.6%, although two fewer deals, in comparison to 2016, with many of the deals continuing to be driven by energy, mining and utilities.[2] These deals also included an uptick of announced deals in the agricultural sector, including 18 deals valued at US$2 billion (an increase of four deals and 160.1% in value over 2016) and the leisure sector, including 26 announced deals valued at US$985 million (an increase of seven deals and US$584 million over 2016).[3] The Intralinks Deal Flow Predictor report predicts that the number of announced M&A deals in Latin America will increase in Q1 2018 by 3% year-on-year. And the International Monetary Fund is predicting that the GDP in Latin America will grow in 2018 by 1.9%, with country-specific variations (Argentina: 2.5%; Brazil: 1.5%; Chile: 2.5%; and Mexico 1.9%) and 3.5% growth projected in Colombia over the medium-term.[4]

Opportunities for Increased International Lender Activity in Latin America

Additional country-specific factors also suggest that in the near- and medium-term there will be increased M&A activity and increased opportunities for international lenders in financing M&A activity in Latin America.

- In Argentina, the federal government's launch of a huge infrastructure plan coupled with the lift of the legal and *de facto* foreign exchange restrictions applicable to cross-border financings seem poised to increase M&A in the country and the opportunities for off-shore lenders to finance that activity.
- In Brazil, although financing for acquisitions has traditionally been provided by local banks and local debentures with much support also being provided at below market levels by the National Development Bank ("BNDES"), BNDES' recent retreat from activity may create additional opportunities for off-shore banks. In this regard, BNDES has been gradually changing its credit portfolio over the past few years from a concentrated portfolio formed by large corporations (known as "Super Nationals") to a more diverse base, including venture capital and seed funds focused on start-ups and small-sized companies. In the near future, also, BNDESPar, the equity investment vehicle of BNDES, will play an important role in M&A activity in Brazil, either by divesting major equity stakes in large corporations or by investing in such small-sized companies mentioned above.[5] Brazilian corporates with US-dollar revenues, including, in particular, exporters of commodities, are the most likely borrowers of US-dollar off-shore debt, given that currency hedging costs may be prohibitive, but market participants continue to explore structures to minimise currency risk for Brazilian borrowers without significant US-dollar revenues.
- In Chile, the election of centre-right President Sebastián Piñera in December 2017 suggests even further increased opportunity for additional M&A activity in Chile, which closed 2017 with a record of 109 transactions.[6]
- In Colombia, the presidential elections in 2018 may lead to some slowdown in M&A activity during the year, but activity should remain in some sectors. Indeed, given the huge wave of road concessions together with a high sponsor concentration, it is expected that international investors will purchase stakes in these projects, which may require acquisition financing, depending on the stage of development of the relevant project. Additionally, multi-latinas continue to expand from and into Colombia and into the countries of the Pacific Alliance (Chile, Perú and México), which acquisitions typically rely on financings from both the international and the local banking markets.
- In Mexico, although political uncertainty, currency volatility and instability in the country's relationship with the US may signal general uncertainty for dealmaking within Mexico, Mexican companies have begun pursuing overseas transactions to secure investment in a more favourable climate, which will present opportunities. Investors will also continue to closely watch how President Donald Trump's policies toward Mexico unfold over the coming months, particularly his stance on the 23-year-old NAFTA agreement.
- In Peru, financing for acquisitions by foreign investors has traditionally been provided by off-shore lenders or affiliated companies. Local investors traditionally have preferred loans from local banks, including bridge loan to bond take-out structures. Recently, local investors with Peruvian

bank relationships have access to medium- and long-term acquisition finance structures through local banks and local investment funds, including mezzanine funds, are providing some acquisition financing to local investors. There have been discussions in political circles recently about eliminating the 18% VAT applicable to interest payments to foreign lenders that are not financial institutions, which would facilitate loans by such off-shore lenders to Peruvian investors, but the legislative change has not yet passed.

Latin American Acquisition Finance Transactions

Pure leveraged, limited-recourse acquisition loan finance transactions occur in Latin America less frequently than in the US or Europe. This is partly because the volumes of M&A activity in the region (US $100 billion in 2017) are still a fraction of US M&A activity (US $1.5 trillion in 2017) and European M&A activity (US $850 billion in 2017).[7] Country and currency risks specific to the region have also added to lenders' perceived risks of such limited-recourse loans. In addition, non-financial institution lenders, which are traditionally the lenders interested in providing term loan Bs, a preferred source of debt financing by private equity funds, have been relatively inactive in the region due to unfavourable local withholding taxes, which are often applicable in the region to off-shore lenders that are not financial institutions. And local banks have often been able to provide competitive pricing in this environment.

In our experience, international lenders have been more active in providing acquisition finance bridge loans in Latin America, which often take the form of bridge-bond take-out structures, and are frequently tied to M&A advisory mandates or other larger client relationships. Also, we have seen that Asian and European banks that are active in the medium- and long-term project finance markets have been active in leveraged acquisition financing – with project-finance-style debt-sizing parameters – of single-asset or portfolio power or infrastructure deals supported by US-dollar linked, long-term commercial contracts. Often, and in line with the business drivers of the international banks, we have seen that acquisition finance in the region has tended to be backed in whole or in part by corporate balance sheets, with customised, non-all-assets collateral packages when leverage exceeds 3.5 to 4.5 times EBITDA.

As private equity funds and other buyers seek loan financing for their targets in Latin America, cross-border acquisition loans will remain for the foreseeable future an important, if not critical, part of the capital toolbox. A buyer will generally require certainty of loan funds before committing to a purchase agreement, whether the acquisition loan financing takes the form of a bridge loan or longer-term financing, whether the target is a corporate or project, and whether the buyer is a strategic corporate or a private equity fund. The increasing volumes of M&A activity in the region, including in the energy, natural resources and infrastructure sectors in particular, would appear to be a promising source of highly bankable senior acquisition loans, with or without capital market take-outs.

Loans *vs*. Bonds

Loans tend to take centre stage in acquisition finance transactions because a loan commitment provides the needed certainty that debt funds will be available at closing. Typically, a purchase agreement for an acquisition will not include a "financing-out", *i.e.*, a right to terminate the purchase agreement if the buyer cannot finance the transaction, and before signing the purchase agreement the buyer will need certainty that the required debt will be available at closing.

Although an acquisition finance transaction may take the form of loans or bonds, it can be a challenge for a buyer to rely on a planned bond issuance to close an acquisition, given the notorious volatility of the capital markets. Buyers tend to rely on loan commitments from banks and other lenders to finance acquisitions, either in the form of term loans or bridge loans, which may be refinanced post-closing with a capital markets bond issuance.

Loan Commitment Documentation in the UK, Europe and the US

Conditionality

Because a purchase agreement for an acquisition will rarely contain a "financing-out", a buyer will want to ensure that its lenders have provided a loan commitment with limited conditionality before signing the acquisition agreement. In recent years, the conditionality of lenders' loan commitments in the acquisition finance context generally follows the "certain funds" standard in the UK and the European markets and the "SunGard" standard in the US. Under "certain funds" conditionality, the lenders' commitment to fund on the closing debt are subject only to: (i) the making of certain key representations; (ii) the absence of major events of default (including insolvency proceedings or payment defaults of the acquisition vehicle); (iii) the absence of illegality; (iv) the absence of a change of control; and (v) security being granted over certain assets of the acquisition vehicle, including the shares of the target being acquired. In contrast, the "SunGard" standard of conditionality limits the conditions such that: (a) the only representations that must be must be true and correct as a condition to funding are the specified loan agreement representations (limited largely to representations relating to corporate existence, power and authority, margin regulations, solvency and anti-terrorism and corruption laws) and the specified acquisition agreement representations (limited to representations and warranties in the purchase agreement relating to the target that, if untrue, would be material to the lenders and with respect to which the buyer can terminate its obligation to the close the acquisition); (b) the collateral in which a security interest must be granted and perfected at closing includes only collateral that may be perfected by the filing of a UCC-1 financing statement or the delivery of possessory collateral such as share certificates; and (c) the only material adverse change or material adverse event ("MAC") that is a condition to funding is the MAC[8] that applies in the purchase agreement – to eliminate any potential daylight between the loan commitment and the purchase obligation.[9]

Security Principles

Lenders in the UK, the European markets and the US markets also include in the commitment documentation an agreed description of the guaranty and security principles that will apply to complete the credit support package after closing. In the UK and the European markets, the guaranty and collateral package will vary considerably depending on the applicable jurisdictions involved, given wide variance in applicable guaranty limitations and security interest legal regimes in the region. In the US, the parties often agree to limit the collateral and guaranty package, such that no security interest is required to be provided in real property valued below a certain threshold, leased real property, motor vehicles, margin stock, interests in joint ventures (and possibly non-wholly owned subsidiaries) and other immaterial assets.

Commitment Documents in Latin America

The Latin American loan market generally follows the US loan market approach to loan documentation, rather than the UK or European approach, including with respect to commitment documentation.

Closing Date Collateral and Security Principles

Similarly, commitment documents with respect to acquisition finance transactions involving Latin American targets tend to follow the US "SunGard" standard of conditionality and US guaranty and security principles framework in the acquisition context. There are several challenges in using the "SunGard" standard of conditionality in Latin America, however, that require the description of closing date collateral in the conditions to closing and the security principles to be revisited.

In general, most Latin American jurisdictions do not have a construct to permit all asset security under a single document or to permit perfection by a single filing in a central filing system of varied security interests. Ordinarily, each category of collateral will require a separate security document and separate perfection steps. Notarisation and registration requirements (which require a registry to register collateral a number of days or weeks after filing, in particular for real estate) and fees may further complicate the process and make the taking of security more expensive and protracted, or outright prohibitive from a commercial standpoint.

If the acquisition target is located in Latin America, it will be important to understand, in each relevant jurisdiction (including each specific country and, sometimes, each applicable state within such country), what the target's valuable assets are given the nature of its business, the steps and timing (and related fees required) to create and perfect a security interest in each applicable category of such assets, and whether there are financial assistance (restrictions on the ability of a company to provide a guaranty in support of, or collateral to secure, indebtedness incurred to finance the purchase of that company) or other limitations on the ability of companies organised in that country to provide guaranties or credit support in the acquisition finance context. Care must be taken to formulate a closing date collateral package that will both ensure that the lenders have a security interest in the important assets of the target and ensure that perfection can be achieved on the closing date without execution risk and to frame the security principles and ongoing collateral package to protect the lenders' interest while managing transaction timing and expense. In contrast to the US market, there is no "standard" guaranty and collateral package for acquisition loans in Latin America. Such packages tend to vary from country to country and from industry to industry within each country depending on the requirements to create and perfect security interest in the assets key for that industry.

We have endeavoured here to provide an overview of considerations in several of the jurisdictions in which M&A activity and acquisition finance transactions have been active.

In Argentina, so long as a guaranty provides arm's-length benefit to the Argentine guarantor and the required corporate formalities are complied with, the guaranty will be enforceable, subject to potential avoidance, depending on the circumstances, if the guarantor enters into insolvency proceedings within two years of the guarantee being granted in the case of new debt. Also, the Argentine courts have held that some transactions in which a company has provided financial assistance to, or a guarantee for, the acquisition of its shares have violated the Argentine Commercial Companies Law ("ACC"), by violating the administrator's duties of loyalty and care and the restriction on companies giving financial assistance or providing guarantee in connection with the acquisition of their own shares. It is not possible under Argentine law for a company to grant a blanket security interest in all of its personal property assets and security will need to be provided under separate documentation for each category of collateral. Also, it is a challenge to obtain a perfected security interest in a bank account, which may require the construction of a trust and additional time and expense. Notary fees, stamp taxes and registration fees can be material in connection with secured transactions and will vary depending on the type of assets pledged and the location of the pledgor and its assets. Registration of some security interests may take between one and several months. Also, the concept of collateral agency is not recognised under Argentine law, so each of the lenders will need to directly be a party to the local security documents and intercreditor arrangements affecting local collateral. A bill is currently being discussed in the Argentine congress that, if adopted, would recognise the concept of collateral agency.

In Brazil, there is no requirement that a Brazilian guarantor receive corporate benefit provided that the required corporate formalities are complied with and, provided further, that a guarantee without sufficient corporate benefit may be avoided in an insolvency proceeding of the guarantor within two years of the guarantee being granted. It is not possible for a company to grant a blanket security interest in all of its personal property assets and security will need to be provided under separate documentation for each category of collateral. Fiduciary liens are the preferable security type for foreign creditors given the protection it brings in insolvency scenarios; although there has been a debate over the legality of fiduciary liens to the benefit of foreign creditors, in particular in connection with fiduciary liens on real estate due to certain restrictions on the ownership of real estate by foreign entities or individuals. Notary fees and registration fees can be material for the taking of security over real property and personal property pledges and will vary by the region where the registry is located. Registration of security can take up to one month, depending on the type of security interest being registered and the location of the registry. If the borrower has outstanding indebtedness with BNDES (subject to certain exceptions), the borrower will need a waiver from BNDES for additional indebtedness, which may take some time. Notably, recent changes to Brazilian law have enhanced the attractiveness of the Brazilian legal regime to international lenders. First, foreclosing on liens over shares of publicly traded companies and other financial assets (*e.g.*, time deposits) has become quicker. Also, Brazil has recently adopted the so-called "Apostille Convention", which should facilitate and expedite the recognition in Brazil of documents executed abroad, avoiding the need for the expensive and time-consuming "consularisation" procedure.

In Chile, so long as the guaranty provides some benefit to the Chilean guarantor and the required corporate formalities are complied with, the guaranty will be enforceable, subject to potential avoidance, depending on the circumstances, if the guarantor enters into insolvency proceedings within two years of the guarantee being granted in the case of new debt. Security should be created under separate documentation for different types of assets (under different categories of pledge depending on who will have possession of the pledged asset and the type of asset). Notary fees and registration fees may apply for the taking of security over real property and personal property pledges, and registration fees will depend on the applicable registry. There are also significant limitations on the effectiveness of security interests over bank accounts, which, in practice, render such security unavailable, and Chilean law does not provide for the existence of collateral trusts.

In Colombia, per a recent doctrine of the Superintendence of Corporations, a parent company may guarantee the obligations of its subsidiaries, even if the corporate purpose of the guarantor does not include such power. This doctrine should be applicable even when the target is the guaranteed company, provided that the entirety of the financing is destined to pay its purchase price. In all other cases (i.e. when a subsidiary is guaranteeing the obligations of its parent company or a sister company) so long as the Colombian guarantor's corporate purpose provides such company the power to guaranty the applicable obligations, the guaranty will be enforceable as a general principle (subject to certain exceptions including, for example, if the guarantor is a simplified stock corporation (*sociedad por acciones simplificada*), or if there is a declared entrepreneurial group between the guarantor and the guaranteed entity). There is generally no prohibition on a Colombian company providing financial assistance to support the acquisition of all of its own shares, except in the case of certain specially regulated companies such as banks, insurance companies and other finance companies. However, if the target is to guarantee a partial acquisition of its own shares, minority shareholder protection rules could apply and grant minority shareholders the right to challenge the guarantee provided by the target. Security should be granted under separate documentation for different types of assets. Alternatively, a *prenda sobre establecimiento de comercio* is available in some cases to cover groups of assets, as are security trust structures. There will be notarial fees and public registry costs depending on the type of security at issue.

In Mexico, so long as the required corporate formalities are complied with, a guaranty will be enforceable, regardless of the value provided to the guarantor, subject in any insolvency to potential clawback within 270 days of the filing for the insolvency proceedings. In Mexico, a non-possessory pledge on assets and rights may generally cover all assets, except real estate, which may need a separate document and filing. As an alternative, a Mexican collateral trust structure could be used to create a security trust structure covering a substantial number of assets, but the trustee costs are significant and administration of the collateral in the trust could become onerous for the borrower. Notary fees and registration fees may apply for the taking of security over real property and personal property pledges, and registration fees will depend on the applicable registry.

In Peru, so long as the required corporate requirements and formalities are complied with, a guaranty will be enforceable, regardless of the value provided to the guarantor, subject to potential actions against the officers and board members of the company under certain circumstances, including if the guarantees create a serious risk to the credits held by other creditors. Peru also restricts the ability of a company to provide financial assistance to a party to acquire its shares, although there may be structuring alternatives to reduce the impact of these Peruvian restrictions. Peru, in contrast to many other Latin American jurisdictions, does permit a blanket security interest under a *Hipoteca sobre Unidad de Producción*, under the applicable rules provided by Peruvian Civil Code, which covers a whole production unit including different types of assets (equipment, machinery, real estate, inventory and spare parts). As an alternative, lenders and holders of debt instruments may rely on the Peruvian guarantee trust structure (Fideicomiso en Garantía), governed by the banking law (*Ley del Sistema Financiero y del Sistema de Seguros y Orgánica de la Superintendencia de Banca y Seguros*) and the regulations issued by the banking regulator (the Superintendencia de Banca, Seguros y AFP), as well as on the securitisation trust (*Fideicomiso de Titulización*), regulated by the capital markets law (*Ley del Mercado de Valores*) and the regulations issued by the securities market regulator (*Superintendencia del Mercado de Valores*). The *Fideicomiso en Garantía* could be used to create a security trust structure covering a substantial number of assets, including future cash flows, with expedited enforcement proceedings and other benefits. The *Fideicomiso de Titulización* is a trust structure that also may cover different types of assets, including the future cash flows, aimed to guarantee the offering and issuance of debt instruments in the local and/or the international markets. There have been issuances of securitisation notes (*Bonos de Titulización*) that have been structured to finance future acquisitions by local investors, who act as originators of the respective *Fideicomiso de Titulización*. Notarial fees will be required to formalise the security agreements as public deeds and the applicable fees will depend on the notary. There are also public registry costs.

Other Latin American Structuring Considerations

In addition to the issues of the closing date and the ongoing credit support package, which are generally addressed in the commitment letters for an acquisition finance loan in the UK and the European and the US markets differently and need to be addressed in the Latin American market on a bespoke basis, there are also distinct issues in Latin American jurisdictions that may impact acquisition finance transactions and which are not typically addressed in the UK, the European or the US commitment letters.

Withholding Tax and other Tax Considerations

The parties will need to consider, in particular, applicable withholding tax obligations and the agreements with respect to tax gross up by the borrower. In many Latin American jurisdictions, a significant withholding tax will apply to interest payments from Latin American corporate borrowers to off-shore lenders, particularly lenders that are not regulated financial institutions or lenders organised in certain locally designated "tax haven" jurisdictions.

For example, in Argentina, if a foreign Lender is a bank or financial institution under the supervision of the relevant central bank or equivalent authority of its jurisdiction and located in a "cooperative jurisdiction" or a jurisdiction that is party to an exchange of information treaty with Argentina, there will be an effective withholding tax rate of 15.05%; otherwise, the effective withholding tax rate is 35%. Also, double taxation treaties may set forth ceilings to the applicable rates. The borrower may also need to pay VAT at the rate of 21% or 10.5% depending on whether the lender is a financial institution and other factors. And there may also be applicable stamp taxes in connection with the execution of the loan agreement, promissory notes and other loan documents depending on where the applicable agreement is signed are signed and/or causes effects, and the applicable industry.

In Brazil, payments of interest to non-residents are generally subject to a 15% withholding tax, which may be reduced in the case of an applicable double taxation treaty in effect between Brazil and the country in which the foreign investor is located or increased to 25% in the case of an investor located in a tax haven jurisdiction, according to a list issued by the Brazilian tax authorities.

In Chile, interest payments by a Chilean borrower to an off-shore lender will be subject to a 35% withholding tax; provided that a reduced 4% withholding tax rate will apply to interest paid to foreign banks or financial institutions, and there may be a reduced rate also if there is an applicable double taxation treaty. In addition, there may be applicable stamp taxes proportional to the principal of the loan or bonds in connection with the execution of the loan agreement or a bond issuance. In Colombia, interest payments to off-shore lenders will be subject to a withholding tax of 14% if the loan from off-shore lenders has a term equal to, or longer than, one year, or 33% if the term is less than one year, subject in each case to the potential application of double taxation treaties as applicable depending on whether the lender is a financial institution.

In Colombia, interest payments to off-shore lenders are generally subject to a 15% withholding tax rate, subject to a number of exceptions. For example, loans provided by lenders located in jurisdictions with which Colombia has a double taxation treaty generally benefit from a lower rate ranging from 0% to 5% depending on the country. However, if a lender is located in a tax haven jurisdiction, the applicable rate is increased to 35%.

In Mexico, interest payments to off-shore lenders are generally subject to a 4.9% withholding tax rate in the case of interest paid to certain financial institutions that are residents of a country that has entered into a tax treaty with Mexico, a 10% withholding tax rate in the case of interest paid to certain financial institutions that are not residents of a tax treaty partner of Mexico, a 15% withholding tax rate in the case of interest paid to reinsurance companies or interest derived from financial leases, a 21% withholding tax rate in the case of interest paid to sellers of machinery in connection with a sale on credit, a 35% withholding tax rate in the case of interest paid to other lenders and a 40% withholding tax rate in the case of interest paid to a related party located in a tax haven.

In Peru, interest paid to off-shore lenders will be generally subject to a 4.99% withholding tax (*Impuesto a la Renta*), provided that certain formalities are complied with regarding funding and the corporate purpose of the loan. However, if the off-shore lender is a related party of the borrower or the issuer of the applicable debt instrument or if the lender or the investor on the applicable debt instrument is an individual domiciled in a tax haven, the withholding tax rate is 30%. Interest on debt instruments issued by local issuers acquired by foreign companies, investment funds, trusts and other entities domiciled in a tax haven, or on loans provided by such entities, are subject to the 4.99% withholding tax rate, provided that the respective investor or lender, as the case may be, is not a related party to the local borrower or issuer. Early prepayment premiums may also be subject to such withholding tax.

In Peru, in addition to withholding taxes, VAT (*Impuesto General a las Ventas*) may also apply. Interest on loans granted by foreign banks and other regulated financial entities will not be subject to the Peruvian 18% VAT. If the loans are provided by an off-shore entity that is not a regulated financial entity, including a corporation, the applicable interest payments will be subject to such VAT. In the case of notes and other debt instruments that constitute *valores mobiliarios*, which requires that the issuance include 10 or more instruments, issued by public or private offering by local issuers, the interest paid to foreign investors, including those domiciled in tax havens, will not be subject to the VAT. In addition, the VAT will not be applicable to interest payable under local instruments that constitute *títulos valores*, which require that the public offering and placement be through the Lima Stock Exchange.

Foreign Exchange Controls

Similarly, foreign exchange controls may require specific structuring to comply with local requirements. Foreign exchange controls are various forms of controls imposed by a government on the purchase or sale of foreign currencies by residents or on the purchase or sale of local currency by non-residents.

In Argentina, the foreign exchange controls applicable to cross-border financings have recently been lifted, allowing disbursements to be made and kept abroad, and conversion from Argentine Pesos to US Dollars to repay or prepay financings before or after collateral enforcement.

In Brazil, remittances from Brazil to off-shore lenders will need to be registered in the Brazilian Central Bank's system. Further authorisation by the Central Bank may be required for the conversion of such Brazilian currency-denominated amount into foreign currency and its remittance abroad upon the occurrence of certain macroeconomic events (*i.e.*, disequilibrium in the balance of payments), but the Brazilian Central Bank has shown less strict foreign exchange enforcement over time, and there is no known precedent in which Central Bank authorisation has been required in the past decades. Although the repayment of a loan by a Brazilian company is not subject to the financial transactions tax, such tax may become payable on the closing of a foreign exchange transaction for the inflow of funds into Brazil on the granting of the loan, depending on the amortisation term of the principal; under current law such tax is payable at a 6% rate if the term of the loan is fewer than 180 days, and 0% if the term of the loan is equal to or greater than 180 days.

Chile has no applicable currency control issues, and the exchange rate under which Chilean pesos would be converted to US dollars, or *vice versa*, may be freely agreed upon between the parties, provided that, in extreme cases, the Central Bank may intervene to regulate such conversion rates.

In Colombia, the foreign exchange regulations require foreign lenders to have a Central Bank code and require notifying the Central Bank of disbursements on a loan with non-Colombian lenders and of remittance of funds abroad to repay a loan with non-Colombian lenders. Repayment of loans to foreign lenders also must be made through specified foreign exchange intermediaries or compensation accounts, which are off-shore bank accounts that are registered with the Central Bank and subject to specified reporting obligations, and set-off by the lenders will not be permitted.

In Mexico and Peru, there are no applicable currency controls.

Conclusion

Given the tremendous opportunities for Latin American M&A activity in the coming years and the important role of loan facilities in financing acquisitions, understanding the local laws applicable to acquisition financing transactions in Latin America will be critically important to market participants going forward.

Endnotes

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market matters, Carlos Saco-Vertiz Tudela, Partner, Sacovertiz & Landerer Abogados.

2. Global and Regional M&A Report FY 2017 by *Mergermarket*, An Acuris company.
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4. World Economic Outlook, October 2017, "Seeking Sustainable Growth: Short-Term Recovery, Long-Term Challenges", dated October 10, 2017 by the International Monetary Fund.
5. http://economia.estadao.com.br/noticias/geral,apos-politica-das-campeas-nacionais-bndes-quer-impulsionar-as-pequenas,70002142089.
6. Landmark Alantra Group.
7. "*Fusiones y adquisiciones cierra 2017 con 109 transacciones: duplica las de 2014*", by Landmark Alantra Group, *Diario Financiero*, January 3, 2018.
8. A MAC condition in a purchase agreement is typically much narrower than a typical MAC condition in a loan agreement and will specifically exclude any changes from market and economic conditions, for example. Agreeing to use the purchase agreement MAC limits the lenders' ability to refuse to fund their commitments under conditions where they might otherwise not be obligated to fund under a typical loan agreement outside of the acquisition context.
9. The UK and European certain funds requirement notably does not include the equivalent of the MAC condition, given that there is rarely a MAC condition to the obligation to close the purchase under a typical purchase agreement in those markets.

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WHITE & CASE

White & Case's Latin America practice has more than 100 lawyers focusing and practising in the region across offices in New York, Miami, Washington DC, Madrid, and on the ground in Mexico City and Sao Paulo. We have an extensive track record of representing lead arrangers/agents and credit parties in the most complex, high-value cross-border finance transactions in Latin America, as well as advising on high-profile cross-border M&A deals. Clients value our regulatory knowledge, practical know-how and significant transactional experience gained through our longstanding presence in the region: in the last 40 years, we have won over 100 'Deal of the Year' awards in Latin America, and White & Case currently holds top tier rankings in *Chambers Latin America* for all main areas of business law, including Band 1 rankings for Banking & Finance and Projects. As a pioneering and truly international law firm, our cross-border experience and diverse team of local, US and English-qualified lawyers consistently deliver results for our clients in both established and emerging markets.

The Mid-Market and Beyond

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Against a backdrop of a bifurcated 2016, which started slowly and built up half way through the year, 2017 provided a stark contrast by increasing on the heady numbers of 2007. S&P's Global Market Intelligence service, LCD, reported full-year leveraged loan volume reached c. $782 billion globally (compared to the $754 billion of 2007) and even cross-border volumes were at $110 billion compared with $84 billion in 2007. In particular, the relative attractiveness of the European market for sponsors continued with the European market share of cross-border transactions being 142% higher than that of 2007, contrasting with the US market share which grew by only 3%. Whilst over 57% of leveraged loan volume in 2017 was opportunistic and geared towards refinancing, repricings and dividends in Europe, the equivalent number in the US market was just below 50%, down from figures reported by Thomson Reuters of nearer two thirds for 2016. While market commentators have posited as to the impact of Brexit, the leveraged lending guidelines, US elections, rising interest rates or reduced ECB and Bank of England intervention, the continued abundance of supply and the desire for returns and to deploy large amounts of capital appears to be driving both the credit and M&A markets forward, with unexpected economic performance metrics globally further lessening the likelihood of any imminent slowdown. Instead, margins remain very tight and loan terms in the mid-market are moving ever closer to their large-cap counterparts as sponsors and borrowers take advantage of burgeoning supply and competitive tension to loosen documentary protections that have been customary in mid-market transactions in the past to reflect the increased risk in locking up capital with smaller EBITDA generating companies.

Background

The increased rise in private debt and direct lending has been well publicised. The relative regulatory-lite forum that such institutions operate in has lent itself to significant flexibility from an execution and terms perspective. Direct lending is not subject to the time and process constraints of the 'distribution model' of syndication and there are often no ratings or marketing materials and no lengthy syndication processes to move through. When coupled with the ability to write increased cheque sizes it is easy to understand why many mid-market sponsors are looking to the direct lending markets for flexibility on terms even where the investment banks are able to offer what is substantially lower pricing. Even that price differential has been reduced in recent times as asset managers raise more funds targeting senior-like returns. Given their constraints around leverage and process, the investment banks in the mid-market have sought to revisit documentary terms with a view to moving towards those terms accepted by the direct lending community. Combined with the more general rise to prominence of incurrence covenants, the banks appear even further inclined to at least consider the terms more commonly accepted by direct lenders. This inter-creditor dynamic makes it easy to see why the current market favours the sponsors, who have been provided with a meaningful variety of financing options, whether in respect of obtaining a covenant-lite financing or finding a solution which provides increased leverage and flexibility for a credit with a more challenging story.

Pricing

Despite the compression of margins, the non-amortising nature of the oft-used TLB has led to sponsors to look for ways to reduce their indebtedness costs, whether by repricing, reducing the impact of prepayment protection (see below) or optimising their ability to take advantage of the margin ratchet. With limitations on the use of that ratchet previously ranging from 6–12 months post initial funding of the deal, now there are a greater number of deals in the market, particularly in the mid-market space, which look to reduce the minimum period during which the margin ratchet cannot be used and, in the case of no minimum period, use a closing date certificate to evidence any day one margin reductions. In the past, credit funds have been reluctant to accept no minimum period before the margin ratchet becomes available so as to guarantee certain required returns from the fund's perspective but in an increasingly competitive landscape some have been willing to live without this, possibly due to their confidence in the way they have underwritten the credit and satisfaction with the base case model. Some creditors have resisted this, arguing that if they are subject to a financial covenant holiday then the borrower should be subject to an equivalent period for the ratchet. In the other direction, the reversion to the highest level previously brought about by the occurrence of any Event of Default is now only possible if certain 'material' Events of Default are triggered. Coupled with reducing fees (down to 30% on undrawn commitment fees and a reduction in some fronting/issuing bank fees) and the 'zero floors' across European deals, the net yield to investors is an area which has been subject to considerable erosion throughout 2017, including in the mid-market space. Adding the reduced (or, in the direct lending space, non-existent) flex requirements, the reduced requirement for mandatory hedging and the tightening of OID spreads, and the overall picture is one of cheaper execution costs to the sponsor. It is worth noting here that the prevailing interest rate environment in Europe has continued to make it an attractive source of financing even for US borrowers and 2017 saw a continued growth across that metric.

Prepayment Protection

For direct lenders in particular, net returns form a key part of the investment thesis. Protection of those returns across the European mid-market, particularly for institutional investors, had been a prevalent feature of credit markets throughout all of 2016, with short-term soft-call protection typically afforded only to the large-cap syndicated deals. This position deteriorated for those investors within larger sponsor-led mid-market deals across 2017, with many moving toward the six-month soft-call protection (with certain exclusions) and a number benefitting from no call protection at all (albeit often subject to a flex right). Whilst soft call 101 protection is typically reserved for the higher echelons of the mid-market, many direct lenders and credit funds have seen a push back on the hard prepayment premia of 12 months ago which they used to mitigate their reinvestment risk. Although not yet in the realms of soft-call protection, direct lenders have seen the 2–3 years of hard call protection eroded away. In any event, those 'more challenging' transactions which include the more customary call protection are rarely as expensive to refinance as would be the case for a second lien or bond financing. Alongside eroded up-front prepayment premia, the markets also seem to be asking for increased flexibility in documents as to the prepayment of *pari passu* and even junior indebtedness (whether or not ahead of the senior secured indebtedness) provided that the opening first-lien or senior secured leverage is not exceeded.

Quantum and Indebtedness

In view of the long-term financing aims achieved by using TLB, and the readily available access to new debt, one particular area of focus for sponsors has been that of incremental debt capacity. This is particularly the case in the mid-market where sponsors are often making acquisitions with a 'buy-and-build' strategy to increase their returns. This is an area where the direct lending institutions have again been able to offer increased flexibility as they are not subject to the leveraged lending guidelines in the US and European markets. Thus, not only has the quantum of debt which is permitted by the documents increased (including the increasing prevalence of some form of 'freebie' in the direct lending space), the flexibility afforded to the sponsor has made the use of such debt more practical due to reduced conditionality. For example, the MFN clauses which offered pricing protection to existing lenders are now subject to a short (often only six-month) sunset, where the need for new financing seems less likely. By the time carve outs to the MFN including non *pari passu* debt, non-term debt and bridging debt are taken into the account, the MFN does not afford a huge amount of lender protection. Many credits also have the MFN running off opening margin instead of the all-in-yield. The 'ROFO' and 'ROLL' rights for existing creditors to participate in new financings seem to have all but disappeared, with the accepted reality being that the existing creditors and their familiarity with that credit are likely to yield the most favourable (and time-efficient) means of access to additional indebtedness.

Dividends and Restricted Payments

The ability of sponsors to return capital on their investment prior to maturity remained a key area of negotiation. Whilst there has been a shift towards convergence with the terms of large-cap transactions, the mid-market has remained more static on the whole, with focus on significant de-leveraging before uncapped basket capacity becomes available and 'available amount' or 'builder baskets' (which are again seen more in the top end of the mid-market) again subject first to significant reduction in leverage. Arguments over the reclassification of payments out are a key theme in these discussions and the flexibility seen in the high-yield markets has not yet become common in the mid-market space.

Acquisitions

Throughout 2017, the continuing theme has been a movement of the mid-market towards the large-cap space with some deals not having any hard monetary cap for acquisitions. Earn-outs and the ability to include them continues to be a thematic ask from sponsors from the large-cap space participating in mid-market deals, together with the flexibility of 'limited conditionality' transactions. This links interestingly with the US market where this type of 'LCT' testing has become more commonly accepted. Notably, however, the historic mid-market conditionality around acquisitions such as look-back and look-forward covenant testing, diligence and other reporting and hard caps has become slowly eroded over the course of 2017 to bring it more into line with the large-cap terms.

Financial Covenants and Definitions

Those deals which were able to satisfy CLO requirements by availing themselves of some form of maintenance covenant have also been subject to a less effective early warning signal of balance sheet issues. While springing covenant headroom is increasingly set around the 35% or above level and that covenant only 'springs' where, in many cases, cash drawings under the revolver are above an agreed level, it is likely that things are very bad indeed by the time this covenant is ever tripped. The increasing ability to incur additional revolving flexibility which does not count towards any 'springing' test makes it even more difficult for such a covenant to be tripped. For the direct lenders there continues to be a disinclination to forego a maintenance financial covenant or to adopt more incurrence-based or bond-like covenants and most lenders will achieve a leverage covenant in the lower-and middle parts of the mid-market and in direct lending transactions. The number of step-downs in these covenants remains highly negotiated but the sponsor ask for a relatively high flatline (given the non-amortising nature of the debt) remains common.

A further shift in the dynamic around financial covenants is with respect to those financial definitions used to build the leverage covenant. The financial definitions in documents have been ameliorated from the sponsor's perspective to provide significant flexibility which is not part of general accepted accounting principles. In particular, the advent of run-rate EBITDA cost-savings adjustments and other newly-seen adjustments which are used not only for cost-savings and synergies but for projected unproven results provide sponsors with increasing flexibility without corresponding visibility on financial performance for lenders. Caps for internal and external verification have been increasing over the past 18 months to fall more in line with the large-cap deals, as have cost-savings and synergies realisation periods although the mid-market has generally maintained an overall cap on such cost-savings and synergies. The ask from sponsors to grow 'baskets' based on these unproven results and to incur liabilities on those 'adjusted' numbers is increasing. For the stronger credits, run-rate adjustments are sometimes accepted.

For equity cures, the market is shifting towards a blend of typical sponsor friendly US and European elements, with EBITDA cures more customarily accepted and some sponsors pushing for consecutive cures. A deemed cure for any prior financial covenant breach is a more regular ask and the permission to overcure is now well-heeled in Europe. A less accepted ask is to be able to effect any cure using 'Group' monies as opposed to those of the sponsor; taken with the ability to draw the revolver for any purposes, this is a difficult ask for lenders in the wake of the more limited downside protection they are afforded. The use of the 'Group' revolver more generally and its position as an 'Acceptable Funding Source' also remains a highly negotiated item.

Reporting

While many sponsors are pushing to provide three sets of quarterly financial statements and then annual statements to avoid the need to produce a fourth quarter unnecessarily, many creditors are resisting this to mitigate issues around the length of time to deliver audited financials, something which is related also to the testing of financial covenants. Timing around monthly financials (or their complete removal in some of the larger mid-market transactions) and budgets is sometimes being extended on a deal-by-deal basis, particularly within a buy-and-build strategy.

Transfers

Direct lenders not relying on any syndication and not subject to the same policy restrictions around freedom of transferability post Event of Default have seen a restricted ability to transfer without consent. The fact that many direct lenders will hold all, or substantially all, of the debt and are focused on returns over the life of the credit has allowed sponsors to ensure that such loans are increasingly illiquid. Industrial competitors and synonymous groups are now frequently completely excluded from any transferability regime. The list of Events of Default which allow for free transferability (which used to be any Event of Default) has been reduced over the course of the last 12–18 months. Sponsors, in an attempt to protect themselves in the downside case, will look to prohibit transfers to loan-to-own investors. Whether there is an absolute prohibition (as now seen on industrial competitors) or an ability to make such transfers only after certain 'material' Events of Default remains a point for negotiation. More careful thought has been given to voting thresholds, with the position in some mid-market transactions moving to match the US market more commonly seen to utilise a 50.1% threshold in order to ensure that one or two holders would find it more difficult to dictate outcomes. There remains some atrophic concerns about junior creditors with cross-holdings but those have largely not been legislated for, given the institutional investor base more readily inclined towards TLB or even second-lien.

Conclusion

Overall, market appetite continued to drive loose covenant packages across the large-cap and mid-market spaces in 2017, with the flexibility more commonly found in historic large-cap transactions now becoming more normative across the upper and middle mid-market. The race for yield remains ultra-competitive and while direct lenders have benefitted from the increased regulation of their investment banking counterparts with respect to regulatory capital and underwriting space, the investment banks are still providing large funding pipelines at lower pricing and on terms which are becoming increasingly more favourable to sponsors and matching those accepted by the direct lending community. The advent of new and larger funds being raised by asset managers is likely to mean that the opportunities which previously favoured banks over direct lenders owing to size constraints will become more and more accessible to the upper echelons of the direct lending market. For the more complex credits from a traditional cashflows perspective, and those which can still satisfy a covenant but which require more complex structuring, the flexibility of direct lending continues to provide a competitive edge. Whether direct lending succumbs to covenant-lite lending outside of one or two market outliers shall remain to be seen. What is clear is that the mid-cap and large-cap leveraged lending markets have, in large part, converged on their terms at the same time as tightening their pricing. This has afforded sponsors with a raft of financing solutions which can be utilised across a variety of structures, in turn leading to increased activity across both the bank and direct lending markets in the search for returns. The continued concern around Brexit is also likely to continue to comfort direct lenders that derive their capital in dollars *versus* certain investment banks, particularly if direct lenders continue to benefit from reduced regulation. The age-old danger remains that with such loose documentary control, a successful financial restructuring in a downside scenario with optimised output for all stakeholders becomes an increasingly challenging outcome. As a result, the key focus for creditors now seems to be on the quality of the underlying credit, rather than on any documentary downside protections.

Acknowledgment

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Andorra

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1 Overview

1.1 What are the main trends/significant developments in the lending markets in your jurisdiction?

There are no significant developments to consider.

1.2 What are some significant lending transactions that have taken place in your jurisdiction in recent years?

Normally, lending transactions in Andorra involve both domestic and foreign lenders and the collateral securities are usually granted over shares and receivables or over real estate properties, as well as personal guarantees granted by the borrowing party.

2 Guarantees

2.1 Can a company guarantee borrowings of one or more other members of its corporate group (see below for questions relating to fraudulent transfer/financial assistance)?

Yes, without prejudice to the restrictions mentioned in the section regarding financial assistance and the considerations contained in question 2.2 below.

2.2 Are there enforceability or other concerns (such as director liability) if only a disproportionately small (or no) benefit to the guaranteeing/securing company can be shown?

According to the Andorran Companies Act, the directors have a duty of diligence towards the company. Furthermore, a resolution passed by the general meeting might be challenged if it is considered that it prejudices the company's interests for the benefit of one or more shareholders or of a third party. In such events, the resolution might be annulled.

2.3 Is lack of corporate power an issue?

Yes, in Andorra the representative of a party to a contract must be duly empowered to act on its behalf.

2.4 Are any governmental or other consents or filings, or other formalities (such as shareholder approval), required?

In general terms, there are no specific requirements concerning governmental authorisations or consents. For transactions outside the ordinary course of business of a company, the authorisation of the general meeting is customarily obtained.

2.5 Are net worth, solvency or similar limitations imposed on the amount of a guarantee?

No, without prejudice to the restrictions mentioned in the section regarding financial assistance and the considerations contained in the answer to question 8.2 concerning guarantees granted by an insolvent company or person.

2.6 Are there any exchange control or similar obstacles to enforcement of a guarantee?

No, there are not.

3 Collateral Security

3.1 What types of collateral are available to secure lending obligations?

The most common types of collateral to secure lending obligations are classified into: (i) personal guarantees, such as bails granted by a third party that acts as guarantor or guarantees on first demand, on which there is not express regulation but that have been admitted by the Andorran courts; and (ii) *in rem* security interest, the most common being mortgages over real estate property and pledges over movable assets with transfer of possession.

3.2 Is it possible to give asset security by means of a general security agreement or is an agreement required in relation to each type of asset? Briefly, what is the procedure?

Under Andorran law, it is not possible to give asset security by means of a general security agreement. In order to create security over specific assets, it is necessary to constitute mortgages or pledges in accordance with the nature of the asset that will be granted as security. With respect to mortgages, it is required to constitute them by means of a public deed. With respect to pledges, even if their constitution is not required to be done by means of a public deed, it is highly advisable to do so in order to ensure their efficacy in front of third parties. Furthermore, pledges normally require the transfer of possession over the collateral.

3.3 Can collateral security be taken over real property (land), plant, machinery and equipment? Briefly, what is the procedure?

In Andorra, mortgages cover the land and the buildings built on it. According to the doctrine, and by virtue of the principle of freedom of contract, a mortgage can be extended to other properties physically bound with the main mortgaged asset.

3.4 Can collateral security be taken over receivables? Briefly, what is the procedure? Are debtors required to be notified of the security?

Andorran doctrine and practice recognise the possibility of taking a security over receivables. Furthermore, there is a judicial precedent in which this type of security has been implicitly recognised.

A security over receivables could be taken by means of a pledge, constituted through the granting of a public deed in front of an Andorran notary.

In accordance with the Andorran practice, notification to the debtor is required in order for the pledge to be perfected.

3.5 Can collateral security be taken over cash deposited in bank accounts? Briefly, what is the procedure?

Yes, this type of collateral security can be taken by means of a pledge over a bank account, which, as in the case of security over receivables, must be constituted by means of a public deed granted in front of an Andorran notary. In this case, it is also necessary to notify the depositary bank about the existence of the pledge.

3.6 Can collateral security be taken over shares in companies incorporated in your jurisdiction? Are the shares in certificated form? Can such security validly be granted under a New York or English law governed document? Briefly, what is the procedure?

Yes, a collateral security can be taken over shares of Andorran companies. Such collateral must also be constituted by means of a public deed granted by an Andorran notary.

In accordance with article 15 of the Companies Act, the shares can be documented by means of nominative titles.

This type of security must be granted under Andorran law-governed documents.

Besides the above-referred notarisation, the pledge must be registered in the relevant public deeds of acquisition of the shares affected by the pledge and in the Registry Book of Shareholders.

3.7 Can security be taken over inventory? Briefly, what is the procedure?

To our knowledge, this type of security is not used in Andorra considering the nature of securities available and the lack of transfer of possession.

3.8 Can a company grant a security interest in order to secure its obligations (i) as a borrower under a credit facility, and (ii) as a guarantor of the obligations of other borrowers and/or guarantors of obligations under a credit facility (see below for questions relating to the giving of guarantees and financial assistance)?

Yes, without prejudice to the restrictions mentioned in the section regarding financial assistance and the considerations in the answer to question 2.2.

3.9 What are the notarisation, registration, stamp duty and other fees (whether related to property value or otherwise) in relation to security over different types of assets?

Notarisation fees are fixed by the Andorran Government and are established proportionally to the amount of the document to be notarised. In the case of securities, the fees are generally calculated over the amount of the secured liability.

The Andorran equivalent of value added tax is applicable to notarisation fees.

3.10 Do the filing, notification or registration requirements in relation to security over different types of assets involve a significant amount of time or expense?

In general terms, the amount of time required in order to notarise a security is not significant. The related expenses depend on the amount of the secured liability, as mentioned in the answer to question 3.9 above.

3.11 Are any regulatory or similar consents required with respect to the creation of security?

No, in general terms there are not.

3.12 If the borrowings to be secured are under a revolving credit facility, are there any special priority or other concerns?

No, in general terms there are not.

3.13 Are there particular documentary or execution requirements (notarisation, execution under power of attorney, counterparts, deeds)?

Please see the answer to question 3.2. Power of attorney must also be notarised.

4 Financial Assistance

4.1 Are there prohibitions or restrictions on the ability of a company to guarantee and/or give security to support borrowings incurred to finance or refinance the direct or indirect acquisition of: (a) shares of the company; (b) shares of any company which directly or indirectly owns shares in the company; or (c) shares in a sister subsidiary?

(a) Shares of the company

Andorran companies, excluding banking institutions and other entities that integrate the Andorran financial system and are allowed to enter into credit transactions with third parties, may grant financial assistance to acquire their own shares or to accept them as security within the limit of 10% of the share capital of the company and as long as: (i) the assistance is charged against distributable profits and unrestricted reserves; (ii) the general meeting authorises the transaction and the maximum amount of shares that can be acquired and their maximum price; and (iii) the company establishes a reserve in its balance sheet equivalent to the amount of its credits or to the value of the shares accepted as security.

(b) Shares of any company which directly or indirectly owns shares in the company

Even if the Companies Act does not provide for a specific prohibition for this type of financial assistance, the prohibition of establishing reciprocal participations at a percentage higher than 10% leads one to believe that the restrictions referred to in (a) above can be equally applicable in this scenario.

(c) Shares in a sister subsidiary

Please see point (b) above.

5 Syndicated Lending/Agency/Trustee/Transfers

5.1 Will your jurisdiction recognise the role of an agent or trustee and allow the agent or trustee (rather than each lender acting separately) to enforce the loan documentation and collateral security and to apply the proceeds from the collateral to the claims of all the lenders?

There are no precedents that may confirm whether such figures would be recognised by the Andorran courts under secured lending structures.

5.2 If an agent or trustee is not recognised in your jurisdiction, is an alternative mechanism available to achieve the effect referred to above which would allow one party to enforce claims on behalf of all the lenders so that individual lenders do not need to enforce their security separately?

Even if there are no judicial precedents that confirm its validity under Andorran law, and following recent trends in neighbouring countries, a parallel debt clause under the loan – which should be subject to a governing law that recognises such figure – could be used to grant Andorran securities directly to the trustee acting on behalf of the lenders.

5.3 Assume a loan is made to a company organised under the laws of your jurisdiction and guaranteed by a guarantor organised under the laws of your jurisdiction. If such loan is transferred by Lender A to Lender B, are there any special requirements necessary to make the loan and guarantee enforceable by Lender B?

Given the ancillary nature of securities with respect to the secured obligation, the assignment of a loan will normally entitle the transfer of the securities attached to it. However, considering the formal requirements applicable to securities in Andorra, and in particular to mortgages and pledges, it would be necessary to formalise such assignment by means of a public deed in order to ensure its efficacy in front of third parties.

6 Withholding, Stamp and Other Taxes; Notarial and Other Costs

6.1 Are there any requirements to deduct or withhold tax from (a) interest payable on loans made to domestic or foreign lenders, or (b) the proceeds of a claim under a guarantee or the proceeds of enforcing security?

Interest payments made to foreign lenders may be made without deduction or withholding on account of the Andorran Non-Resident Income Tax, given that the relevant law establishes a general exemption over interests when the payer is a resident of Andorra or when the interest arises from capital used in Andorra. Concerning interest payments on loans made to domestic lenders, if the lender is: (i) a company, there are no applicable deduction or withholding tax requirements (although interests are taxable); or (ii) an individual, and the paying party (a company or an individual acting in the course of its business) resides in Andorra, there is a withholding requirement for personal income tax at a rate of 10%.

6.2 What tax incentives or other incentives are provided preferentially to foreign lenders? What taxes apply to foreign lenders with respect to their loans, mortgages or other security documents, either for the purposes of effectiveness or registration?

Please see the answer to question 6.1 above. There are no taxes for the purposes of effectiveness or registration.

6.3 Will any income of a foreign lender become taxable in your jurisdiction solely because of a loan to or guarantee and/or grant of security from a company in your jurisdiction?

No, it will not.

6.4 Will there be any other significant costs which would be incurred by foreign lenders in the grant of such loan/guarantee/security, such as notarial fees, etc.?

Please see the answer to question 3.9 above.

6.5 Are there any adverse consequences to a company that is a borrower (such as under thin capitalisation principles) if some or all of the lenders are organised under the laws of a jurisdiction other than your own? Please disregard withholding tax concerns for purposes of this question.

No, there are not.

7 Judicial Enforcement

7.1 Will the courts in your jurisdiction recognise a governing law in a contract that is the law of another jurisdiction (a "foreign governing law")? Will courts in your jurisdiction enforce a contract that has a foreign governing law?

Yes, considering that there is no specific prohibition which bans the contracting parties to submit disputes arising from a contract to a specific law (except when a law provides the specific designation of Andorran law such as disputes arising from rights *in rem* over immovable properties located in the Principality of Andorra, lease contracts over properties located in the Principality of Andorra, and labour disputes, among others).

The Andorran courts would enforce contracts subject to a foreign governing law as long as (i) they are not related to matters which are submitted to the Andorran law by a mandatory rule, (ii) the foreign law does not contradict Andorran public policy, and (iii) the claiming party proves during the trial the content and validity of the applicable foreign law.

7.2 Will the courts in your jurisdiction recognise and enforce a judgment given against a company in New York courts or English courts (a "foreign judgment") without re-examination of the merits of the case?

Yes, as long as it is not considered by the Andorran courts that there is a lack of reciprocity between the Principality of Andorra and New York or England.

In this sense, the enforceability of foreign judgments in the Principality of Andorra is subject to a prior judicial proceeding of recognition (the exequatur proceeding) which falls into the domain of competence of the Andorran High Court of Justice – the highest level of authority in the Andorran judicial system – and which is based on the criterion of reciprocity.

The Andorran court shall verify that the foreign judgment complies with each one of the following conditions: (i) the competence of the jurisdiction that has rendered the foreign judgment; (ii) the regularity of the trial procedure followed; (iii) the accordance of the foreign judgment to national and international public order laws; and (iv) the absence of any type of fraud in Andorran law.

7.3 Assuming a company is in payment default under a loan agreement or a guarantee agreement and has no legal defence to payment, approximately how long would it take for a foreign lender to (a) assuming the answer to question 7.1 is yes, file a suit against the company in a court in your jurisdiction, obtain a judgment, and enforce the judgment against the assets of the company, and (b) assuming the answer to question 7.2 is yes, enforce a foreign judgment in a court in your jurisdiction against the assets of the company?

(a) It will depend on the complexity of the matter. The enforcement of a security in Andorra is subject to the determination that a breach of the main obligation has occurred (an average of between 12 and 18 months is required in matters that do not present a special complexity) and to a second procedure of foreclosure over the secured assets which normally requires several public auctions.

(b) As mentioned in question 7.2, the enforcement of a foreign judgment is subject to the *exequatur* procedure. The average resolution of this type of procedure is between six and 12 months. Once recognition of the foreign judgment is obtained, it is necessary to initiate a foreclosure procedure which is also subject to public auctions.

7.4 With respect to enforcing collateral security, are there any significant restrictions which may impact the timing and value of enforcement, such as (a) a requirement for a public auction, or (b) regulatory consents?

Under Andorran law, a creditor cannot appropriate a secured property without commencing enforcement proceedings, which, in general terms, imply the sale in a public auction of the secured assets. A foreclosure proceeding is regulated by the Foreclosure Act, dated 18th December 2014.

The Foreclosure Act provides two public auctions, the starting price being determined by an appraisal (which in certain events of disagreement between the parties must be established by an independent appraisal) of 70% for the first auction and of 50% for the second auction. The direct award of the collateral is only contemplated in exceptional cases and in the event that the public auctions are declared deserted. If a foreign secured party is finally awarded with real estate property, a foreign investment authorisation might be required.

7.5 Do restrictions apply to foreign lenders in the event of (a) filing suit against a company in your jurisdiction, or (b) foreclosure on collateral security?

There are no restrictions for foreign lenders to file a suit in Andorra against an Andorran company. In the event of foreclosure and direct awarding of real estate property, the Foreign Investment Act might be applied and a previous authorisation might be required.

7.6 Do the bankruptcy, reorganisation or similar laws in your jurisdiction provide for any kind of moratorium on enforcement of lender claims? If so, does the moratorium apply to the enforcement of collateral security?

Please see the answer to question 8.1 below.

7.7 Will the courts in your jurisdiction recognise and enforce an arbitral award given against the company without re-examination of the merits?

The recognition of foreign arbitral awards is subject to the exequatur procedure on the same terms as described in the answer to question 7.2. Furthermore, the Andorran Arbitration Act, dated 18th December 2014, establishes that the exequatur on arbitral awards is subject to the New York Convention of 1958, notwithstanding any more favourable international treaty on the matter.

8 Bankruptcy Proceedings

8.1 How does a bankruptcy proceeding in respect of a company affect the ability of a lender to enforce its rights as a secured party over the collateral security?

In accordance with the Andorran Decree on Insolvency, dated 4th October 1969, a declaration of bankruptcy or the establishment of a judicial agreement of a person would imply that: (i) its creditors would not be allowed to demand their credits individually; (ii) their credits would be part of the insolvency estate represented by the administrator appointed by the court and; and (iii) all individual actions in process at the time would be suspended.

However, if the creditor's rights are secured by means of *in rem* securities, such as pledges and/or mortgages, their credits would receive the consideration of privileged securities, and any enforcement action initiated by them would not be suspended as a result of the declaration of bankruptcy. Furthermore, their credits would not be part of the insolvency estate, except in the event that the securities were not sufficient to cover the secured liability.

Under an insolvency procedure, the administrator appointed by the court may require the secured creditor to cancel any pledge it may hold on a previous payment of the amount secured.

Concerning mortgages, if no action has been initiated in order to execute them before the declaration of insolvency, the administrator, with the court's authorisation, is entitled to realise the sale of the mortgaged properties within three months after the declaration of insolvency. Notwithstanding, the secured creditor, within the two-month period after the relevant notification from the court, may initiate the relevant proceeding in order to enforce its security. All of such sales shall be realised under the public auction proceeding carried out by the competent authority.

In both cases, if the amount recovered is insufficient to cancel the amount of the debt secured, the creditor's credits will be part of the insolvency estate, for the outstanding amount of the debt as ordinary creditors.

8.2 Are there any preference periods, clawback rights or other preferential creditors' rights (e.g., tax debts, employees' claims) with respect to the security?

Under the Andorran Insolvency Decree, creditors' rights are qualified as privileged or ordinary. The law contemplates a general privilege in favour of the employees of the debtor over its properties. However, the Andorran courts have determined on several occasions that employees' privilege does not affect the privilege granted by *in rem* securities.

The Andorran Decree on Insolvency also provides the unenforceability of certain acts carried out by the debtor after the date of the declaration of insolvency against the mass of creditors, and particularly: (i) gratuitous dispositions and all the contracts in which debtors' obligations notably exceed its counterpart's obligations; (ii) payments made concerning debts not falling due at the moment of declaration of insolvency; (iii) mortgages or securities granted after the date of the declaration of insolvency for previous debts; and (iv) debtors' acts challenged by the administrators or by the creditors on the basis of simulation. A court declaration of insolvency must determine the date from which the debtor is considered to be insolvent. Such date must not be earlier than 18 months before the court's declaration. As a result, the third party involved in the rescinded act would be obliged to restitute the goods or services, plus interests and fruits, if any.

8.3 Are there any entities that are excluded from bankruptcy proceedings and, if so, what is the applicable legislation?

According to the Insolvency Act, bankruptcy proceedings are solely applicable to commercial companies and individuals that carry out commercial activities. Please bear in mind that under the Andorran law for establishing a framework for the recovery and resolution of credit institution, the bankruptcy procedures applicable to such entities is subject to certain specificities.

8.4 Are there any processes other than court proceedings that are available to a creditor to seize the assets of a company in an enforcement?

Yes, extrajudicial procedures are available to the parties as long as they are agreed upon by them. Such procedures are normally carried out by Andorran notaries and are subject to the performance of several auctions. It is highly advisable to determine the procedure to follow in the security document.

9 Jurisdiction and Waiver of Immunity

9.1 Is a party's submission to a foreign jurisdiction legally binding and enforceable under the laws of your jurisdiction?

Andorran courts have exclusive jurisdiction over certain matters where a specific law so provides, for instance: in claims related to the Andorran nationality; in disputes arising from rights *in rem* over immovable properties located in the Principality of Andorra and lease contracts over properties located in the Principality of Andorra; and in disputes related to the validity, invalidity or dissolution of Andorran companies or their resolutions, among several others. Therefore, if the matter in question is not affected by an exclusive jurisdiction clause, the submission to a foreign jurisdiction made by the parties to a contract would be enforceable under the laws of Andorra.

Under Andorran law, the competent jurisdiction to resolve a dispute is the jurisdiction in which the defendant is domiciled, whenever there does not exist a specific provision in the law that attributes the exclusive jurisdiction to the Andorran courts, or whenever the parties have not agreed to submit the claim to any other jurisdiction. Additionally, the doctrine considers that, as regards the resolution of disputes in contractual matters, the first rule on the attribution of jurisdiction is the autonomous will of the parties. In the absence of designation by the contracting parties, the jurisdictional competence corresponds to the jurisdiction in which the defendant is domiciled

9.2 Is a party's waiver of sovereign immunity legally binding and enforceable under the laws of your jurisdiction?

A part of the doctrine admits the possibility to waive the sovereign immunity. Regarding the immunity of execution, the restriction to waive is considered to be related to the nature of the assets, it being understood that for certain type of assets, immunity is absolute.

10 Licensing

10.1 What are the licensing and other eligibility requirements in your jurisdiction for lenders to a company in your jurisdiction, if any? Are these licensing and eligibility requirements different for a "foreign" lender (i.e. a lender that is not located in your jurisdiction)? In connection with any such requirements, is a distinction made under the laws of your jurisdiction between a lender that is a bank *versus* a lender that is a non-bank? If there are such requirements in your jurisdiction, what are the consequences for a lender that has not satisfied such requirements but has nonetheless made a loan to a company in your jurisdiction? What are the licensing and other eligibility requirements in your jurisdiction for an agent under a syndicated facility for lenders to a company in your jurisdiction?

There are no restrictions in that sense. However, if an entity carries out financing activities on a regular basis in Andorra, it must be duly authorised and it will be subject to regulation for its financial activities.

11 Other Matters

11.1 Are there any other material considerations which should be taken into account by lenders when participating in financings in your jurisdiction?

The majority of the matters have been mentioned in the previous answers.

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Angola

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1 Overview

1.1 What are the main trends/significant developments in the lending markets in your jurisdiction?

Due to the significant fall in oil prices in international markets, since June 2014, the national economy has faced (i) a contraction in economic activity, (ii) an exponential increase in inflation rates, (iii) a deterioration in the indicators of the fiscal sector, although there have been significant efforts by the Government to improve the collection of taxes in other sectors of the economy, (iv) a significant fall in net international reserves, and (v) a lending squeeze on the economy, which has conditioned the development of the private sector.

1.2 What are some significant lending transactions that have taken place in your jurisdiction in recent years?

The landmark lending transactions in 2017 have been: (i) the EUR 220.6 million loan from Standard Chartered Bank (SCB) to finance the construction project of the transport system of energy associated with the Laúca utilisation hydropower plant to the Angolan Government; and (ii) the USD 150 million loan from Gemcorp Capital for the conclusion of the Laúca utilisation hydropower plant to the Angolan Government.

2 Guarantees

2.1 Can a company guarantee borrowings of one or more other members of its corporate group (see below for questions relating to fraudulent transfer/financial assistance)?

As a general rule, the corporate powers of a company are restricted to those rights and obligations necessary or appropriate to pursuing the corporate object of the company (which, generally, is to make a profit).

Under Article 6(3) of the Angolan Companies Code, there is a legal presumption that granting guarantees in respect of obligations of other entities is contrary to the purpose of companies, unless there is a justifiable own interest of the company in providing the guarantee or the company in question is in a group or control relationship with the other company.

Such a justifiable own interest of the company is evident in the provision of downstream guarantees, but is less evident in the provision of upstream and cross-stream guarantees. In the case of upstream and cross-stream guarantees, it is advisable for the necessary resolutions to be passed justifying the own interest of the company, which may be an indirect one, in providing the guarantee.

2.2 Are there enforceability or other concerns (such as director liability) if only a disproportionately small (or no) benefit to the guaranteeing/securing company can be shown?

In such situations, it is likely that there is no justifiable own interest to the company in providing the guarantee/security and, unless the company is in a group or control relationship with the entity whose obligations it guarantees/secures, the provision of the guarantee/security may be considered null and void.

Pursuant to Article 1175 of the Angolan Civil Procedure Code, in the absence of benefit or the existence of only a disproportionately small benefit to the company, the provision of the guarantee/security may be terminated in the context of insolvency proceedings relating to the company if the guarantee/security is provided during the two-year period prior to the declaration of insolvency.

The provision of the guarantee or security with a disproportionate, small (or no) benefit to the company may give rise to the breach of duties of directors towards the company and, therefore, liability.

2.3 Is lack of corporate power an issue?

Yes, please see question 2.1 above.

2.4 Are any governmental or other consents or filings, or other formalities (such as shareholder approval), required?

Except for certain state-owned and other public sector companies, unless there is a restriction contained in the articles of association of the company, in principle, no governmental approvals, consents, filings or other formalities are required by law, for a guarantee provided by an Angolan company to be enforceable.

However, it is common practice for there to be a requirement for either shareholder approval or board approval to grant the guarantee. Usually, such approval will contain an express reference to the benefit of the company from the provision of the guarantee (even if the benefit is an indirect one) or to the control or group relationship (if any) with the entity benefiting from the provision of the guarantee.

2.5 Are net worth, solvency or similar limitations imposed on the amount of a guarantee?

No, but please see question 2.2 above as to corporate benefit.

2.6 Are there any exchange control or similar obstacles to enforcement of a guarantee?

No exchange controls or other obstacles exist in Angola regarding the enforcement of a guarantee (inbound).

3 Collateral Security

3.1 What types of collateral are available to secure lending obligations?

Under book II, chapter VI of the Angolan Civil Code there are various types of collateral available to secure lending obligations, such as:

(i) provision of bonds;
(ii) bail;
(iii) consignation of income;
(iv) mortgage;
(v) liens; and
(vi) right of retention.

3.2 Is it possible to give asset security by means of a general security agreement or is an agreement required in relation to each type of asset? Briefly, what is the procedure?

Under Angolan law, the provision of general security (i.e. over the assets of a given entity generally) is considered null and void because of a lack of determination of the specific assets that become subject to the security.

It is therefore necessary for a security agreement to identify, to the greatest extent possible, the assets subject to the security created by the agreement. The security agreement must contain at least certain criteria that would make it possible to identify the secured assets at a given time.

The use of one single agreement or separate agreements will depend on the type of security being granted, as mortgages and escrow of income must be granted by public deed, whereas pledges may be granted by means of private agreements.

3.3 Can collateral security be taken over real property (land), plant, machinery and equipment? Briefly, what is the procedure?

Yes, collateral security may be taken over such assets by means of a deed of mortgage.

A mortgage over a factory will include the real estate and all the machinery and equipment in it, which is identified in a schedule to the deed.

3.4 Can collateral security be taken over receivables? Briefly, what is the procedure? Are debtors required to be notified of the security?

Yes, collateral security by means of a pledge over receivables may be taken. A written agreement is required, as well as notification of the creation of the pledge to the debtors, so that the pledge may be enforced against them.

3.5 Can collateral security be taken over cash deposited in bank accounts? Briefly, what is the procedure?

Yes. There are two types of pledge that can be taken over cash deposited in bank accounts: a pledge created under the Angolan Civil Code; and a financial pledge.

The Angolan Civil Code pledge is the most common form of pledge. The financial pledge, which may be created if the pledgee is a bank, provides more flexibility to the pledgor upon enforcement.

In any event, formalities include the execution of an agreement and notice to the bank where the cash is deposited (if the custody bank is not the pledgee). The acknowledgment of the pledge by the bank is not required, but is useful to ensure swift enforcement.

3.6 Can collateral security be taken over shares in companies incorporated in your jurisdiction? Are the shares in certificated form? Can such security validly be granted under a New York or English law governed document? Briefly, what is the procedure?

Yes, collateral security may be taken over shares in companies incorporated in Angola as a pledge of shares.

Shares may be either in certificated form or in book-entry form. Yes, provided that any formalities required under Angolan law for the validity and effectiveness of the pledge are complied with. The procedure will depend on the type of company in question.

If the company is a private limited liability company (*sociedade por quotas*), registration of the pledge over the shares at the Commercial Registry is required.

If the company is a public limited liability company (*sociedade anónima*) and the shares are in certificate form, a pledge of shares of this type of company requires the annotation of the creation of the pledge on each share certificate and registration of the pledge in the books of the issuer. The creation of the pledge over book-entry shares is made by annotation of the creation of the pledge in the securities account in which the shares are deposited and registered in the books of the issuer.

3.7 Can security be taken over inventory? Briefly, what is the procedure?

Security over inventory is possible if the security is granted in favour of a credit institution. The procedure includes the execution of a written agreement. Upon default or the occurrence of other circumstances as set out in the pledge agreement, it is customary for the pledgee or security agent to give an enforcement notice to the pledgor crystallising the stock. Alternatively, parties may agree on the provision of regular notices detailing the pledged stock.

3.8 Can a company grant a security interest in order to secure its obligations (i) as a borrower under a credit facility, and (ii) as a guarantor of the obligations of other borrowers and/or guarantors of obligations under a credit facility (see below for questions relating to the giving of guarantees and financial assistance)?

Yes, but please see the restrictions on the provision of guarantees in question 2.1 above, which are also applicable in relation to the provision of security interests by companies.

3.9 What are the notarisation, registration, stamp duty and other fees (whether related to property value or otherwise) in relation to security over different types of assets?

The costs for the creation of security are, generally, as follows:

(i) notarial fees (only applicable where the execution of a public deed is required): this depends on the nature and complexity of the act to be executed;

(ii) registration fees: this depends on the nature of the act and the value of the share capital; and

(iii) stamp duty (please see below on the applicability of stamp duty): this depends on the nature and complexity of the act to be executed.

3.10 Do the filing, notification or registration requirements in relation to security over different types of assets involve a significant amount of time or expense?

In principle there should be no timing issues. Filings, notifications and registrations can be done in a matter of a few days.

Expenses can be considerable if stamp duty is due on the granting of guarantees or the creation of security.

3.11 Are any regulatory or similar consents required with respect to the creation of security?

No regulatory or similar consents apply, except for assets held by state-owned entities or shares of concessionaires of public services, which must be assessed on a case-by-case basis.

3.12 If the borrowings to be secured are under a revolving credit facility, are there any special priority or other concerns?

No, there are not. In any case, please note that the creditors benefitting from *in rem security* have a privileged status under the Angolan Civil Procedure Code. The fact that the credit facility is a revolving one does not affect priority or raise other concerns.

3.13 Are there particular documentary or execution requirements (notarisation, execution under power of attorney, counterparts, deeds)?

Yes, the creation of security over real estate requires the execution of a deed before a notary. In this case, the powers of attorney, if any, must also be granted before a notary public. The execution of a deed in Angola before a notary requires the parties (whether Angolan or foreign entities) to have a tax identification number. This number must also be provided for the registration of a security interest in favour of a given entity.

4 Financial Assistance

4.1 Are there prohibitions or restrictions on the ability of a company to guarantee and/or give security to support borrowings incurred to finance or refinance the direct or indirect acquisition of: (a) shares of the company; (b) shares of any company which directly or indirectly owns shares in the company; or (c) shares in a sister subsidiary?

(a) Shares of the company

Yes, this is expressly forbidden by Article 344 of the Angolan Companies Code. Few exceptions are available. The violation of this prohibition may lead to criminal liability of the directors/managers of the company in question and the agreement, guarantee or security interest may be declared null and void.

(b) Shares of any company which directly or indirectly owns shares in the company

No express prohibition exists, but it is generally understood as applicable. Furthermore, the corporate powers of the company may be restricted in respect of the granting of guarantees or security – please see question 2.1 above.

(c) Shares in a sister subsidiary

No express prohibition exists, but please note that the corporate powers of the company may be restricted in respect of the granting of guarantees or security – please see question 2.1 above.

5 Syndicated Lending/Agency/Trustee/Transfers

5.1 Will your jurisdiction recognise the role of an agent or trustee and allow the agent or trustee (rather than each lender acting separately) to enforce the loan documentation and collateral security and to apply the proceeds from the collateral to the claims of all the lenders?

The role of the agent acting on behalf of the secured creditors is recognised in Angola, provided that the agent is also a secured creditor, which is usually the case. This requirement derives from the fact that, under Angolan law, only an entity which is a creditor may request the registration of the security in its own name. In such circumstances, and besides the fact that the agent is also named as a secured creditor in the documentation, the documentation must provide that the agent will also be acting as a representative of the other creditors in enforcing the security.

The role of the trustee is not recognised in Angola.

5.2 If an agent or trustee is not recognised in your jurisdiction, is an alternative mechanism available to achieve the effect referred to above which would allow one party to enforce claims on behalf of all the lenders so that individual lenders do not need to enforce their security separately?

This is not applicable.

5.3 Assume a loan is made to a company organised under the laws of your jurisdiction and guaranteed by a guarantor organised under the laws of your jurisdiction. If such loan is transferred by Lender A to Lender B, are there any special requirements necessary to make the loan and guarantee enforceable by Lender B?

Yes, notice to the borrower and guarantor of the assignment is required, as well as registration of the security (if subject to registration) with the appropriate registry (land registry, commercial registry, motor vehicle registry, financial intermediary or company books, as applicable).

In addition, please note that the assignment of security against a company that is in an insolvency proceeding will, from a practical perspective, also require the notice of the assignment to be given to the court so that the new creditor can be recognised in the insolvency proceeding.

However, please note that there might be situations in which the guarantee may not be assigned. For example, if the parties have restricted the ability of the guarantor to assign, or if the guarantee has been provided *intuitu personae* (i.e. the nature of the guarantee is not separable from the person or the borrower).

6 Withholding, Stamp and Other Taxes; Notarial and Other Costs

6.1 Are there any requirements to deduct or withhold tax from (a) interest payable on loans made to domestic or foreign lenders, or (b) the proceeds of a claim under a guarantee or the proceeds of enforcing security?

Payments of interest by an Angolan taxpayer to a foreign lender will be subject to a withholding Capital Investment Income Tax, at a rate of 15 per cent. No withholding tax is applied to the proceeds of a claim under a guarantee or the proceeds of enforcing security.

6.2 What tax incentives or other incentives are provided preferentially to foreign lenders? What taxes apply to foreign lenders with respect to their loans, mortgages or other security documents, either for the purposes of effectiveness or registration?

The law does not establish any specific tax exemptions or incentives for foreign lenders with respect to their loans, mortgages or other security documents.

Some operations are exempt from Stamp Duty. These include interest arising from public bonds and guarantees/securities granted in connection with operations executed through the Angolan stock exchange.

6.3 Will any income of a foreign lender become taxable in your jurisdiction solely because of a loan to or guarantee and/or grant of security from a company in your jurisdiction?

The income of a foreign lender deriving from payments of interest will become taxable in Angola by virtue of the borrower being considered tax resident in Angola. Please note that, as mentioned in question 6.1 above, there will be withholding tax on the payments of interest in this situation.

6.4 Will there be any other significant costs which would be incurred by foreign lenders in the grant of such loan/guarantee/security, such as notarial fees, etc.?

There are other costs, such as notarial fees and land registry fees, for the registration of a mortgage over real estate. These will not be significant unless the security is granted over several properties.

According to the updated Regulation of the Fees for Registration of the Property, the cost of registration of a mortgage depends on the value of the property and the complexity of the act to be submitted by a notary.

6.5 Are there any adverse consequences to a company that is a borrower (such as under thin capitalisation principles) if some or all of the lenders are organised under the laws of a jurisdiction other than your own? Please disregard withholding tax concerns for purposes of this question.

No specific adverse consequences (other than described above as to withholding tax) will arise by virtue of the lenders being incorporated outside Angola.

7 Judicial Enforcement

7.1 Will the courts in your jurisdiction recognise a governing law in a contract that is the law of another jurisdiction (a "foreign governing law")? Will courts in your jurisdiction enforce a contract that has a foreign governing law?

Under the general principle set out in the Angolan Civil Code, the parties to an agreement may choose the governing law of the agreement, provided their choice corresponds to a serious interest of the parties or is the law of a jurisdiction that has a connection with the agreement and is legitimate in the context of the principles of private international law.

7.2 Will the courts in your jurisdiction recognise and enforce a judgment given against a company in New York courts or English courts (a "foreign judgment") without re-examination of the merits of the case?

Any final judgment obtained in a competent jurisdiction in respect of any sums payable in connection with the agreements would be enforced by the courts of Angola under the conditions set out in the Angolan Civil Procedure Code before re-examining the merits of the case.

7.3 Assuming a company is in payment default under a loan agreement or a guarantee agreement and has no legal defence to payment, approximately how long would it take for a foreign lender to (a) assuming the answer to question 7.1 is yes, file a suit against the company in a court in your jurisdiction, obtain a judgment, and enforce the judgment against the assets of the company, and (b) assuming the answer to question 7.2 is yes, enforce a foreign judgment in a court in your jurisdiction against the assets of the company?

In general, filing a suit in Angola, obtaining a judgment and enforcing it could take 36 months on average. Enforcing a foreign judgment in Angola against the assets of the company could take 18 months. In both scenarios, the timeframe for enforcement of the court decision will depend on how long it takes to identify the assets to be seized.

7.4 With respect to enforcing collateral security, are there any significant restrictions which may impact the timing and value of enforcement, such as (a) a requirement for a public auction, or (b) regulatory consents?

Yes, timing of the enforcement may be affected in the event that there is a public auction of the assets or in the event that such auctions are not successful, if, for instance, no offers higher than the reserve price are received.

Regulatory consents may also impose a significant delay in the conclusion of the enforcement in the event that the sale of the enforced assets to the acquirer is subject to obtaining regulatory consents, in the context of competition laws or regulated sectors (sale of qualified shareholdings in financial institutions, defence industries, public services concessionaires).

7.5 Do restrictions apply to foreign lenders in the event of (a) filing suit against a company in your jurisdiction, or (b) foreclosure on collateral security?

No, in principle, no such restrictions will apply.

7.6 Do the bankruptcy, reorganisation or similar laws in your jurisdiction provide for any kind of moratorium on enforcement of lender claims? If so, does the moratorium apply to the enforcement of collateral security?

Yes, under the Angola Civil Procedure Code, the start of an insolvency action will imply a moratorium on the enforcement of collateral security against the insolvent or quasi-insolvent borrower or guarantor.

7.7 Will the courts in your jurisdiction recognise and enforce an arbitral award given against the company without re-examination of the merits?

The Angolan Republic is a party to the New York Arbitration Convention and therefore any arbitral awards given in another contracting state will be recognised without re-examination of the merits of the claim.

In relation to arbitral awards given in a state which is not a party to the New York Arbitration Convention, or any other convention to which Angola is a party, the enforcement of an arbitral award in Angola is subject to the recognition of the award by a court in Angola, irrespective of the nationality of the parties.

8 Bankruptcy Proceedings

8.1 How does a bankruptcy proceeding in respect of a company affect the ability of a lender to enforce its rights as a secured party over the collateral security?

Yes, under Article 1142 (3) of the Angolan Civil Procedure Code, the start of an insolvency action will suspend all enforcement proceedings against the company.

8.2 Are there any preference periods, clawback rights or other preferential creditors' rights (e.g., tax debts, employees' claims) with respect to the security?

Under Article 1175 of the Angolan Civil Procedure Code, there is a two-year period of suspicion during which any acts that are "prejudicial" to the insolvent entity and are carried out in bad faith will be set aside.

In addition, Article 1212 of the Angolan Civil Procedure Code sets out the specific situations in which certain acts may be set aside.

Under the Angolan Civil Code there is also a concept of *impugnação pauliana* (Paulian Action) pursuant to which an action could be brought by a creditor to set aside a transaction that results in a decrease in the bankrupt company's assets and in circumstances in which there was no consideration, provided that certain requirements are met.

Preferential creditor's rights exist under Angolan law. These include court fees, tax debts and employees claims.

8.3 Are there any entities that are excluded from bankruptcy proceedings and, if so, what is the applicable legislation?

Yes, the Angolan Republic and certain public sector entities, particularly financial institutions, are excluded under the Angolan Civil Procedure Code and, under Articles 108 and 121, the financial institutions law governing the insolvency of such entities is applicable.

8.4 Are there any processes other than court proceedings that are available to a creditor to seize the assets of a company in an enforcement?

Under (i) the Angolan Civil Code, (ii) the Angolan Commercial Code, (iii) the rules on financial pledges, or (iv) the rules on banking pledges, it is possible for the enforcement of a pledge to be conducted out of court.

In the case of a pledge created under the rules of the Angolan Civil Code, the parties may agree to an out-of-court sale of the pledged assets. However, in this situation, the pledged assets will, in principle, be in the possession of the pledgee or a custodian appointed by the parties.

In the case of a financial pledge, the Commercial Code pledge, or a banking pledge, the assets may not be in the possession of the pledgee. If the assets are in the possession of the pledgee or an agent appointed by the pledgee, the pledgee may appropriate the assets, but must return any excess amounts to the pledgor.

9 Jurisdiction and Waiver of Immunity

9.1 Is a party's submission to a foreign jurisdiction legally binding and enforceable under the laws of your jurisdiction?

Yes, please see answer to question 7.2 above.

9.2 Is a party's waiver of sovereign immunity legally binding and enforceable under the laws of your jurisdiction?

In the event that an entity benefits from sovereign immunity, the waiver of the benefit of this immunity will be valid. However, it should be noted that the assets of this entity which are in the public domain (*domínio público*), or used for the purpose of pursuing a public service, may not be seized and the entity may not waive immunity over these assets, unless there is a specific law approved for this purpose.

10 Licensing

10.1 What are the licensing and other eligibility requirements in your jurisdiction for lenders to a company in your jurisdiction, if any? Are these licensing and eligibility requirements different for a "foreign" lender (i.e. a lender that is not located in your jurisdiction)? In connection with any such requirements, is a distinction made under the laws of your jurisdiction between a lender that is a bank *versus* a lender that is a non-bank? If there are such requirements in your jurisdiction, what are the consequences for a lender that has not satisfied such requirements but has nonetheless made a loan to a company in your jurisdiction? What are the licensing and other eligibility requirements in your jurisdiction for an agent under a syndicated facility for lenders to a company in your jurisdiction?

Under the Financial Institutions Law (as approved by Law No. 12/15 of 17 June), only licensed entities may engage in lending activity in Angola on a professional basis. The provision of loans to Angolan entities on a professional and regular basis will trigger a licensing requirement in Angola. However, if a foreign entity provides loans to Angolan entities on a one-off or very infrequent basis no licensing requirement will apply as the foreign lender may be held not to be carrying on activity in Angola. For this, it would require a repetition of acts or transactions in Angola.

11 Other Matters

11.1 Are there any other material considerations which should be taken into account by lenders when participating in financings in your jurisdiction?

We believe that the questions above fairly address the main material issues that arise generally in the context of lending transactions.

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Bruno Xavier de Pina, the partner who heads PLMJ's Angola Desk, has gained comprehensive experience over the last 13 years in providing legal support to clients from China to Canada with interests in Africa, in particular Angola, and around the world.

Before joining PLMJ, Bruno worked at Deloitte for four years and in other Portuguese law firms, Miranda Correia Amendoeira & Associados and Raposo Bernardo & Associados, both in Lisbon.

Bruno earned his law degree from the University of Lisbon in 2001. He also earned a postgraduate in tax from the Lisbon School of Economics and Management (ISEG) in 2003 and is admitted to practise under São Tomé e Príncipe law, as a member of the São Tomé and Príncipe Bar Association since 2007.

Bruno has acquired significant experience in international projects, including factories; international JVs; structuring projects comprising EPCI contracts; assisting and advising the major international banks in the refinancing effects of oil operations in the Angolan off-shore block; and numerous cases providing assistance in foreign exchange law matters. Bruno is also skilled in providing legal support to lenders in external financing deals to the Republic of Angola. These include a working capital financing agreement, an infrastructure financing agreement (motorways) and several equipment financing agreements (turbines, locomotives, etc.). Bruno also advised an Angolan bank on the restructuring of the debt relating to a real estate project.

Bruno is ranked in *Chambers Global*, *The Legal 500* and *IFLR1000*. In September 2017, he won the special Outstanding Achievement award at the Iberian Lawyer 40 under Forty awards ceremony. This award recognises the 40 best lawyers on the Iberian Peninsula under the age of 40, and Bruno Xavier de Pina was one of the award winners, taking home the special Outstanding Achievement award, given for his work in developing legal support for clients worldwide with interests in Africa and around the world. (https://www.plmj.com/en/about-plmj/awards-and-rankings/awards/bruno-xavier-de-pina-wins-iberian-lawyer-outstanding-achievement-award-in-barcelona/17955/.)

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Senior associate João Bravo da Costa is dual qualified to practise in Angola and Portugal. He is also qualified to practise in the State of New York. He joined PLMJ Network in 2011, having previously worked at Miranda, Correia, Amendoeira & Associados in its Lisbon and Luanda offices from 2005. João has a law degree from Universidade Católica Portuguesa and was admitted to the Portuguese and Angolan Bar Associations in 2008 and 2009, respectively. João is a lawyer with extensive experience in banking, corporate and commercial law.

João has significant experience in advising foreign investors in the development and implementation of investment projects in various sectors of the economy, including financing agreements involving private entities of the State as borrower. He has also provided legal advice to an international bank in relation to a short-term transaction and the subsequent agreement with an international oil and gas company that is a member of the Angolan group Offshore Oil Block.

João is ranked in *Chambers Global*, *The Legal 500* and *IFLR1000*.

GLA
GABINETE LEGAL ANGOLA
ADVOGADOS

Under Law 16/16 of 30 September, the name GLA will be changed.

The new name is awaiting the approval of the Angolan Bar Association.

GLA is a law firm that brings together a group of leading Angolan legal professionals who share a firm interest and great satisfaction in working in Angola for Angola in strict compliance with the professional and ethical rules of the Angolan Bar Association.

GLA's lawyers have signed a cooperation agreement with PLMJ under which they ensure local support for clients of PLMJ Network. The services GLA provides are backed up by close cooperation with the lawyers of the PLMJ Africa Desk and this is a close and ongoing partnership that results in the provision of highly specialised services with a great deal of added value and enormous technical quality for all our clients.

GLA's team of professionals is made up of a number of lawyers with differing professional interests and levels of seniority who have professional and academic experience gained in Angola and other countries.

Note: Under Angolan law, the name GLA is in the process of changing. A proposal to constitute a law firm with a new name is in progress.

Argentina

Juan M. Diehl Moreno

Marval O'Farrell & Mairal

Diego A. Chighizola

1 Overview

1.1 What are the main trends/significant developments in the lending markets in your jurisdiction?

The main significant development is the abrogation of the foreign exchange restrictions which have been adopted in Argentina since 2001, mainly affecting cross-border financing.

Since December 17, 2015, the new elected authorities in Argentina have been implementing a series of measures to progressively deregulate and implement more flexible regulations. The new regulation removed the requirement for residents to transfer to Argentina and settle in the foreign exchange market the proceeds disbursed under any financial indebtedness incurred with a non-resident. Also, the minimum maturity term has been eliminated, and principal amounts can be repaid or voluntarily or mandatorily prepaid. Finally, the new regulation eliminated the 30% mandatory deposit for the inflow of certain funds to Argentina through the foreign exchange market.

These developments, together with other economic and political measures taken by the new administration, are starting to create a new investment environment that has begun to show an increase in cross-border financing.

1.2 What are some significant lending transactions that have taken place in your jurisdiction in recent years?

- In 2017, Banco de la Ciudad de Buenos Aires granted Araucaria Energy S.A. a US$ 25,000,000 loan.
- In 2017, Citibank N.A., Goldman Sachs Bank USA, Industrial and Commercial Bank of China Limited Dubai (DIFC) Branch and Itaú Unibanco S.A. Nassau Branch granted Cablevisión Holding S.A. a US$ 750,000,000 loan.
- In 2017, Industrial and Commercial Bank of China (Argentina) S.A., Banco de Galicia y Buenos Aires S.A. and General Electric Company granted UENSA y UGEN (MSU Energy Group) a US$ 230,000,000 loan.
- In 2017, Japan Bank for International Cooperation and Deutsche Bank AG granted the Argentine Republic a US$ 51,000,000 loan.
- In 2016, International Finance Corporation granted Adeco Agropecuaria S.A./Pilaga S.A. a US$ 50,000,000 loan.
- In 2016, ICBC, Dubai Branch granted Loma Negra Compañía Industrial Argentina S.A. a US$ 50,000,000 Medium-Term Facility.
- In 2015, HSBC BANK USA, N.A. granted Cargill SACI a US$ 50,000,000 Pre-Export Finance Loan.
- In 2015, Unicredit S.p.A., BNP Paribas, Italian Branch and GE Capital Interbanca S.p.A. granted AEB a €71,500,000 loan.
- In 2015, International Finance Corporation granted Arla Foods Ingredients a US$ 56 million loan.
- In 2015, Banco Hipotecario, BACS, ICBC and Citibank granted Petrolera Pampa S.A. a US$ 83.4 million loan.
- In 2015, BBVA Banco Francés, Banco Santander Río, HSBC, Citibank, Banco Macro, Banco Galicia, Banco Hipotecario, BACS, ICBC, Banco Patagonia and Banco de la Pampa granted Bayer S.A. a US$ 245 million loan.

2 Guarantees

2.1 Can a company guarantee borrowings of one or more other members of its corporate group (see below for questions relating to fraudulent transfer/financial assistance)?

Yes, it is possible to secure the borrowings of other members of the corporate group. The company acting as a guarantor should receive proper (arm's-length) benefits or consideration in return. Otherwise, it may be considered that the granting of the guarantee derives no benefit for the securing company and, hence, other creditors could challenge such transaction.

In addition, the by-laws of the securing company should include the prerogative to grant borrowings to third parties or, alternatively, the main activity of the company should be financing. Nevertheless, certain jurisprudence resolved that if the by-laws do not include said prerogative, the irregularity may be fixed by a subsequent ratification of the shareholders.

These requirements should be strictly defined when the guarantee is upstream (a controlled entity acting as guarantor of an obligation of its direct or indirect parent company or an affiliate).

2.2 Are there enforceability or other concerns (such as director liability) if only a disproportionately small (or no) benefit to the guaranteeing/securing company can be shown?

In case the securing company does not have any financial corporate purpose, nor receives a consideration or benefit, the guarantee may be deemed out of the scope of the securing company's corporate purpose (*ultra vires*) and, consequently, may be declared void.

Further, pursuant to Argentine law, directors must act loyally towards the company and its shareholders, which includes the director's responsibility to perform its duties with the diligence of a "good businessman" and in the interest of the company. Any failure to comply with these standards results in directors' unlimited liability for the damages arising therefrom.

To be released from any such liability, the director must timely file written objections to the company's resolution that caused the damages, and, if applicable, give notice thereof to the company's statutory auditors or file proceedings for challenging the decision.

Therefore, although it is not specifically provided, if a guarantee is deemed out of the scope of the securing company's purpose, it might be understood as a breach of the director's duties and, consequently, the director would be deemed responsible for negligence.

2.3 Is lack of corporate power an issue?

Yes. Corporate power is required to grant guarantees and any guarantee granted without sufficient corporate power could trigger director liability, as explained above.

2.4 Are any governmental or other consents or filings, or other formalities (such as shareholder approval), required?

No governmental authorisation, consent or approval is required to grant a guarantee. However, it is advisable that the Board of Directors or the shareholders' meeting previously approves the transaction, particularly if the guarantee is for a significant amount considering the net worth of the guarantor and there is no specific provision in the by-laws of the guarantor. A unanimous approval through a shareholders' meeting is also advisable.

Also, if the security consists of a mortgage over real property located in a security zone (close to borders and other strategic zones), upon execution, transfer of land will require prior approval from the Security Zone Commission, unless the transferee is an Argentine individual.

In addition, third parties' consents may be required for the assignment of agreements to a trust. As a general rule, since contracts involve both rights and obligations, the transfer of the obligations is not allowed unless the express consent of the counterparty is obtained (see questions 3.1 and 3.4).

2.5 Are net worth, solvency or similar limitations imposed on the amount of a guarantee?

As long as the company operates within its corporate purpose, as explained in question 2.1, Argentine law does not provide limitations on the amount of a guarantee; however, deduction of interest may be limited under certain thin capitalisation rules. Please refer to question 6.5.

2.6 Are there any exchange control or similar obstacles to enforcement of a guarantee?

Foreign exchange rules allow residents to make payments abroad without entering and settling the funds through the Argentine Foreign Exchange Market (the "FX Market"). Regardless of whether the funds are entered through the FX Market or not, the debt shall be registered in the survey of debt issuance of external debt and liabilities established by Communique A 6401, as amended. Argentine foreign exchange rules do not affect a foreign lender's ability to exercise its rights against a foreign guarantor.

If the guarantee is established over a local asset and its enforcement implies the collection of Argentine Pesos, the foreign lender is able to purchase foreign currency for repatriation purposes. Also, proceeds obtained from a bankruptcy proceeding can be transferred abroad.

3 Collateral Security

3.1 What types of collateral are available to secure lending obligations?

In general terms, Argentine law recognises two kinds of guarantees: the "personal" guarantees; and the "asset-backed" guarantees.

"Personal" guarantees are granted by a person or a legal entity committing its property to assure the performance of one or more obligations of the debtor. Upon the debtor's default, the creditor may eventually take legal action over the debtor's property and the guarantor's property. This guarantee, unlike asset-backed guarantees, does not create a lien or a privilege in favour of the creditor.

"Asset-backed" guarantees are granted over a specific property owned by the guarantor. In this kind of guarantee, either the debtor or a third party may be the guarantor. Unlike personal guarantees, asset-backed guarantees grant the creditor (i) the rights of "persecution" and "preference" over the asset in question, which means that the creditor has the right to pursue the guarantor's property, even if the guarantor sells or transfers the property, and (ii) the right to execute the guarantee and receive the corresponding payment with preference over other creditors, even in the event of insolvency or bankruptcy of the debtor or the guarantor.

The most common guarantees are the following:

(a) Mortgage: The mortgage is the most frequently used security over immovable property. Also for certain movable property which has significant value, the law specifically demands the constitution of a mortgage instead of a pledge (i.e. airplanes). For further details, please refer to question 3.3.

(b) Pledge: A pledge may be constituted over movable property, including but not limited to: machinery; vehicles; patents; and trademarks. For further details please refer to question 3.3.

(c) Trust in Guarantee: A trust may secure both movable and immovable property for a maximum term of 30 years. Goods held in trust form an estate separate from that of the trustee and the trustor. Trusts must be registered with the appropriate public registry. Also, if the property given in trust is registered in a public registry, the relevant registry will record the property in the trustee's name. Therefore, they should not be affected by any individual or joint actions brought by the trustee's or trustor's creditors, except in the case of fraud. The beneficiary's creditors may exercise their rights over the proceeds of the goods held in trust and be subrogated to the beneficiary's rights.

    Any individual or legal entity may be appointed as a trustee of an ordinary trust. Financial entities that solicit services to act as trustees must obtain prior authorisation to do so. Although there is no ruling on the issue, it is advisable that the trustee be a different person from the secured creditor (although there is no obstacle if the trustee is a controlled or controlling entity of the secured party).

(d) Security Assignments: Assets may also be assigned as security. One of the differences with a trust is that, in the case of security assignments, assigned assets are typically limited to rights or credits including, without limitation, receivables.

    The creditor may demand payment of the credit to either the assignor or the debtor of the assigned credit. If the assignor pays the amounts owed, then the assigned credit should be assigned back to the assignor.

3.2 Is it possible to give asset security by means of a general security agreement or is an agreement required in relation to each type of asset? Briefly, what is the procedure?

Although it is not possible to execute a general security agreement, including different types of collateral securities, it is possible to execute a general agreement including more than one asset of the same type; for example, a pledge may include machinery and vehicles. In any case, the assets must be clearly identified in the security agreement.

In relation to the procedure, a security is executed by means of an agreement between parties, subject – in certain cases – to certain formalities. For example, mortgages must be made through public deeds.

Argentine law allows the pledge over an inventory of goods ("floating pledge"). Please refer to question 3.3.

3.3 Can collateral security be taken over real property (land), plant, machinery and equipment? Briefly, what is the procedure?

Collateral security can be taken over real property (mortgage) or over machinery and equipment (pledge).

a) Mortgage: A mortgage generally secures the principal amount, accrued interest, and other related expenses owed by the debtor. To be valid, the following conditions should be met:

(i) The mortgagor must own the property or properties to be mortgaged.

(ii) The mortgagor must have the capacity to transfer its assets.

(iii) In certain cases, prior consent of the spouse is required.

(iv) The mortgage must be granted over one or more specific properties and the maximum amount and the obligation secured must be certain and determined. Conditional, future or undetermined obligations are permitted to be secured, provided that a maximum amount of the guarantee is determined upon creation of the mortgage. Additionally, the mortgage over real property extends to: (i) all its accessories as long as they are attached to the principal property; (ii) the supervening improvements made to the property; and (iii) the asset's earned income (*frutos civiles y rentas*).

Mortgages must be executed in writing by means of a public deed, which must be registered with the Land Registry of the jurisdiction where the property is located to be valid *vis-à-vis* third parties.

A mortgage remains in full force and effect until all amounts secured have been paid or the mortgage is otherwise cancelled. The registration of a mortgage will automatically expire 20 years after the date upon which it was registered, unless renewed.

b) Pledges: The debts secured by a pledge can be conditional, future or undetermined, or otherwise uncertain in amount.

Pledges in Argentina are mainly governed by the Argentine Civil and Commercial Code, which came into force in August 1, 2015.

According to the provisions of the current legislation, there are two classes of pledges:

(i) "Unregistered Pledge": the pledged assets can be delivered to the creditor or placed in the custody of a third party. Upon default, the creditor may sell the pledged asset through a public auction. The distinction between Civil and Commercial Pledge adopted by both abrogated Civil and Commercial Codes was not embodied into the new Civil and Commercial Code. The New Code provides that parties may agree on the following: (i) that the creditor may obtain ownership of the asset for the estimated value of it, made at the time of maturity of the debt, as set by the expert appointed by the parties or designated by the judge at the request of the creditor; or (ii) by means of a special sales proceeding.

(ii) "Registered pledge": There are two types of registered pledges: the "fixed pledge", used for specified assets; and the "floating pledge", used for a certain inventory of goods, with no precise identification of the goods. A floating pledge allows for the replacement of the goods of the pledged inventory.

The registration of a fixed pledge involves the filing of the petition to the Pledge Registry of the jurisdiction in which the personal property is located.

The pledge agreement is legally binding between the parties from the date of execution. Upon registration, the agreement is effective *vis-à-vis* third parties. It shall be effective *vis-à-vis* third parties from the execution date if the petition to register the pledge is filed before the corresponding registry within 24 hours of its execution.

The registration of a pledge expires five years after the date on which it was registered, unless renewed. Once perfected, a pledge remains in full force and effect until all amounts secured have been fully paid or the pledge is otherwise cancelled.

The floating pledge may be created through a notarised private document, using the form provided by the Registry of Pledges for such purposes (a public deed is not required).

3.4 Can collateral security be taken over receivables? Briefly, what is the procedure? Are debtors required to be notified of the security?

Yes. Collateral security can be taken over receivables. In order to have effect *vis-à-vis* third parties, a private assignment agreement must be executed and the assigned debtor must be notified by a notary public.

Alternatively, a trust structure may be used. Please refer to question 3.1.

3.5 Can collateral security be taken over cash deposited in bank accounts? Briefly, what is the procedure?

Argentine law recognises the validity of a pledge over cash. In this case, the pledge shall have full effect upon delivery of the amounts pledged to the pledgee. These guarantees are not usual, though.

As for the procedure, please refer to question 3.3.

3.6 Can collateral security be taken over shares in companies incorporated in your jurisdiction? Are the shares in certificated form? Can such security validly be granted under a New York or English law governed document? Briefly, what is the procedure?

Yes. To be valid, the shareholder must inform the company about the terms and conditions of the pledge and the Board of Directors must record the existence of the pledge (i) in the Registry of Shares Book, and (ii) with a notation at the back of the share certificate (unless the shares are not represented in titles – i.e. book-entry shares).

Pursuant to Argentine law, movable assets which are permanently situated in a place and are not intended to be moved to a different jurisdiction are governed by the rules of the place where they are located. Thus, a guarantee agreement over the shares of a local company shall be governed by the rules of Argentina.

Parties in a loan agreement may freely agree on the law applicable to the contract (see question 7.1), but Argentine law must rule the content, conditions and effects of a security over the shares of the company.

3.7 Can security be taken over inventory? Briefly, what is the procedure?

Yes, under a "floating pledge". Please refer to question 3.3.

3.8 Can a company grant a security interest in order to secure its obligations (i) as a borrower under a credit facility, and (ii) as a guarantor of the obligations of other borrowers and/or guarantors of obligations under a credit facility (see below for questions relating to the giving of guarantees and financial assistance)?

(i) Yes, debtors may guarantee their own obligations. Please refer to questions 3.1 and 3.3 above.

(ii) Yes. It is a guarantee of a third party, different from the debtor. Please refer to questions 3.1 and 3.3 above.

3.9 What are the notarisation, registration, stamp duty and other fees (whether related to property value or otherwise) in relation to security over different types of assets?

Notarisation, registration and other fees vary depending on the jurisdiction in which the agreement is executed.

The following chart details the main costs applicable to different securities:

Security	Fees
Real Property (Mortgage)	Notary Fees: 1% of the principal amount. Stamp Tax: 1% of the economic value of the agreement in the City of Buenos Aires; 1.8% in other jurisdictions such as the Province of Buenos Aires. Registration Fees: AR$ 800.
Chattel Personal Property (Pledge)	Notary Fees: low depending on the characteristics of the pledge. Registration Fees: 1% to 2% of the guaranteed obligation. Stamp Tax: 1% of the economic value of the agreement in the City of Buenos Aires; 1.2% in other jurisdictions such as the Province of Buenos Aires.
Accounts Receivable/ Debt Securities	Notary Fees: low, depending on the characteristics of the security. Registration Fees: 0.2% of the guaranteed obligation. Stamp Tax: 1% of the economic value of the agreement in the City of Buenos Aires; 1.2% in other jurisdictions such as the Province of Buenos Aires.

3.10 Do the filing, notification or registration requirements in relation to security over different types of assets involve a significant amount of time or expense?

Registration before the applicable registry may take between approximately one and six months, depending on the type of assets involved.

As to expenses, please see the table in question 3.9.

3.11 Are any regulatory or similar consents required with respect to the creation of security?

There are no explicit statutory restrictions on the ability of Argentine companies to create pledges on their assets to secure *their own* obligations. However, certain limitations to, or special requirements on, the ability of an Argentine company to create pledges in its assets may be included in the by-laws of the company.

In addition, the by-laws may require express approval for the creation of any pledge on the assets of a company by its Board of Directors, in which case a resolution of the Board would be needed. In the absence of such requirement, the pledge may be created by any representative acting pursuant to an adequate power of attorney or, in the case of a corporation, by the president of the company.

3.12 If the borrowings to be secured are under a revolving credit facility, are there any special priority or other concerns?

No special priorities are provided for revolving credit facilities. In this kind of loan, careful drafting should be taken into account. The guarantee granted at execution of the agreement may secure the subsequent renewals of the loan.

3.13 Are there particular documentary or execution requirements (notarisation, execution under power of attorney, counterparts, deeds)?

For documentary requirements, please refer to question 3.3.

When a public deed is required, signing in counterparts, although not expressly prohibited, is not advisable since it could create certain issues in terms of proof.

4 Financial Assistance

4.1 Are there prohibitions or restrictions on the ability of a company to guarantee and/or give security to support borrowings incurred to finance or refinance the direct or indirect acquisition of: (a) shares of the company; (b) shares of any company which directly or indirectly owns shares in the company; or (c) shares in a sister subsidiary?

The limitations referred to above with respect to guarantees also apply here. In addition, there might be a tax impact related to a leverage buy out operation.

It should be noted that Income Tax Law does not provide clear parameters to distinguish between "debt" and "capital". Guidelines can be found in the Income Tax Law and its Regulating Decree, when they require – for irrevocable contributions – that "in no case shall there accrue interest or any accessories for the contributor".

As explained in question 6.1, a borrower is able to deduct interest (for income tax purposes) as long as the expenses were incurred to generate taxable income.

The Argentine Tax Authority has challenged the deduction of interest in cases of a leverage buy out to acquire shares of local companies. The National Tax Authority considered that such expense is not necessary to obtain taxable income or to keep or maintain its source. In certain cases, the resolution of the Tax Authority was confirmed by the Tax Court. The matter is pending a final ruling from the Argentine Supreme Court of Justice.

5 Syndicated Lending/Agency/Trustee/ Transfers

5.1 Will your jurisdiction recognise the role of an agent or trustee and allow the agent or trustee (rather than each lender acting separately) to enforce the loan documentation and collateral security and to apply the proceeds from the collateral to the claims of all the lenders?

In Argentina, the role of the agent or trustee is governed by the rules of contract. Therefore, the parties in a syndicated lending may freely determine the functions and powers of the agent; such powers might include calculating the due amount of principal and interest, calculating financial ratios, informing the compliance or defaults of the debtor's obligations under the agreement, and keeping and guarding the loan documentation.

The figure of the agent in a syndicated loan is different from the figure of a collateral agent. Since in Argentina the guarantees must be linked to the credits which are guaranteed, it is not possible to split the holder of the credit from the holder of the guarantee. Thus, if a collateral agent is appointed, it might act as representative of the creditors but not as the holder of the rights arising from the guarantee. All creditors should be incorporated in the relevant security agreement and registered as secured parties rather than registering the relevant security in the name of a trustee or security agent. Thus, a security agent may enforce guarantees on behalf of the lenders (as *apoderado*), provided that it is duly empowered to do so by a power-of-attorney and the guarantee provides for such possibility.

The classic US-like structure of collateral agent, pursuant to which security interests are granted directly to the trustee for the benefit of the lenders, may pose certain procedural issues and challenges in Argentina.

5.2 If an agent or trustee is not recognised in your jurisdiction, is an alternative mechanism available to achieve the effect referred to above which would allow one party to enforce claims on behalf of all the lenders so that individual lenders do not need to enforce their security separately?

- The credits and the guarantee might be transferred to a trustee, who will be committed to enforcing the security if the debtor fails to comply with the agreement and applying the proceeds from the security among the grantors beneficiaries.
- A real property might be transferred to a trustee, who might constitute a guarantee trust over such property in favour of the creditors.
- The guarantee might be granted in favour of one creditor, who commits to act as a collateral agent based on an intercreditor agreement.

5.3 Assume a loan is made to a company organised under the laws of your jurisdiction and guaranteed by a guarantor organised under the laws of your jurisdiction. If such loan is transferred by Lender A to Lender B, are there any special requirements necessary to make the loan and guarantee enforceable by Lender B?

The assignment of credits must be documented in an agreement. A debtor's intervention in the agreement is not required.

The enforceability of the credits by the new lender is subject to two requirements: (i) the transfer of the credit; and (ii) the debt being payable.

Debtors should be given notarised notice of the assignment to be effective *vis-à-vis* third parties and the debtor itself, in case of a judicial claim. The notice could also be made through a private instrument with an unequivocal date (*fecha cierta*).

6 Withholding, Stamp and Other Taxes; Notarial and Other Costs

6.1 Are there any requirements to deduct or withhold tax from (a) interest payable on loans made to domestic or foreign lenders, or (b) the proceeds of a claim under a guarantee or the proceeds of enforcing security?

As a general rule, deduction is allowed only for expenses incurred to generate taxable income.

Interest is deductible for the borrower. Interest deduction is limited by thin capitalisation rules (see question 6.5), unless a Double Tax Treaty with a non-discrimination clause is applicable. In such a case, total deduction could be possible. Recently, Law No. 27,430, which provides amendments to the Income Tax Law ("ITL"), was published. It establishes relevant modifications in the treatment of thin capitalisation rules. It also establishes that interest on financial debts – without including the debts generated by acquisitions of goods, leases or services related to the business line – incurred with individuals, residents or not, will be deductible up to the annual amount that establishes the Executive Power or up to the equivalent of 30% of the net income of the fiscal year that results before deducting both interest and amortisation, whichever is higher.

The accumulated surplus in the three previous fiscal years may be added to this limit, as the amount of interest effectively deducted from the applicable limit is lower. The interest that could not have been deducted may be added to those corresponding to the following five fiscal years.

In addition, if the loan is made with a related party, with a party located in a low-tax jurisdiction or the funds do not arise from a low-tax jurisdiction (regardless if it is related or not), interest is deductible only when paid, and transfer-pricing rules apply. ITL, modified by Law No. 27,430, defines non-cooperative jurisdiction as any jurisdiction or country that: (i) has not signed an information exchange agreement with Argentina; (ii) has not signed a convention to avoid double taxation with Argentina; or (iii) has signed either agreement or convention but does not comply with its obligation to share information with Argentina. The Executive Branch is responsible for issuing a list of non-cooperative jurisdictions.

6.2 What tax incentives or other incentives are provided preferentially to foreign lenders? What taxes apply to foreign lenders with respect to their loans, mortgages or other security documents, either for the purposes of effectiveness or registration?

There are no tax incentives for foreign lenders.

Foreign lenders will be taxed by income tax only on their profits from Argentina (Argentine-source income). When the lender is a banking or financial institution under the supervision of the relevant Central Bank or equivalent authority and is situated either in a jurisdiction that, in accordance with the regulations under the Income Tax Law, is not considered as a "low-tax jurisdiction", or in a jurisdiction that is party to an exchange of information treaty with Argentina and, as a result of the application of its internal regulations, cannot refuse to disclose information to Argentine authorities on the basis of bank or stock secrecy rules, the presumed net income in case of cross-border interest payments is 43% and, deriving from that, a 15.05% effective withholding rate. In all other cases of cross-border interest payments, the presumed net income is 100% and, therefore, the effective withholding rate is 35%. The Argentine debtor is responsible for the withholding and payment of the tax. Argentina has entered into treaties for the avoidance of double taxation with different countries. In certain cases, such treaties set forth ceilings to the effective withholding abovementioned. Value Added Tax ("VAT") applies to the sale of goods, the provision of services and the importation of goods and services. Under certain circumstances, services rendered outside Argentina, which are effectively used or exploited in Argentina, are subject to VAT.

Interest arising from a loan granted by a foreign entity is subject to VAT and the Argentine debtor is responsible for the payment of the tax.

The tax is levied on the interests paid and the current general rate is 21%. However, interests arising from loans granted by foreign banks are subject to a 10.5% rate when the central banks of their countries of incorporation have adopted the regulations provided by the Basel Committee.

Argentine Provinces and the City of Buenos Aires apply the Turnover Tax (Tax on Gross Income), levied on gross income obtained from the exercise of onerous and habitual activity within each relevant jurisdiction. The tax rate varies in each jurisdiction.

For tax purposes, the activity of lending money is presumed to be carried out on a habitual basis, even if carried out once, and therefore is subject to Turnover Tax. The amount of returned capital is excluded from the taxable base. Thus, only the total amount of interest will be subject to Turnover Tax. Notwithstanding, it is not clear if interest collected by a foreign lender is subject to Turnover Tax.

Stamp Tax is a local tax levied on public or private instruments executed in Argentina, or documents executed abroad with effect in one or more relevant jurisdictions within Argentina. In general, this tax is calculated on the economic value of the agreement. Each jurisdiction applies different tax rates to different types of agreements, but the most common rate is 1%, e.g., the City of Buenos Aires. Certain ways of entering into contracts do not trigger this tax.

Finally, a tax imposed on credits and debits in bank accounts (the "TDC") must be paid in the case of credits and debits in Argentine bank accounts at a rate of 0.6%. However, the credit of the borrower in an Argentine bank account arising from the disbursement of principal of the loan would not be subject to the TDC since the disbursement of principal under a "banking loan" is exempt from the TDC.

6.3 Will any income of a foreign lender become taxable in your jurisdiction solely because of a loan to or guarantee and/or grant of security from a company in your jurisdiction?

Non-Argentine residents without a permanent establishment in Argentina are only subject to Income Tax on their Argentine-source income. Only income from Argentine sources will be taxed by the Argentine Income Tax.

6.4 Will there be any other significant costs which would be incurred by foreign lenders in the grant of such loan/guarantee/security, such as notarial fees, etc.?

For notarisation, registration and other fees, please refer to question 3.9. Also, the loan and the guarantees will generally be taxed by Stamp Tax. For the purposes of the Stamp Tax, the loan and the guarantees could be considered independently even if they were agreed in the same document. Then, the transaction might be doubly taxed in certain jurisdictions. However, in the City of Buenos Aires, for example, there is an exemption by which the guarantees may not be subject to Stamp Tax if the main agreement has already paid the tax.

6.5 Are there any adverse consequences to a company that is a borrower (such as under thin capitalisation principles) if some or all of the lenders are organised under the laws of a jurisdiction other than your own? Please disregard withholding tax concerns for purposes of this question.

Under Argentine Income Tax Law (recently modified, please refer to question 6.1), thin capitalisation rules apply only to interest in respect of loans granted by foreign-related financial institutions (located in or with funds that do not arise from jurisdictions which are not considered non-cooperative jurisdictions) to Argentine residents or not. It establishes that interest on financial debts – without including the debts generated by acquisitions of goods, leases or services related to the business line – incurred with individuals, residents or not, will be deductible up to the annual amount that establishes the Executive Power or up to the equivalent of 30% of the net income of the fiscal year that results before deducting both interest and amortisation, whichever is higher. The accumulated surplus in the previous three fiscal years may be added to this limit, as the amount of interest effectively deducted from the applicable limit is lower. The interest that could not be deducted may be added to those corresponding to the following five fiscal years. This limitation will not apply if the recipient of the interest payments is a non-related party.

If the lender is located in a non-cooperative jurisdiction (regardless of whether it is related or not) or in a low-tax jurisdiction, interest is deductible only at the moment it is paid and transfer pricing rules apply.

7 Judicial Enforcement

7.1 Will the courts in your jurisdiction recognise a governing law in a contract that is the law of another jurisdiction (a "foreign governing law")? Will courts in your jurisdiction enforce a contract that has a foreign governing law?

Yes. Parties are able to choose the laws that will govern the agreement as long as some connection to the system of the chosen law exists. Further, foreign law will only be valid to the extent that it does not contravene Argentine international public policy (i.e. criminal, tax, labour and bankruptcy laws). Also, rights associated with real estate are governed exclusively by local laws.

7.2 Will the courts in your jurisdiction recognise and enforce a judgment given against a company in New York courts or English courts (a "foreign judgment") without re-examination of the merits of the case?

Yes. In principle, the courts of Argentina will recognise as valid and will enforce judgments of foreign courts if they refer to monetary transactions, subject to the compliance with certain procedural conditions (*exequatur*).

7.3 Assuming a company is in payment default under a loan agreement or a guarantee agreement and has no legal defence to payment, approximately how long would it take for a foreign lender to (a) assuming the answer to question 7.1 is yes, file a suit against the company in a court in your jurisdiction, obtain a judgment, and enforce the judgment against the assets of the company, and (b) assuming the answer to question 7.2 is yes, enforce a foreign judgment in a court in your jurisdiction against the assets of the company?

In Argentina, the length of litigation disputes depends on the complexity of the case and on whether appeals to court rulings are admitted.

Assuming the lender's creditor is unsecured, it might take between three and six years to obtain and enforce a final judgment. The render of a final decision might be delayed if foreign legislation governs the relationship between the parties.

Argentine procedural rules provide a fast-track proceeding called "exequatur" for the recognition and enforcement of a foreign judgment, which might last between one and three years. Exequatur proceedings do not require a re-examination of the merits of the case.

Despite the estimation above, freezing injunctions might be granted by Argentine courts if procedural requirements are met.

7.4 With respect to enforcing collateral security, are there any significant restrictions which may impact the timing and value of enforcement, such as (a) a requirement for a public auction, or (b) regulatory consents?

In principle, there are no restrictions in order to enforce collateral security. Nevertheless, if the guarantor does not comply with its obligations, the creditor would have to file a suit in court.

Please refer to questions 2.6 and 7.3.

7.5 Do restrictions apply to foreign lenders in the event of (a) filing suit against a company in your jurisdiction, or (b) foreclosure on collateral security?

In order to file a suit against a company in Argentina, the foreign lender must prove, if it is a company, that it is duly incorporated under the laws of its country.

7.6 Do the bankruptcy, reorganisation or similar laws in your jurisdiction provide for any kind of moratorium on enforcement of lender claims? If so, does the moratorium apply to the enforcement of collateral security?

The Bankruptcy Law does not provide any kind of moratorium on enforcement of lender claims.

Please refer to question 8.1.

7.7 Will the courts in your jurisdiction recognise and enforce an arbitral award given against the company without re-examination of the merits?

Yes. Arbitral tribunals are competent in monetary disputes. The enforcement of the arbitral award will be as equal as the enforcement of a judgment.

Arbitral tribunals may not solve cases in which Argentine tribunals have exclusive jurisdiction, nor when there is an express prohibition against arbitration (e.g. certain provincial matters).

8 Bankruptcy Proceedings

8.1 How does a bankruptcy proceeding in respect of a company affect the ability of a lender to enforce its rights as a secured party over the collateral security?

Bankruptcy and reorganisation ("*concurso preventivo*") proceedings in Argentina generally cause personal actions to mutate into credit verifications ("*verificación de créditos y privilegios*") within the proceeding. All creditors with credits with cause or title prior to the debtor's petition for reorganisation proceedings, or a court's declaration of bankruptcy, must file their credit verification requests with the bankruptcy/reorganisation proceeding court.

Although the creditor does not have to wait until the credit filing procedure is finished before requesting the liquidation of the asset, the court will perform a summary examination of the documentation evidencing the creditor's preference and request the opinion of the trustee before carrying out the liquidation of the asset. During the reorganisation proceeding, security interest claims with respect to real guarantees shall continue its procedure before the court where they were initiated, provided that the creditors first verify their credits with the reorganisation proceeding's court.

Also, in the case of reorganisations, the court may, in the event of evident urgency or need, order the suspension for 90 days of any auction of property subject to a mortgage or a pledge ordered by any other judge.

A credit with a special preference has priority over credits with general preferences and unsecured credits. However, the recognition of these credits must be verified and accepted by the court, as explained in question 7.6.

Credits with special preferences will have priority on a specific asset, such as mortgages and pledges. This kind of preference can be enforced exclusively on the relevant assets and up to the proceeds of the liquidation of such asset.

8.2 Are there any preference periods, clawback rights or other preferential creditors' rights (e.g., tax debts, employees' claims) with respect to the security?

The court may determine a preference period of up to two years prior to the bankruptcy proceedings, depending on the date when insolvency was first evidenced.

Certain acts which occur during that preference period may be ineffective, such as: acts for which no consideration is given; debts paid prior to its maturity; and security interests obtained for a debt which is un-matured and which was originally unsecured.

There are two types of preferences:

(i) Special preferences, which are granted exclusively over certain specific assets of the debtor, e.g.: securities over the proceeds from the sale of the secured asset; expenses related to the assets that continue to be in debtor's possession; and salaries, etc.

(ii) General preferences, which are granted over all of the debtor's assets, e.g.: labour credits not subject to a special preference; social security debts; and certain personal expenses (such as funeral or medical costs), etc.

8.3 Are there any entities that are excluded from bankruptcy proceedings and, if so, what is the applicable legislation?

Yes. Among others, insurance companies, cooperative associations and public entities, such as the Nation, Provinces and Municipalities, the Catholic Church and embassies.

Financial institutions are, with a few exceptions, subject to general bankruptcy law. However, the Central Bank's cancellation of their banking licence is required, and they may not voluntarily enter into a reorganisation or bankruptcy proceeding.

8.4 Are there any processes other than court proceedings that are available to a creditor to seize the assets of a company in an enforcement?

Yes. The debtor may enter into out-of-court agreements with all or part of the creditors. A certain majority of unsecured creditors is required.

These agreements imply a debt restructure and are enforceable against all the unsecured creditors who executed it, including those that did not approve its content or voted against it.

To be enforceable against all unsecured creditors, the out-of-court agreement must be endorsed or validated by a competent court. Companies that are regulated by special insolvency rules (e.g., banks and insurance companies) cannot enter into this kind of proceeding.

9 Jurisdiction and Waiver of Immunity

9.1 Is a party's submission to a foreign jurisdiction legally binding and enforceable under the laws of your jurisdiction?

In principle, Argentine law allows parties of an international contract to submit to a foreign jurisdiction in matters of an economic nature.

9.2 Is a party's waiver of sovereign immunity legally binding and enforceable under the laws of your jurisdiction?

Yes. The waiver of sovereign immunity is valid under Argentine law (it should be expressly provided in the underlying agreement).

10 Licensing

10.1 What are the licensing and other eligibility requirements in your jurisdiction for lenders to a company in your jurisdiction, if any? Are these licensing and eligibility requirements different for a "foreign" lender (i.e. a lender that is not located in your jurisdiction)? In connection with any such requirements, is a distinction made under the laws of your jurisdiction between a lender that is a bank *versus* a lender that is a non-bank? If there are such requirements in your jurisdiction, what are the consequences for a lender that has not satisfied such requirements but has nonetheless made a loan to a company in your jurisdiction? What are the licensing and other eligibility requirements in your jurisdiction for an agent under a syndicated facility for lenders to a company in your jurisdiction?

There are no eligibility requirements in Argentina for lenders, agents or security agents, whether they are residents or foreigners, from the licensing perspective. A loan may be granted by, and the agent may be, an individual, a company, a bank, or any other entity.

In the case of loans granted by banks, the role of an agent is generally performed by a financial entity.

In principle, lenders do not need to be licensed or authorised to grant loans, provided that the financing activity is not performed on a regular basis. Otherwise, certain corporate and regulatory issues should be considered.

From a corporate standpoint, foreign companies are able to perform isolated acts in Argentina but if they want to perform their activities on a regular basis, a branch or a subsidiary must be established. For such purpose, foreign companies must: (i) evidence before the Public Registry the existence of the company; (ii) establish a domicile in Argentina; and (iii) justify the decision of establishing such branch or subsidiary, and appoint a legal representative.

From a regulatory perspective, if the activities performed by the lender fall under "financial intermediation" (intermediation between the supply and demand of financial resources on a regular basis), prior authorisation of the Central Bank is required. An activity shall be deemed financial intermediation if it combines both raising local or foreign funds and granting financing to third parties with such funds.

The activity in Argentina of the subsidiaries or representation offices of foreign financial entities is subject to regulation by the Central Bank, who will grant the required authorisation subject to the analysis of the backgrounds and responsibility of the foreign entity and its local office.

11 Other Matters

11.1 Are there any other material considerations which should be taken into account by lenders when participating in financings in your jurisdiction?

There are no other material considerations which should be taken into account.

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Australia

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1 Overview

1.1 What are the main trends/significant developments in the lending markets in your jurisdiction?

2017 was a good year for borrowers – with bank funding costs down and a scarcity of assets/names driving better pricing and terms for the borrowers who came to market, together with the emergence of many alternative sources of funding on competitive terms. These include a strong demand from the Australian debt capital markets (medium term notes) and US private placement markets for infrastructure borrowers. Strong corporates such as Sydney Airport, AMP Group and Ramsay continued to tap the syndicated loan markets.

On the more highly leveraged transactions, 2017 will be remembered as the year in which unitranche financings (such as iNova, Laser Clinics and Novotech) and Australian law-governed AUD-only Term Loan Bs (Camp Australia, Leap Legal/Infotrack and Craveable Brands) really made a big impact. While traditional senior/senior + holdco mezzanine leveraged loans continue to be used (e.g. Icon Cancer Care), some of the larger sponsors are now running dual-track financing strategies, forcing banks providing traditional syndicated loans to compete with unitranche financings provided by institutional lenders/debt funds.

1.2 What are some significant lending transactions that have taken place in your jurisdiction in recent years?

- Large corporate loans syndicated in the Asia-Pacific loan markets included Sydney Airport on its A$1.4 billion refinancing – voted KangaNews' syndicated loan deal of the year 2017, Transurban Group's A$1bn+ refinancing and the Port of Brisbane refinancing.
- The first Australian law standalone covenant-lite AUD Term Loan B facility for an Australian corporate, arranged by Goldman Sachs and JPMorgan for leading tech companies LEAP Legal Software and Infotrack and the senior and mezzanine AUD Term Loan B facilities for the debt recapitalisation of Craveable Brands.
- Significant acquisition financings including Carlyle/PEP's iNova acquisition, QIC/Goldman Sachs PIA/Pagoda Investment consortium's acquisition of Icon Cancer Care and KKR's acquisition of Laser Clinics Australia.

KWM was involved on all the above transactions (including on the vendor/bidder side).

2 Guarantees

2.1 Can a company guarantee borrowings of one or more other members of its corporate group (see below for questions relating to fraudulent transfer/financial assistance)?

Yes. However, corporate benefit and other requirements need to be considered. These issues are outlined below.

2.2 Are there enforceability or other concerns (such as director liability) if only a disproportionately small (or no) benefit to the guaranteeing/securing company can be shown?

The directors of a company owe a duty to the company to act for the benefit of the company in its best interests, with due care and diligence, in good faith and for a proper purpose. Directors must also avoid any conflict between a director's duty to the company and that director's personal interest. Directors must comply with these duties when resolving to give a guarantee.

In determining whether to grant a guarantee or provide security, directors may consider both direct benefits and indirect benefits of doing so. Indirect benefits may include that the provision of the guarantee is a requirement for the ongoing support of other members of the corporate group where the support also indirectly benefits the company. While it is not sufficient that the guarantee benefits the corporate group as a whole, a director of a wholly owned subsidiary may take into account the best interests of its holding company as long as the constitution of the company permits it to do so and the company is solvent at all relevant times.

A guarantee that does not commercially benefit a company may be voidable or, in a liquidation, the guarantee could be deemed an uncommercial transaction or unfair preference. A breach of duties by directors can result in civil and criminal penalties and personal liability for directors.

2.3 Is lack of corporate power an issue?

An Australian company has all the powers of an individual. This includes the power to give a guarantee. However those powers may be limited by the company's constitution.

Third parties dealing with a company are entitled to make certain statutory assumptions, including that the company's constitution has been complied with unless they know or suspect the assumption to be incorrect.

2.4 Are any governmental or other consents or filings, or other formalities (such as shareholder approval), required?

Shareholder approval is not strictly required except for public companies in connection with related party transactions, subject to certain exemptions, the most relevant being where the transaction is on arm's-length terms or is for the benefit of 100%-owned subsidiaries. For private companies, it remains good practice to get shareholders' approval.

If the provision of a guarantee constitutes financial assistance, such as a guarantee of a loan used to assist the acquisition of shares in the company, the financial assistance must either (a) not materially prejudice the interests of the company or its shareholders or the company's ability to pay its creditors, (b) be approved by shareholders and the shareholders of relevant holding companies, or (c) fit within another exception.

Transactions which involve consumers and small business are subject to additional requirements under national consumer protection legislation.

2.5 Are net worth, solvency or similar limitations imposed on the amount of a guarantee?

There are no specific requirements of this nature that apply in addition to the corporate benefit requirements outlined above. However, guarantees given while a company is insolvent/nearly insolvent or which render a company insolvent can be set aside by a liquidator. Directors may also be subject to personal and criminal liability for entering into such guarantees.

2.6 Are there any exchange control or similar obstacles to enforcement of a guarantee?

There are no exchange controls that would prevent payment under a guarantee or restrict enforcement of a guarantee. However, Australian sanctions laws prohibit dealings with designated persons and entities in various countries.

3 Collateral Security

3.1 What types of collateral are available to secure lending obligations?

Most assets are available to secure lending obligations, subject to applicable contractual restrictions and, in limited cases, statutory restrictions. The regimes which apply to taking security differ according to whether the collateral is "personal property", in which case the *Personal Property Securities Act 2009* (Cth) ("**PPSA**") applies, or whether the collateral is real property, in which case State and Territory-based real property legislation applies.

The PPSA is modelled on the Canadian and New Zealand Acts and shares similarities with Art. 9 of the Uniform Commercial Code. Generally speaking, security interests are interests in personal property that secure payment or performance and include some "deemed security interests" (such as certain leases of personal property and assignments of certain receivables) which may not secure payment or performance.

3.2 Is it possible to give asset security by means of a general security agreement or is an agreement required in relation to each type of asset? Briefly, what is the procedure?

Yes. A general security agreement ("**GSA**") granting general security over all or substantially all of the present and future assets of the grantor is routinely entered into. It is also possible to take security over one or more types of specific assets under a specific security agreement ("**SSA**") (e.g. shares in a company, book debts, deposit accounts, goods). Otherwise, it is not usual to provide for security over different collateral classes in separate documents.

A GSA will typically cover all real and personal property. However, if the collateral is land and the land is material to the security package, separate real property mortgages are also usually entered into and registered on the appropriate real property register for priority perfection purposes.

The PPSA provides for perfection of a security interest in personal property by one of three means:

- registration on the Personal Property Securities Register ("**PPSR**") – this is the most common method of perfection;
- in the case of goods and certain intangible rights, possession by the secured party; or
- in the case of certain financial assets (including shares and bonds), control by the secured party.

It is not mandatory to perfect security interests governed by the PPSA, but if they are not perfected, then:

- they vest in the grantor immediately upon the grantor entering voluntary administration, bankruptcy or liquidation;
- a competing secured party may have a higher priority interest; and/or
- third parties may acquire an interest in the collateral free of the secured party's interest.

Australian law recognises fixed charges (or, using PPSA terminology, security interests over "non-circulating assets") and floating charges (security interests over "circulating assets").

3.3 Can collateral security be taken over real property (land), plant, machinery and equipment? Briefly, what is the procedure?

Yes.

Security over interests in land typically takes the form of a registered mortgage. Separate State and Territory laws regulate interests in land including real property mortgages and set out the applicable registration procedure.

Security over plant, machinery and equipment is usually taken under a GSA or SSA. Since plant, machinery and equipment (as long as they are not fixtures attached to land) are personal property, security over them is registrable on the PPSR.

3.4 Can collateral security be taken over receivables? Briefly, what is the procedure? Are debtors required to be notified of the security?

Yes.

Security over receivables can be taken under a GSA or an SSA.

If a "fixed charge" over receivables is required, the secured party must control dealings by the grantor with the receivables and register that it has control.

There is no requirement to notify the debtor in order to perfect the security interest or to obtain priority over other security interests. However, the secured party may wish to do so to obtain legal title to the receivables and the legal right to enforce in its name and power to give a good discharge.

3.5 Can collateral security be taken over cash deposited in bank accounts? Briefly, what is the procedure?

Yes.

Security over accounts with a bank or an approved deposit-taking institution (an "**ADI**") can be taken under a GSA or an SSA.

An ADI with a security interest in an ADI account held with it is taken to have perfected its security interest by control and need not take any steps to perfect its security interest in that account. However, any other person who takes a security interest in an ADI account can only perfect their security interest by registration on the PPSR.

If a "fixed charge" is required over a bank account or ADI account, the secured party must control dealings by the grantor with the account and register that it has control.

3.6 Can collateral security be taken over shares in companies incorporated in your jurisdiction? Are the shares in certificated form? Can such security validly be granted under a New York or English law governed document? Briefly, what is the procedure?

Yes.

Security over shares in a company can be taken under a GSA or an SSA.

Shares in unlisted Australian companies are generally certificated. It is market practice in Australia that security over certificated shares is perfected by control (i.e. secured party holding share certificates and blank share transfer forms) as well as by registration on the PPSR.

Shares in listed Australian companies are uncertificated and are recorded on an electronic register. They are transferred in accordance with Australian Securities Exchange rules. In addition to registration on the PPSR, control is obtained by the secured party entering into an agreement with a "controlling participant" to regulate dealings with the shares in the clearing system.

Even though an English or New York law-governed document can create valid security over shares in an Australian company, an Australian law-governed GSA or SSA is the preferred technique used in practice, given Australian law is likely to govern the validity and perfection of the security under conflicts of law rules in the PPSA and at general law.

3.7 Can security be taken over inventory? Briefly, what is the procedure?

Yes.

Security over inventory can be taken under a GSA or an SSA.

If a "fixed charge" over inventory is required, the secured party must control dealings by the grantor with the inventory and register that it has control.

It is not usual for a secured party to take control over inventory as the grantor will need the freedom to deal with it in the ordinary course of business.

3.8 Can a company grant a security interest in order to secure its obligations (i) as a borrower under a credit facility, and (ii) as a guarantor of the obligations of other borrowers and/or guarantors of obligations under a credit facility (see below for questions relating to the giving of guarantees and financial assistance)?

Yes. This is subject to corporate benefit, financial assistance requirements and other issues mentioned in this paper.

3.9 What are the notarisation, registration, stamp duty and other fees (whether related to property value or otherwise) in relation to security over different types of assets?

Notarisation is not required under Australian law. The duty and fees associated with taking security in Australia are registration fees.

The fees for registering a security interest on the PPSR are nominal. Such registration can be made for seven years, 25 years or no stated end time.

The fees for registering a real property mortgage vary between States and Territories, but are similarly nominal, other than in South Australia and Queensland.

3.10 Do the filing, notification or registration requirements in relation to security over different types of assets involve a significant amount of time or expense?

No. There is no significant time or expense, and registrations on the PPSR are instantaneous. However, the PPSR registration system is highly prescriptive and invalidating errors are easy to make, so care needs to be taken to ensure that registrations are correctly made.

3.11 Are any regulatory or similar consents required with respect to the creation of security?

Foreign lenders and foreign beneficiaries of security over Australian assets may need to consider the application of the Australian Government's Foreign Investment legislation, which is administered by the Foreign Investment Review Board ("**FIRB**"). Under some circumstances, notification and FIRB approval is required before taking or enforcing security.

In general terms, if security over Australian assets is held in the ordinary course of carrying on a business of lending money and solely as security for the purposes of a moneylending agreement, then a moneylender exemption will usually apply. The moneylender exemption also covers the acquisition of an interest by way of enforcement of a security held solely for the purposes of a moneylending agreement. Where the exemption applies, notification and FIRB approval is not required when taking or enforcing the security.

A "moneylending agreement" is defined to mean:

(a) an agreement entered into in good faith, on ordinary commercial terms and in the ordinary course of carrying on a business (a moneylending business) of lending money or otherwise providing financial accommodation, except an agreement dealing with any matter unrelated to the carrying on of that business; and

(b) for a person carrying on a moneylending business, or a subsidiary or holding entity thereof, an agreement to acquire an interest arising from a moneylending agreement (within the meaning of paragraph (a)).

For foreign government investors, the moneylender exemption requires that if an interest is acquired by way of enforcement of a security, that interest is disposed of (or a genuine sale process is commenced) within six months of the acquisition (or 12 months for an ADI), otherwise separate FIRB approval is required.

A foreign government investor includes a body politic of a foreign country, foreign governments, their agencies or related entities from a single foreign country that have an aggregate interest (direct or indirect) of 20% or more in the entity (or 40% or more if from multiple foreign countries), or if the entity is otherwise controlled by foreign governments, their agencies or related entities, and any associates, or could be controlled by them including as part of a controlling group.

3.12 If the borrowings to be secured are under a revolving credit facility, are there any special priority or other concerns?

No. If the security taken is perfected (whether by registration, control or possession), there are no specific priority concerns just because the security secures a revolving credit facility.

3.13 Are there particular documentary or execution requirements (notarisation, execution under power of attorney, counterparts, deeds)?

Australian documentary and execution requirements are not particularly onerous. Notarisation is not required.

An Australian company will generally sign in accordance with s. 127 of the *Corporations Act 2001* (Cth) ("**Corporations Act**") (by two directors, a director and secretary, or the sole director and secretary) because certain assumptions as to corporate authority can be relied upon by the counterparty. However, it is also common for Australian companies to sign under a power of attorney.

The execution of deeds by some foreign companies can present some minor logistical issues to ensure that the execution is valid; however, these issues are generally broadly understood in the market.

4 Financial Assistance

4.1 Are there prohibitions or restrictions on the ability of a company to guarantee and/or give security to support borrowings incurred to finance or refinance the direct or indirect acquisition of: (a) shares of the company; (b) shares of any company which directly or indirectly owns shares in the company; or (c) shares in a sister subsidiary?

A company is prohibited from financially assisting the acquisition of its shares or shares in its holding company, other than as set out below. A breach of the financial assistance provisions will not affect the validity of the transaction but can lead to civil offences for persons involved in the contravention and may lead to criminal offences where the breach was dishonest.

(a) Shares of the company

A company can give financial assistance if it either: (a) does not materially prejudice the interests of the company or its shareholders or the company's ability to pay its creditors; or (b) the financial assistance is approved by shareholders and the shareholders of relevant holding companies. There are some other fact-specific exemptions. Approval by shareholders of a company (first company) and the shareholders of the ultimate Australian holding company of the first company is referred to as a "whitewash" procedure and is routinely sought unless it is clear that there is no material prejudice to the interests of the company, its shareholders or its ability to pay creditors. The procedure involves lodging the shareholder approval documents with the Australian Securities and Investment Commission ("**ASIC**"). A 14-day waiting period applies before the financial assistance can be given.

(b) Shares of any company which directly or indirectly owns shares in the company

The financial assistance provisions also apply in situations where the financial assistance relates to shares being acquired in a holding company of the company giving the financial assistance. A holding company is any company that holds more than 50% of the shares, possesses more than 50% of the voting rights or otherwise controls the company board.

(c) Shares in a sister subsidiary

The financial assistance prohibition does not apply to the acquisition of shares in sister subsidiaries.

5 Syndicated Lending/Agency/Trustee/Transfers

5.1 Will your jurisdiction recognise the role of an agent or trustee and allow the agent or trustee (rather than each lender acting separately) to enforce the loan documentation and collateral security and to apply the proceeds from the collateral to the claims of all the lenders?

The use of agents for lenders and security trustees in syndicated lending agreements is common market practice in Australia.

Lenders will typically appoint an agent to represent them (in a non-fiduciary capacity), to perform defined administrative duties, to liaise with the borrower and security providers and to coordinate the lender group.

In most cases, security for a syndicated loan is granted to a security trustee who is able to enforce the security at the direction of the lenders (or the agent for the lenders) and is required to distribute the proceeds of enforcement in accordance with the security trust deed.

5.2 If an agent or trustee is not recognised in your jurisdiction, is an alternative mechanism available to achieve the effect referred to above which would allow one party to enforce claims on behalf of all the lenders so that individual lenders do not need to enforce their security separately?

This is not applicable in Australia.

5.3 Assume a loan is made to a company organised under the laws of your jurisdiction and guaranteed by a guarantor organised under the laws of your jurisdiction. If such loan is transferred by Lender A to Lender B, are there any special requirements necessary to make the loan and guarantee enforceable by Lender B?

Transfer and substitution mechanics are typically documented in the facility agreement and security trust arrangements. They set out the agreed manner in which rights and obligations of an outgoing lender are assigned or novated to an incoming lender with the consent of all parties where required. Other than the specified documentary requirements (including obtaining necessary consents), nothing additional is required.

In some circumstances, depending on the location of the loan and security, stamp duty may be chargeable in connection with an assignment of a loan.

6 Withholding, Stamp and Other Taxes; Notarial and Other Costs

6.1 Are there any requirements to deduct or withhold tax from (a) interest payable on loans made to domestic or foreign lenders, or (b) the proceeds of a claim under a guarantee or the proceeds of enforcing security?

Australia levies interest withholding tax ("**IWT**") on interest payments (which is broadly defined for these purposes and includes amounts in the nature of, or in substitution for, interest and certain other amounts) under debt interests made by an Australian borrower in Australia to an offshore lender, unless an exemption applies. The rate of IWT is 10% of the gross amount of interest paid.

Some common exemptions to this are:

- a lending that is an issuing of "debentures" (such as bonds and notes) or a "syndicated loan" which results from a public offer made in a particular manner; and
- the "financial institution" exemption which is contained in certain double tax treaties which the Australian government has with a number of countries.

Interest that is effectively connected with an Australian branch of a non-resident lender would be taxed in Australia on an assessment basis rather than a withholding tax basis.

It is currently unclear whether or not any payment by a guarantor under a guarantee on account of interest owing by the borrower would be subject to IWT. The better view is that such payments (other than interest paid on an overdue amount) do not constitute "interest" for IWT purposes, and, if so, would not be subject to IWT.

6.2 What tax incentives or other incentives are provided preferentially to foreign lenders? What taxes apply to foreign lenders with respect to their loans, mortgages or other security documents, either for the purposes of effectiveness or registration?

There are none in Australia.

6.3 Will any income of a foreign lender become taxable in your jurisdiction solely because of a loan to or guarantee and/or grant of security from a company in your jurisdiction?

In most cases, the entry by a foreign lender into a loan agreement with an Australian borrower or taking security over assets in Australia will not of itself subject the lender to income taxation in Australia. However, this will depend on the circumstances, including whether or not the lender conducts any other business or has any relevant presence in Australia.

6.4 Will there be any other significant costs which would be incurred by foreign lenders in the grant of such loan/guarantee/security, such as notarial fees, etc.?

None other than those discussed above.

6.5 Are there any adverse consequences to a company that is a borrower (such as under thin capitalisation principles) if some or all of the lenders are organised under the laws of a jurisdiction other than your own? Please disregard withholding tax concerns for purposes of this question.

Australia has thin capitalisation rules which restrict interest deductions if the amount of debt used to finance Australian operations exceeds specified limits subject to safe harbours including *de minimis* exemptions.

The thin capitalisation rules apply to all debt interests, including debt advanced by related and unrelated lenders, whether Australian or foreign, and therefore are not restricted to debt advanced by a foreign lender.

Any cross-border debt financing into Australia must also comply with Australia's transfer pricing rules. The parties should be dealing on an arm's-length basis and the debt should be priced having regard to arm's-length conditions.

7 Judicial Enforcement

7.1 Will the courts in your jurisdiction recognise a governing law in a contract that is the law of another jurisdiction (a "foreign governing law")? Will courts in your jurisdiction enforce a contract that has a foreign governing law?

In Australia, parties to a contract are free to select the governing law of the contract. However, to be enforceable, the choice of law must be made in good faith and must not contravene public policy.

7.2 Will the courts in your jurisdiction recognise and enforce a judgment given against a company in New York courts or English courts (a "foreign judgment") without re-examination of the merits of the case?

England

Generally yes, subject to fulfilment of registration requirements.

Under the *Foreign Judgments Act 1992* (Cth) and related regulations, English judgments can be registered and take on the status of an Australian judgment, subject to satisfying the following requirements:

- the judgment needs to be a "money judgment". That is, it must be a judgment under which money is payable;
- the judgment must not be under appeal;
- the judgment must not be wholly satisfied;
- the judgment must be enforceable in England; and
- the application for registration must be within six years of the date of the English judgment.

New York

There is no reciprocal bilateral arrangement for recognition of judgments between Australia and the United States. Instead, common law principles for recognition and enforcement of foreign judgments apply. To be enforceable at common law:

- the judgment must be final and conclusive;
- the New York court must have exercised its jurisdiction over the defendant;
- the defendant must have submitted (or be deemed to have submitted) to the jurisdiction of the New York court; and
- the judgment must be for a monetary sum.

7.3 Assuming a company is in payment default under a loan agreement or a guarantee agreement and has no legal defence to payment, approximately how long would it take for a foreign lender to (a) assuming the answer to question 7.1 is yes, file a suit against the company in a court in your jurisdiction, obtain a judgment, and enforce the judgment against the assets of the company, and (b) assuming the answer to question 7.2 is yes, enforce a foreign judgment in a court in your jurisdiction against the assets of the company?

It is not possible to specify a typical timeframe to finalise enforcement against assets. The timetable will be subject to variables including the type and complexity of the claim, the exact nature of the enforcement process, whether a formal insolvency process or liquidation is involved and whether the borrower or guarantor is cooperative.

7.4 With respect to enforcing collateral security, are there any significant restrictions which may impact the timing and value of enforcement, such as (a) a requirement for a public auction, or (b) regulatory consents?

The process of enforcement will be governed by the terms of the security documents and loan agreements, the PPSA and the Corporations Act.

In most circumstances, no regulatory consents are required in order to enforce. However, as set out in question 3.11, FIRB approval may be an issue in limited circumstances.

Restrictions also apply to enforcing collateral security in the event of insolvency, dependent upon the type of insolvency proceedings undertaken. We discuss this in section 8 below.

A receiver appointed by creditors under a security document is subject to statutory duties. This includes an obligation to sell collateral at market value or, if market value is not known, at the best price reasonably obtainable. While this does not in itself require a public auction, in many circumstances, a public auction or other transparent sale process will be required in order to demonstrate that the receiver has complied with its duties. This may have timing implications for recovery depending on the nature of the assets involved.

7.5 Do restrictions apply to foreign lenders in the event of (a) filing suit against a company in your jurisdiction, or (b) foreclosure on collateral security?

Subject to our comments about FIRB in question 3.11, there are no restrictions which apply specifically to foreign lenders.

7.6 Do the bankruptcy, reorganisation or similar laws in your jurisdiction provide for any kind of moratorium on enforcement of lender claims? If so, does the moratorium apply to the enforcement of collateral security?

In administration, there is a moratorium which runs from the date an administrator is appointed. Administration can be commenced in a number of ways, including by the directors of the company or a person with a perfected security interest over the whole or substantially the whole of the property of the company (the latter being a "**Substantial Chargee**").

The length of this moratorium period varies and the moratorium prohibits any enforcement proceedings being commenced against the company or in relation to its property. However, a Substantial Chargee can enforce its security interest during a decision period of 13 business days from notice of commencement of the administration. Other exceptions include enforcement with the administrators' consent or leave of the court.

While an Australian company is in liquidation, a person is prohibited from commencing or proceeding with civil proceedings except by leave of the court. This prohibition does not apply to a secured party's right to realise or otherwise deal with its perfected security interest.

See also question 8.1 below.

7.7 Will the courts in your jurisdiction recognise and enforce an arbitral award given against the company without re-examination of the merits?

Yes, an award made in an international arbitration with a seat in one of the Contracting States to the *United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards (New York, 10 June 1958*) (the "**New York Convention**") will generally be recognised and enforced by Australian courts, as if the award were a judgment or order of that court. Australian courts will not re-examine the merits of the arbitral award.

There are limited grounds upon which the court may refuse to enforce the foreign award under Article V of the New York Convention.

8 Bankruptcy Proceedings

8.1 How does a bankruptcy proceeding in respect of a company affect the ability of a lender to enforce its rights as a secured party over the collateral security?

This depends on the type of bankruptcy proceedings undertaken.

See also question 7.6 above.

The Australian Government has recently introduced new "safe harbour" and "*ipso facto*" laws.

The "*ipso facto*" laws will apply to contracts, agreements and arrangements entered into on or after 1 July 2018, to impose a stay on contractual counterparties of companies who become subject to any of the following procedures: administration; implementing a scheme of arrangement to avoid being wound up in insolvency; or receivership. The stay will apply to express rights arising for the following reasons: (1) the company being subject to the procedure; (2) the company's financial position during the procedure; (3) a reason prescribed in the regulations relating to the company possibly being subject to the procedure or the company's financial position; or (4) a reason in substance contrary to the stay. The stay also applies to self-executing rights; i.e. rights that apply automatically without a party taking action.

Importantly, the stay will not apply to, *inter alia*: (1) if a company is in administration, a Substantial Chargee's rights to take enforcement action during the 13-business day "decision period" commencing from the company entering into administration; (2) drawstops, i.e. a creditor is not forced to advance new money; (3) contracts or arrangements entered during the procedure; (4) a right prescribed in the regulations (yet to be published as at the date of this chapter); or (5) consent of the administrator, scheme administrator receiver or liquidator, as applicable officer or a right if a court so orders.

The impact of these "*ipso facto*" reforms on lending practices is wide-ranging. With the regulations still to be published, market participants will need to seek detailed advice before undertaking their next transaction.

8.2 Are there any preference periods, clawback rights or other preferential creditors' rights (e.g., tax debts, employees' claims) with respect to the security?

A liquidator can seek court orders to set aside certain transactions entered into or where steps were taken to give effect to the transaction in a period before the external administration (i.e. the "**hardening period**"). This may include making payments or granting security. In relation to security, the key "voidable transactions" are:

- uncommercial transactions – a transaction which was entered into by a company when it was insolvent or as a result of which the company becomes insolvent and which a reasonable person would not have entered into; and
- unfair preferences – where there is a shortfall in security, a transaction between an insolvent company and a creditor under which that creditor receives more for its unsecured debt than it would have in a winding up.

Below is a summary of the hardening periods:

Transaction	Not related party	Related parties
Unfair preference	6 months	4 years
Uncommercial transactions	2 years	4 years
Unreasonable director-related transactions	N/A	4 years
Obstruction of creditors' rights	10 years	
Unfair loan	Indefinite	

Security interests over circulating assets (including receivables, inventory and cash in bank accounts) which are not subject to control:

(a) may be void as against a liquidator if it was created within six months of the external administration and the company was insolvent, except insofar as it secures a new advance; and

(b) will rank in a winding up behind certain statutorily preferred creditors such as employee entitlements and administrator's indemnity for debts and remuneration.

Normal directors' duties also apply to a director's decision to grant security (see question 2.2 above), and if security has been granted in breach, secured lenders may be subject to clawback risk under concepts of knowing receipt/knowing assistance. The "hardening period" is six years.

8.3 Are there any entities that are excluded from bankruptcy proceedings and, if so, what is the applicable legislation?

No. However, banks, other ADIs and insurers are subject to different and specific insolvency regimes under legislation including the *Banking Act 1959* (Cth) and the *Insurance Act 1973* (Cth).

8.4 Are there any processes other than court proceedings that are available to a creditor to seize the assets of a company in an enforcement?

Yes. A secured party may enforce its security by appointing a receiver (or receiver and manager) or entering into possession as mortgagee in possession.

Appointment and powers of a receiver or mortgagee in possession is governed by the terms of the security document. The PPSA also provides certain notice requirements which may apply to enforcement against personal property. In addition, the PPSA provides a range of statutory enforcement options – these do not apply where a privately appointed receiver or other controller is realising assets of a corporate borrower or guarantor, but do apply to other controllers. The PPSA provisions are, in many instances, contracted out of.

Where the relevant security is a real property mortgage, a secured party can also either appoint a receiver or enter into possession as mortgagee under the relevant State or Territory laws. A mortgagor can restrain the sale where it can be shown that the power of sale has not become exercisable or the mortgagee is in breach of the duty to sell.

Some statutes may provide other remedies as well.

9 Jurisdiction and Waiver of Immunity

9.1 Is a party's submission to a foreign jurisdiction legally binding and enforceable under the laws of your jurisdiction?

Yes. Under the *Foreign Judgments Act 1991* (Cth), a party's submission to a foreign jurisdiction is legally binding and enforceable in Australia provided that the subject matter is not illegal and not contrary to public policy.

9.2 Is a party's waiver of sovereign immunity legally binding and enforceable under the laws of your jurisdiction?

As a general rule, a party's waiver of sovereign immunity will be legally binding and enforceable under the *Foreign States Immunities Act 1985* (Cth).

10 Licensing

10.1 What are the licensing and other eligibility requirements in your jurisdiction for lenders to a company in your jurisdiction, if any? Are these licensing and eligibility requirements different for a "foreign" lender (i.e. a lender that is not located in your jurisdiction)? In connection with any such requirements, is a distinction made under the laws of your jurisdiction between a lender that is a bank *versus* a lender that is a non-bank? If there are such requirements in your jurisdiction, what are the consequences for a lender that has not satisfied such requirements but has nonetheless made a loan to a company in your jurisdiction? What are the licensing and other eligibility requirements in your jurisdiction for an agent under a syndicated facility for lenders to a company in your jurisdiction?

If a person provides a "financial service", it must obtain an Australian Financial Services Licence from ASIC under the Corporations Act and comply with a range of conduct obligations. Although loan facilities are excluded from the Corporations Act, issuing, acquiring or arranging a derivative, swap or deposit product will constitute a financial service, as will providing advice in connection with those products.

There are no licensing or registration requirements in Australia that apply specifically to entities that act as an agent or security trustee.

Approval is required from the Australian Prudential Regulation Authority ("**APRA**") before an entity (including a bank) carries on banking business in Australia. The use of the word "bank", "banking", "credit union" and related words when a company or bank carries on business in Australia is also restricted unless the company is registered as a bank or has approval from APRA.

In most cases, the making of a single loan in Australia or taking of security in Australia by any entity does not require the lender or secured party to be registered with ASIC as a foreign company. However, this is a complex issue that depends on the circumstances including the amount of business that the entity carries on in Australia and the presence that the entity has in Australia.

Registration and reporting requirements apply under the *Financial Sector (Collection of Data) Act 2001* (Cth) ("**FSCODA**") to lenders, depending on the nature and scale of their lending activities in Australia. Generally, if 50% of a lender's assets in Australia consist of debts due to them from the provision of finance, then they will be registrable with APRA under the FSCODA.

Registration with the Australian Transaction Reports and Analysis Centre and compliance with the *Anti-Money Laundering and Counter-Terrorism Financing Act 2006* (Cth) will be required for loans made at or through the lender's (or its agent's) permanent establishment in Australia.

Breaches of applicable legislation may results in fines or penalties being imposed.

11 Other Matters

11.1 Are there any other material considerations which should be taken into account by lenders when participating in financings in your jurisdiction?

The issues outlined above provide a general overview of the main legal considerations which are most likely to be relevant to secured lenders in Australia.

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- Banking Law Firm of the Year, ALB China Law Awards 2016 and 2017.
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Chapter 29

Austria

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1 Overview

1.1 What are the main trends/significant developments in the lending markets in your jurisdiction?

Lending markets in Austria have continued to improve over the last few years. Not much different from other jurisdictions, this is certainly a result of a trend of overall recovery from the financial crisis and the general economic upturn, which has improved the demand for corporate and non-corporate loans.

Factors which became significantly more important for the overall strategies of the banks' lending business include the regulatory framework, such as the framework regulating the determination of risk-weighted assets and of own funds.

Austrian credit institutions have also continued to deal with their fair share of non-performing loans, which kept the market on trading with such non-performing loans active.

Financial markets have also caused, in respect to "negative interest rates", Austrian banks to implement a minimum interest rate of 0% in corporate and retail loan agreements. This led to lawsuits involving the Austrian Consumer Protection Association. The Austrian Supreme Court has rendered several decisions, stating that zero floor clauses violate Sec. 6 para 1 cif 5 Austrian Consumer Protection Act, if they are not accompanied by an interest cap protecting the borrower against high interest rates. However, the Supreme Court also stated that banks are not obliged to pay "negative" interest to their borrowers if the agreed reference value (e.g. EURIBOR or LIBOR) becomes negative. All decisions issued to date in respect of zero floor clauses relate to consumer loans. Thus, it is unclear thus far if the principles applied by the courts to consumer credits also apply to loans granted to corporate borrowers.

The Act on the Recovery and Resolution of Banks (*Sanierungs- und Abwicklungsgesetz* (BaSAG), implementing the Bank Recovery and Resolution Directive 2014/59/EU (BRRD)) covers CRR credit institutions and CRR investment firms, including certain CRR financial institutions, financial holding companies and branches of third-country institutions to the extent they are part of a group of credit institutions. BaSAG, which came into effect on 1 January 2015, requires "recovery plans" to be drawn up by institutions to identify impediments and outline measures which could guarantee effective resolutions. The impact of this Act to the lending market might be described as having a confidence-building effect, in particular with respect to the syndicated loan market.

Additionally, particularly in syndicated loan scenarios, the Austrian Act on Financial Collateral (*Finanzsicherheiten-Gesetz* (FinSG)), which regulates the granting and enforcement of financial collateral arrangements between participants in the financial markets, becomes more and more important. The FinSG provides for wider and less regulated means of enforcement of the collateral and in particular, the FinSG provides for the option to agree on an immediate realisation of the collateral if an insolvency, liquidation, or reorganisation proceeding is opened against the collateral provider.

1.2 What are some significant lending transactions that have taken place in your jurisdiction in recent years?

One significant lending transaction in 2017 in Austria concerned AT&S Austria Technologie & Systemtechnik Aktiengesellschaft in connection with a hybrid bond with a total volume of EUR 175m. In 2016, STADA Arzneimittel AG issued a new promissory note to investors, whereby the volume amounted to EUR 350m at fixed as well as variable interest rates. Very recently, it has been reported that German Vonovia made an offer to take over the Austrian Buwog-Group, a publicly owned real estate holding, for EUR 5.2 billion, it being reported that Vonovia's take-over is to a great extent debt financed. Austrian infrastructure projects are frequently also subject to public financings which are usually linked to loans or guarantees issued by credit institutions. One major loan of that type is the European Investment Bank's EUR 400m financing of the Vienna Airport passenger terminal, with the involvement of Austrian credit institutions as guarantors. It is noteworthy to mention that there is also a general trend in the Austrian lending market to scrutinise long-term loans in terms of agreed interest *versus* market interest.

2 Guarantees

2.1 Can a company guarantee borrowings of one or more other members of its corporate group (see below for questions relating to fraudulent transfer/financial assistance)?

Austrian law does not restrict downstream guarantees (or other security). However, there are stringent limitations, which apply to upstream and side-stream guarantees provided by corporations (and equivalent entities).

As a basic principle, distributions to (direct or indirect) shareholders of a corporation (AG, GmbH, GmbH & Co KG, i.e., a limited partnership in which the only unlimited partner is a GmbH) may only be effected under specific circumstances, namely (a) in the form of formal dividend distributions based on a shareholders' resolution, (b) in the case of a capital decrease (which also requires a shareholders' resolution), or (c) in the form of a distribution of liquidation surplus. Besides that, it is recognised that a company and its shareholders may enter into transactions with each other on arm's-length terms and conditions. This requirement entails that the management of the company makes – prior to entering into such a transaction – a comprehensive assessment of a proposed transaction, in particular of the risks involved, and shall only enter into such transactions with its (direct or indirect shareholder or a sister company) if and to the extent that it would enter into the transaction on identical terms and conditions with any unrelated third party. However, the management must not enter into a transaction, if by any such transaction the existence of the company would be threatened.

To some extent, Austrian law jurisprudence also accepts specific corporate benefits as an adequate means of justification for granting upstream and side-stream guarantees. Such corporate benefit must not be disproportionate to the risk and must be specific and not only a general corporate benefit, such as a general "group benefit".

Austrian case law on these restrictions is based on a case-by-case evaluation and has become increasingly stringent over the last 20 years. In practice, it is advisable to have the management of the company assess the proposed transaction in accordance with the above criteria. Potential consequences of a breach of these Austrian capital maintenance rules include personal liability of the management as well as nullity of the respective transaction.

The above principles do not only apply in respect to funds or loans paid by a company but to all benefits granted by such company, including guarantees for borrowings.

2.2 Are there enforceability or other concerns (such as director liability) if only a disproportionately small (or no) benefit to the guaranteeing/securing company can be shown?

As discussed in question 2.1 above, a violation of the stringent capital maintenance rules will have the result of the transaction being made void. Only if transactions are *per se* (economically and as per the assumed intention of the parties, if they reasonably would have entered also in the remaining part of the transaction) dividable into separate parts, then Austrian jurisprudence holds that the violation of capital maintenance rules shall render the transaction partially void. Whether any such transaction (e.g. a guarantee) would be found by any competent court to be only partially or entirely void would be decided on a case-by-case basis, which therefore causes tremendous risks on the predictability of such type of transaction.

Shareholders and managing directors of corporations may be held personally liable for damages, if capital maintenance rules are violated. The provision of a guarantee/security for only a disproportionately small (or no) benefit would presumably constitute such a violation. In case of a violation, managing directors are liable for their own culpable behaviour; i.e. if they did not act in accordance with the standard of care of a prudent business man, provided that the directors' liability is in principle only towards the company, but not towards individual shareholders or creditors (although exceptions apply).

In order to mitigate the risks of nullity of a guarantee or personal liability of the management of the company providing the guarantee, it has become common practice in Austria to include limitation language, restricting the (potential) enforcement of upstream or cross-stream security arrangements to the maximum permissible extent under Austrian law. Since the validity of upstream or cross-stream guarantees needs to be subject to a case-by-case evaluation, any reliance on stream or cross-stream guarantees and the according use of limitation language causes ambiguities and is likely to decrease the commercial value of such guarantees.

2.3 Is lack of corporate power an issue?

Austrian companies are generally not subject to the *ultra vires* doctrine. Internal restrictions, which may be based on organisational regulations or on internal approval procedures (e.g. if the supervisory board has to consent to a measure), are allowed and very common, but they generally have no effect on the validity of agreements with third parties. However, such internal restrictions may have to be observed; e.g. in cases where the third party was aware of the excess of corporate power by the corporations' representative and if the damage to the company resulting therefrom must have been obvious to such third party or if the management and the third party had acted collusively with the management to the company's detriment.

2.4 Are any governmental or other consents or filings, or other formalities (such as shareholder approval), required?

The Austrian Banking Act (*Bankwesengesetz*) requires a banking licence to be issued by the Austrian regulator (Financial Market Authority) for the lending business, i.e. the commercial providing of financing to borrowers. Notified licences of a credit institution domiciled in another European economic area (EEA) jurisdiction (based on the home Member State concept) will be held equivalent for that purpose. The same applies for the acquisition of (loan) receivables on a commercial basis (i.e., factoring) which, in principle, prevents work-around-structures, such as the disbursement of a loan by an Austrian "fronting bank" and immediate acquisition of the loan by a foreign, non-licensed lender. Limited exceptions to that principle apply, *inter alia*, to insurance companies granting loans for the purposes of creating a reserved asset base for the purpose of their insured persons/customers.

Limited exceptions also apply in the context of small-category financings such as crowd-funding which, in Austria, has only recently been regulated in statutory law and provides for exceptions from both the bank licence and capital markets' prospectus requirements, if and to the extent that a financing does not exceed certain thresholds.

Resolutions, such as shareholders' resolutions, are – as set out in question 2.3 – not a general requirement for the validity and enforceability for an act of the legal representative of an Austrian corporation (limitations may apply as set out in question 2.3). However, it is, especially with respect to larger/syndicated financings, standard market practice to obtain shareholder approvals for entering into a loan agreement, security agreement or other associated finance documents or to obtain capacity opinion, which will be based on the respective review of corporate resolutions.

2.5 Are net worth, solvency or similar limitations imposed on the amount of a guarantee?

Beside general limitations arising from capital maintenance rules (as discussed before) and customary contractual enforcement limitations, it shall be noted that guarantees, and the maximum amount owed under a guarantee, will be interpreted on a very strict basis and ambiguities in the wording of the guarantee may be interpreted by a court to the detriment of the beneficiary of the guarantee.

2.6 Are there any exchange control or similar obstacles to enforcement of a guarantee?

Under Austrian law, there are no such exchange controls which would pose obstacles to the enforcement of guarantees.

3 Collateral Security

3.1 What types of collateral are available to secure lending obligations?

The types of collateral that may be used in Austria to secure lending obligations can be divided into two general groups: on the one hand personal collateral; and *in rem* collateral on the other hand.

Most common types of personal collateral for securing lending obligations are (a) assumption of debt (*Schuldbeitritt*), (b) sureties (*Bürgschaften*), (c) guarantees, and (d) letters of comfort (*Patronatserklärungen*).

Most common types of *in rem* collateral are (a) pledge of assets (such as a pledge on movables or a mortgage), (b) transfer of title for security purposes (*Sicherungsübereignung*), (c) assignment for security purposes (*Sicherungszession*), and (d) retention of title (*Eigentumsvorbehalt*).

In lending transactions, the most common types of collateral are share pledges, mortgages, account pledges, assignment of current and future receivables, trademark and IP-right pledges, and sometimes the pledge on stock in warehouses (which, based on the very stringent law on perfection, basically requiring that the pledgee takes control over the stock, is difficult to establish and maintain).

3.2 Is it possible to give asset security by means of a general security agreement or is an agreement required in relation to each type of asset? Briefly, what is the procedure?

Austrian law does not recognise the concept of a general security interest in all (current and future) assets of the pledgee or the assignee. Due to the diversity of perfection requirements for the different types of collateral under Austrian law (e.g. entry into the land-book for mortgages, book entry for the assignment of claims as an alternative to the notification to the third-party debtors, the notification of the company when pledging shares in an Austrian Limited Liability Company) but also for reasons of enhancing the enforceability of collateral even in case one category of collateral was not perfected or is not enforceable for any reason, standard market practice is to have one security agreement for each asset class.

3.3 Can collateral security be taken over real property (land), plant, machinery and equipment? Briefly, what is the procedure?

Real property can be provided as security in the form of a pledge (mortgage). In order to become effective, such pledge must be agreed upon between the pledgor and the pledgee, where such pledge agreement does not require a specific form, but for perfection needs to be registered in the land register, where the real property that is being pledged is located. For the purpose of being entered into the land register, the pledgor of the property must provide a specific consent declaration regarding the registration (*Aufsandungserklärung*), which must be made in authenticated form. Multiple pledges over one individual property are possible and will be ranked towards each other in terms of priority (the point in time, when the application for registration of the pledge in the land register reaches the competent land register, the court is decisive). It is also possible to establish a mortgage over more than one property by creating a simultaneous mortgage (*Simultanhypothek*). The registration of a pledge over real property in the land register is subject to significant registration fees. The registration fee amounts to 1.2% of the secured amount of the real property. To avoid such fees in some lending scenarios, the lender agrees to receive a registrable (i.e. authenticated) pledge agreement, together with a ranking (*Rangordnungsbescheid*) which provides for a term of one year that no third party may enter in the specific rank another mortgage (which, however, due to the limited term of one year of such ranking order, the 0.6% fee of the secured amount associated with the entry of such ranking order and the fact that, only if the mortgage is registered will the critical period of rescission under insolvency laws start to run, which may by not practical in most lending scenarios).

A pledge of real estate generally extends also to any fixtures and accessories. Any equipment that is not connected to a real property in the sense of the preceding sentence is considered to be movable property. With regard to security agreements in respect to movables, no specific formal requirements must be observed. However, Austrian law imposes strict standards of perfection that either require a physical transfer of the pledged goods or any equivalent measure, such as handing over via declaration, in case the physical transfer would be too burdensome to be performed. The same strict perfection requirements are required in case of full title transfer of such goods for security purposes (in order to avoid circumvention).

Also, warehouse pledges are generally admissible under Austrian law, provided the stringent rules in respect to the perfection of the assets contained in the warehouse are observed, which basically requires signage of the goods and the appointment of a warehouse custodian, who shall be strictly bound by the instructions of the pledgee only and shall ensure that goods are only removed from the warehouse if so accepted by the pledgee.

3.4 Can collateral security be taken over receivables? Briefly, what is the procedure? Are debtors required to be notified of the security?

Security rights may be taken over receivables either by way of pledge or by way of full transfer of rights (for security purposes) via assignment.

According to Austrian law, in general, the transfer of receivables as such merely requires an agreement between the assignor and the assignee. As a general rule, while it is not necessary that each and every claim is specifically identified, any receivable that is to be assigned must be sufficiently identifiable. If the respective receivables are recorded in the creditor's/assignor's books, according to Austrian case law it is required that the pledge or assignment is annotated both in the list of obligors of the assignor as well as in the list of open accounts. As an alternative, the assignment of receivables may be also perfected by notification of the third-party debtors of such receivables. Provided that the receivables are sufficiently identified, it is also possible under Austrian law to assign (or pledge) future receivables.

Receivables pledges and security transfers may also extend to future receivables or certain categories of receivables, if and to the extent that such receivables are duly described in the security agreement.

3.5 Can collateral security be taken over cash deposited in bank accounts? Briefly, what is the procedure?

Under Austrian law, collateral security may be taken over cash deposited in bank accounts. Such cash collateral is commonly established in the form of account pledges, which are not subject to any special form requirements and therefore in practice principally drawn up in simple written form. In order to become perfected, the bank that holds the respective account must be notified (in its capacity as the third-party debtor).

The commonly used general terms and conditions of Austrian banks provide for a general pledge over all funds of a bank's customer for any funds transferred by customers into custody of the bank (i.e. the funds of customers on bank accounts). This standard pledge agreement contained in the general terms and conditions is typically waived or subordinated if the funds on bank accounts are pledged for security purposes for a pledgee other than the bank holding the account.

3.6 Can collateral security be taken over shares in companies incorporated in your jurisdiction? Are the shares in certificated form? Can such security validly be granted under a New York or English law governed document? Briefly, what is the procedure?

Security rights over shares in a Limited Liability Company (*Gesellschaft mit beschränkter Haftung – GmbH*) are generally created by way of pledge. While the actual transfer of GmbH shares requires a notarial deed, a share pledge may be done in (simple) writing form. For the perfection of the GmbH share pledge, the notification of the company is required. In practice, share pledges are commonly made together with a power of attorney for the sale of the shares in case of an event of default by the pledgee, whereby such power of attorney needs to be executed by the pledgor in authenticated form to comply with the requirement that a power of attorney for the sale of shares in a GmbH has to be authenticated.

The pledge of shares of a Stock Corporation (*Aktiengesellschaft*) differs from the pledge of GmbH shares, as shares of an AG are typically certificated as securities, which is especially reflected in the different perfection requirements. In contrast to the GmbH, the sale of shares in AGs requires no specific form and thus, powers of attorney for the sale, if any, are not required to be authenticated.

Generally, the perfection of *in rem* securities over movables (such as certificated securities) requires that the pledgee obtains direct or indirect (e.g. via the account bank) possession in the shares. Only shares in stock-exchange listed companies may be certificated as bearer shares (*Inhaberaktien*). This is effected through a global share certificate with the shares then being introduced into an electronic clearing system. In such case, a pledge may be created by transferring the shares to the pledgee's securities deposit account or by blocking the pledgor's account in the pledgee's favour.

3.7 Can security be taken over inventory? Briefly, what is the procedure?

As set out in question 3.3, Austrian law imposes strict standards of perfection for all kind of movables, including inventories, and either requires a physical transfer of the pledged goods to the pledgor (or its custodian) or any equivalent measure, such as handing over via declaration, in case the physical transfer would be too burdensome to be performed. In respect to inventory – as is the case with respect to general warehouse pledges – for perfection of the security, it will be necessary that the inventory is stored separately from all other goods of third parties and access to the inventory (and any release of inventory) is strictly observed – and subject to agreement by the pledgee – by a custodian of the pledgee.

3.8 Can a company grant a security interest in order to secure its obligations (i) as a borrower under a credit facility, and (ii) as a guarantor of the obligations of other borrowers and/or guarantors of obligations under a credit facility (see below for questions relating to the giving of guarantees and financial assistance)?

Subject to the limitations arising from the stringent capital maintenance rules under Austrian law there are no general obstacles under Austrian law that a company may at the same time under one credit facility grant security for its own obligations as borrower under such credit facility and grant security (or guarantee) for the obligations of other obligors under such guarantee facility (which is, e.g., regularly the case, if a holding company takes up the loan and guarantees as the borrower the obligations of all or certain of its direct and indirect subsidiaries).

3.9 What are the notarisation, registration, stamp duty and other fees (whether related to property value or otherwise) in relation to security over different types of assets?

Stamp duty is governed by the Stamp Duty Act (*Gebührengesetz*) and follows a strict civil approach, which is that stamp duty is levied on various legal transactions concluded in physical written form (but also electronically, such as via e-mail). Also, legal documents executed abroad can trigger stamp duty. Stamp duty is levied either when both parties to an agreement are Austrian residents or when the written document evidencing the transaction is brought to Austria in its original form or in the form of a notarised copy, provided that the legal transaction has legal effect in Austria; or a legal obligation is assumed under the legal document or will be performed in Austria. Furthermore, stamp duty may be also triggered if based on a written document another legal binding action occurs in Austria or if such document is used as evidence before authorities or courts.

The Stamp Duty Act provides for a wide variety of documents, which trigger stamp duty. Documents often used in connection with loan agreements include: sureties, which trigger a 1% stamp duty; assignment agreements, which trigger a 0.8% stamp duty; or mortgages, which trigger a 1% stamp duty.

The mere granting of a loan or the provision of a fully abstract guarantee does not trigger stamp duty. The Stamp Duty Act also provides a general exemption from stamp duty for legal transactions, which are directly linked and made for the purpose of securing claims arising from loan agreements (though application of such exemption has to be carefully considered).

When creating mortgages, the underlying pledge agreement must be authenticated to obtain registration in the land register. Notarisation fees usually depend on the value of the transaction. In addition, registration of mortgages in the land register triggers a registration fee of 1.1% of the fair value of the mortgage.

3.10 Do the filing, notification or registration requirements in relation to security over different types of assets involve a significant amount of time or expense?

Registers for perfection of security over assets exist in Austria for mortgages and – even though in principle an entry in the books of the owner of IP rights is also considered a permissible method of perfection of, e.g., trademark pledges – the trademark and patent register. Thus, only in respect of mortgages and IP rights will public authorities be involved in the perfection (registration) process of pledges. Registration of pledges in those registers shall usually be completed in a timeframe of up to two weeks. If timing is of the essence, informal pre-notification to the register is a practical means to ensure a swift process.

3.11 Are any regulatory or similar consents required with respect to the creation of security?

No regulatory or similar consents are required with respect to the creation of security. It shall be noted, however, that if, e.g., a mortgage is created or shares are pledged in a corporation owning real estate, the realisation of such collateral might be hampered by the fact that the acquisition of real estate by non-Austrian parties might be subject to restrictions as to real estate transfer in relation to foreign parties. Further, the realisation of pledges in shares or in a business may be subject to merger control.

3.12 If the borrowings to be secured are under a revolving credit facility, are there any special priority or other concerns?

No special priorities or other concerns exist in relation to the securing of revolving borrowings, provided that, if future claims are to be secured, such future claims must be clearly identifiable.

3.13 Are there particular documentary or execution requirements (notarisation, execution under power of attorney, counterparts, deeds)?

With regard to notarisations, see questions 3.3 and 3.6 above. Where a security agreement is executed on the basis of a power of attorney (*Vollmacht*), parties require authorisation pursuant to the power of attorney to be evidenced on the basis of a complete chain of corresponding powers certified by notaries or corresponding entries in commercial registers (*Firmenbuch*). In case a power of attorney is executed by a foreign company, a foreign notary may confirm the identity of the signatories and the content of the respective foreign commercial register. In some cases of foreign certification, an apostille is required.

4 Financial Assistance

4.1 Are there prohibitions or restrictions on the ability of a company to guarantee and/or give security to support borrowings incurred to finance or refinance the direct or indirect acquisition of: (a) shares of the company; (b) shares of any company which directly or indirectly owns shares in the company; or (c) shares in a sister subsidiary?

As set out in more detail in question 2.1 above, Austrian companies are subject to strict capital maintenance rules, which generally (subject to exemptions which are described in questions 2.1 above) do not permit up-stream guarantees or other up-stream securities. Thus, in case of acquisition of shares in a company, such acquisition must not be collateralised by shares of the target company. The same restrictions apply to "sister subsidiaries", if they are directly or indirectly subsidiaries of the target's direct and indirect shareholders.

On the other hand, down-stream collateral, such as shares in a direct or indirect shareholder company (holding company) of the target company, can serve as collateral for the acquisition financing without violating the down-stream collateral capital maintenance rules.

5 Syndicated Lending/Agency/Trustee/Transfers

5.1 Will your jurisdiction recognise the role of an agent or trustee and allow the agent or trustee (rather than each lender acting separately) to enforce the loan documentation and collateral security and to apply the proceeds from the collateral to the claims of all the lenders?

Accessory collateral, such as sureties or pledges, must not be separate from the underlying secured obligation, otherwise the collateral will cease. Therefore, the concept of "security trustees" or agents, as well as a generic type of "parallel debt" is not recognised under Austrian law to validly establish collateral for one "security agent" which is not at the same time a lender or not a lender in respect of all obligations which shall be secured by the (accessory) collateral. It is, therefore, market practice to include a parallel debt structure for the security trustee concerning security governed by Austrian law. In order to ensure accessory, the Austrian market practice either provides that all secured parties are at the same time pledgees (or direct beneficiaries) under the security agreements or that a "security agent" is appointed, whereby it is agreed among all lenders with the consent of the borrower (or other obligors) that such security agent is the joint and several creditor (*Gesamthandgläubiger*) of all claims, it being further agreed among all creditors that only the security agent shall (following a decision process among all lenders) have the right to enforce the collateral and will then distribute the proceeds from such enforcement among all lenders in proportion to their exposure under the secured obligations.

In respect of non-accessory collateral (e.g. guarantees), it is not required for their validity that they are directly connected with the secured obligation. However, since loan documentation typically includes accessory and non-accessory collateral, it is market practice to provide for joint and several creditorship if the lenders desire to execute their rights arising from the collateral via one security agent.

5.2 If an agent or trustee is not recognised in your jurisdiction, is an alternative mechanism available to achieve the effect referred to above which would allow one party to enforce claims on behalf of all the lenders so that individual lenders do not need to enforce their security separately?

As discussed in question 5.1, the most common lending practice provides that the (Austrian type of) security agent is a joint and several creditor (*Gesamthandgläubiger*) of all claims of any of the lenders.

5.3 Assume a loan is made to a company organised under the laws of your jurisdiction and guaranteed by a guarantor organised under the laws of your jurisdiction. If such loan is transferred by Lender A to Lender B, are there any special requirements necessary to make the loan and guarantee enforceable by Lender B?

In this context, it is necessary to observe that Austrian law differentiates between fully abstract guarantees (*Garantien*) and sureties (*Bürgschaften*).

Guarantees are considered to be separate non-accessory claims against the guarantor according to Austrian law. Therefore, generally, a guarantee would need to be assigned to Lender B, provided, however, that the guarantor retains all objections *vis-à-vis* Lender B that result from the guarantee agreement with Lender A upon a transfer of the loan and assignment of the guarantee.

In contrast, sureties are considered to be accessory claims according to Austrian law, which is consequently automatically transferred upon assignment of the secured loan. Also different to guarantees, the grantor of a surety is not only entitled to raise objections resulting from the surety upon transfer of the loan, but also to raise objections which stem from the relationship between the obligor and creditor under the loan agreement.

6 Withholding, Stamp and Other Taxes; Notarial and Other Costs

6.1 Are there any requirements to deduct or withhold tax from (a) interest payable on loans made to domestic or foreign lenders, or (b) the proceeds of a claim under a guarantee or the proceeds of enforcing security?

Interest payments and repayments of principal under loan transactions are generally not subject to withholding tax. Rather, such payments will have to be taken into account for purposes of the (corporate) income tax of the lender. However, if a payment of interest is effected to a non-Austrian lender then withholding tax in the amount of 35% may apply. There are numerous double taxation treaties concluded between Austria and other jurisdictions, which typically provide for such withholding tax to be considered as deductible and/or refundable. Due to the introduction of comprehensive cross-border information undertakings among authorities, the withholding tax legislation is not applicable from the end of 2016 onwards.

As regards proceeds of a claim under a guarantee or the proceeds of enforcing security, there is generally also no requirement imposed by Austrian law to deduct or withhold tax.

6.2 What tax incentives or other incentives are provided preferentially to foreign lenders? What taxes apply to foreign lenders with respect to their loans, mortgages or other security documents, either for the purposes of effectiveness or registration?

No Austrian taxes of any kind, e.g. stamp duty, issue, registration or similar taxes apply with regards to loans, mortgages or other security document for their effectiveness or registration and, similarly, no incentives whatsoever are provided in a preferential way to foreign lenders.

In case the foreign lender acts as an investor, the Austrian government in general would welcome such foreign direct investment. This is especially the case if those investments have the prospect to create new jobs in high-tech fields or promote capital-intense industries (cash grants may possibly be awarded). A particular focus is also given to investments that enhance research and development where specific tax incentives are available. A similar priority for the government is the environment; thus investments should not have any negative impact in this regard. Financial incentives may also be provided according to EU guidelines to promote investment in Austria, which are equally available to domestic and foreign investors, and range from tax incentives to preferential loans, guarantees and grants. Most of these incentives are available only if the planned investment meets specified criteria (e.g. implementation of new technology or reduction of unemployment).

6.3 Will any income of a foreign lender become taxable in your jurisdiction solely because of a loan to or guarantee and/or grant of security from a company in your jurisdiction?

Generally, no income of a foreign lender will become taxable in Austria, solely because of a loan, a guarantee or generally the grant of a company in Austria.

6.4 Will there be any other significant costs which would be incurred by foreign lenders in the grant of such loan/guarantee/security, such as notarial fees, etc.?

In Austria, no taxes or stamp duty will apply for the granting of loans (such loan fees were abolished in Austria in 2011) or (abstract) guarantees.

With regard to surety agreements and mortgages, which are not linked to loans, stamp duty at the rate of 1% of the secured interest will apply. Similarly, for assignments not linked to loans, stamp duty at the rate of 0.8% of the secured interest will apply.

Also, notary fees may be payable; e.g. with respect to the creation of mortgages, which must be notarised for registration and will depend on the transaction value. In addition, the registration of a mortgage in the land register will incur a registration fee of 1.1% of the mortgage.

6.5 Are there any adverse consequences to a company that is a borrower (such as under thin capitalisation principles) if some or all of the lenders are organised under the laws of a jurisdiction other than your own? Please disregard withholding tax concerns for purposes of this question.

In general, Austrian law does not provide for any such consequences.

7 Judicial Enforcement

7.1 Will the courts in your jurisdiction recognise a governing law in a contract that is the law of another jurisdiction (a "foreign governing law")? Will courts in your jurisdiction enforce a contract that has a foreign governing law?

Austrian law and conflicts of law rules generally permit the choice of a foreign law as the governing law of a contract, which is also the case if the respective contract is to be enforced in Austria. Regulation (EC) 593/2008 of 17 June 2008 on the Law applicable to Contractual Obligations (*Rom I Verordnung*) is applicable in Austria and must be observed in this context. Following such Regulation, Austrian courts will principally recognise the contractual choice of foreign law, subject to certain requirements (e.g. actual conflict of laws, or the contract relates to a civil and/or commercial matter), and to this extent, Austrian courts have jurisdiction for claims under such a contract. However, some restrictions apply regarding the granting and perfection of security rights, which, depending on the type of security, is in many cases governed by local Austrian law (e.g. for pledges over shares in Austrian companies, pledges over security assignments of Austrian law-governed receivables or for the creation of mortgages over real estate properties located in Austria). Hence it is common market practice that security rights over assets that are located in Austria, including those which are provided by Austrian domiciled transferors or pledgors, have Austrian law-governed security documentation.

Also, in cases where there is no actual conflict of law or where the contract is solely connected to EU Member States, the parties are not allowed to choose the law of a non-Member State. Additionally, no choice of law will be recognised by Austrian courts which would violate Austrian *ordre public*.

7.2 Will the courts in your jurisdiction recognise and enforce a judgment given against a company in New York courts or English courts (a "foreign judgment") without re-examination of the merits of the case?

As regards the enforcement of judgments or awards that were not rendered in Austria, there are generally the following options:

- Court judgments of EU Member States: The enforcement of judgments rendered in another EU Member State is governed by Regulation (EC) No 1215/2012 on the Jurisdiction and Recognition and Enforcement of Judgments in Civil and Commercial Matters (Brussels Ia Regulation). As in Austria the Brussels Ia Regulation is applicable, judgments from other EU Member States are recognised without any special procedure being required or any re-examination of the merits of the case (exceptions may apply, mainly with respect to Austrian *ordre public*).
- Court judgments of non-EU Member States: Beyond the applicability of the Brussels Ia Regulation, enforceability of foreign judgments is conditional and depends on whether there is a bilateral treaty between Austria and the home state of the other party. Austrian law requires reciprocity to be ensured under bilateral treaties/regulations and is assumed as a fundamental criterion for the enforcement of court judgments. Additionally, it is required that Austrian law would not have denied the foreign court, having rendered the relevant decision, if the defendant in the enforcement proceedings has been duly convoked in the original proceedings before the foreign court and if the relevant judgment is final in the sense that it may no longer be challenged before the courts and authorities of the foreign state. In case the counterparty had not had the opportunity to participate in the foreign court proceedings, the enforcement of such court judgment may be denied. The same applies in case the enforcement is aimed at an action which may not be enforced or that is not allowed under Austrian law, or if the Austrian *ordre public* would be violated.
- Arbitral awards: Austria is a contract state of the New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards. Arbitral proceedings and the enforcement of arbitral awards are common in Austria (see in this respect question 7.7 below).

7.3 Assuming a company is in payment default under a loan agreement or a guarantee agreement and has no legal defence to payment, approximately how long would it take for a foreign lender to (a) assuming the answer to question 7.1 is yes, file a suit against the company in a court in your jurisdiction, obtain a judgment, and enforce the judgment against the assets of the company, and (b) assuming the answer to question 7.2 is yes, enforce a foreign judgment in a court in your jurisdiction against the assets of the company?

As a general rule, the time it takes for an Austrian court to render a decision is based on several factors such as the complexity of the case, and the overall workload of the specific court. Usually (considering the above-mentioned factors) a judgment might be expected within one year with regard to question 7.3 (a). With regard to question 7.3 (b), the best case scenario for an enforcement of a judgment from an EU Member State may be expected within a few days and a couple of months in case of judgments from a non-EU Member State. Although those estimations are generally applicable, they vary from case to case and proceedings could require significantly more time. The timeframe may be stretched by remedies especially, and in particular most first instance judgments that may be appealed.

7.4 With respect to enforcing collateral security, are there any significant restrictions which may impact the timing and value of enforcement, such as (a) a requirement for a public auction, or (b) regulatory consents?

For the different types of securities and any other contractual arrangements, the enforcement of contractual security rights varies significantly. Security rights are usually enforced by statutory law applied by courts as a general principle, but deviations are possible in case of contractual arrangements between parties, which are permissible. Regarding the most relevant types of security, the following statutory rules and market practices apply:

Share pledges: Common market practice for shares in Limited Liability Companies and shares in Stock Corporations is to agree on out-of-court enforcements. This requires information to the pledgor as well as a valuation of the shares and subsequent disposal to the best bidder (usually the pledgor is also granted the right to participate in the bidding process).

Mortgages: A public auction is required for mortgages; the involvement of the court could lead to delays in the enforcement procedure.

Receivables: There is no specific enforcement procedure in place for receivables. The assignee (or the pledgee if granted a power to collect) is entitled to directly claim the payment from the debtor in case of default.

Guarantees/suretyships: There is no specific type of enforcement procedure for personal security such as guarantees or surety. Following the terms and conditions agreed in the security arrangement (e.g. priorities), the payment can be requested directly from the obligor (and enforced in court proceedings).

Movable property: The standard practice for movable property is to modify the enforcement procedure under statutory law to permit out-of-court enforcements. Adhering to a cooling-off period of one month and following public auctions, movable goods may be sold after notification of the pledgor.

7.5 Do restrictions apply to foreign lenders in the event of (a) filing suit against a company in your jurisdiction, or (b) foreclosure on collateral security?

Foreign lenders may be required to deposit court fees before proceedings commence. Lenders seated in EU Member States or states that are party to the Hague Convention on Civil Procedure of 1 March 1954 are usually not required to post collaterals for court costs.

7.6 Do the bankruptcy, reorganisation or similar laws in your jurisdiction provide for any kind of moratorium on enforcement of lender claims? If so, does the moratorium apply to the enforcement of collateral security?

Upon opening of the insolvency proceedings, the litigation and execution of claims of individual creditors is no longer permitted.

The enforcement of a claim then requires the filing of the claim as an insolvency claim (*Insolvenzforderungen*) with the insolvency court. The claim application period (*Anmeldungsfrist*) is published in the edict; however, the claim may also be filed after expiration of such period (additional court fees may apply). The insolvency administrator collects all claims in the claim table (*Anmeldeverzeichnis*), which is presented to the court. All claims that were duly filed are examined in the examination hearing (*Prüfungstagsatzung*). At such examination hearing, the insolvency administrator must declare whether the individual claims are acknowledged or declined. If the insolvency administrator acknowledges the claim and no other creditor contests such claim, the claim is considered to be acknowledged and the creditor will be take part *pro rata* in the distribution of the applicable insolvency quota. With regard to the enforcement of collateral security, please see questions 8.1 and 8.2 below.

7.7 Will the courts in your jurisdiction recognise and enforce an arbitral award given against the company without re-examination of the merits?

An arbitral award rendered by an arbitral tribunal having its seat in Austria generally constitutes an executory title under the Austrian Enforcement Act (*Exekutionsordnung*) and does not require a declaration of enforceability by a domestic court. Under these circumstances, it is considered sufficient to attach to the enforcement request a copy of such arbitral award with a confirmation of its final and binding nature and enforceability issued primarily by the chairman of the arbitral tribunal.

In respect to foreign arbitral awards, the New York Convention of 1958 is the prime basis for the recognition and enforcement. Sec. 611 Austrian Code on Civil Procedure (*Zivilprozessordnung*) provides possible legal grounds for re-examining/setting aside an arbitral award. However, in general, an Austrian Court will not re-examine the merits of an arbitral case, but only based on procedural errors (e.g. if the decided dispute is not covered by the arbitral agreement or if an arbitral agreement does not exist at all or if the matter in dispute must not be arbitrated). Certain exceptions apply; especially where an arbitral award conflicts with the fundamental values of the Austrian legal system (public policy).

8 Bankruptcy Proceedings

8.1 How does a bankruptcy proceeding in respect of a company affect the ability of a lender to enforce its rights as a secured party over the collateral security?

A secured creditor is barred from exercising enforcement rights regarding its security for a maximum period of six months after the opening of insolvency proceedings, if the exercise of such enforcement rights would endanger the operation of the debtor's business. However, this does not apply where the performance of such enforcement rights is necessary to prevent the secured creditor from being exposed to severe personal or economic danger, provided that it is not possible (and will not be possible) to provide full satisfaction to the creditor by execution into other assets of the debtor.

In insolvency proceedings, secured creditors are divided into categories. The claims of secured creditors are settled in a determined order. First, rights to separation of property (*Aussonderungsrechte*) are handled. Property of third parties caught in the insolvency proceedings must be returned to such third parties. After that, rights to separate satisfaction (*Absonderungsrechte*) are handled. Separate satisfaction is granted to creditors, whose claims are secured by a pledge or otherwise either by law or by agreement. The insolvency administrator may initiate auctions or forced administration of the insolvency estate's immovable assets, even if the asset is subject to a right of separate satisfaction.

8.2 Are there any preference periods, clawback rights or other preferential creditors' rights (e.g., tax debts, employees' claims) with respect to the security?

The Austrian Insolvency Act provides rules which allow for claims to contest transactions which possibly decrease the assets of the debtor prior to the opening of insolvency proceedings. In this respect, transactions that were entered into by the debtor and a third party, which discriminate other creditors, might be contested. The respective transaction must be contested by the appointed insolvency administrator.

Generally, for the contestation of transactions, the following is required: (i) an existing transaction; (ii) such transaction is entered into prior to the opening of the insolvency proceedings; (iii) the transaction somehow decreases the assets of the debtor; (iv) the transaction discriminates other creditors; and (v) the claim fulfils one of the specific contesting provisions of the Austrian Insolvency Act.

The Austrian Insolvency Act provides basically for the following specific contesting provisions:

(i) Intent to discriminate (*Benachteiligungsabsicht*):

This provision applies if transactions were concluded by the debtor for the purpose of discriminating creditors within the last 10 years prior to the initiation of the insolvency proceedings, where the contracting third party knew of such intent of the debtor. In case such third party did not know, but was required to have known of such intent, the period to contest the transaction is reduced to two years.

(ii) Squandering of assets (*Vermögensverschleuderung*):

A transaction is contestable if it is seen as squandering the company's assets. As a prerequisite, the contracting third party must have known or should have known that the transaction qualifies as squandering the debtor's assets and the transaction must have been entered into within the year prior to the opening of insolvency proceedings.

(iii) Dispositions free of charge (*Unentgeltliche Verfügungen*):

Transactions that were made free of charge and which were entered into within the two years prior to the opening of the insolvency proceedings are contestable.

(iv) Preferential treatment of creditors (*Begünstigung*):

This provision applies where a transaction discriminates one creditor *vis-à-vis* the others or is intended to prefer one creditor *vis-à-vis* the others after the debtor is materially insolvent or after the application for the opening of insolvency proceedings has been submitted or 60 days prior to either such event.

(v) Knowledge of illiquidity (*Kenntnis der Zahlungsunfähigkeit*):

A legal act based on the knowledge of illiquidity of the debtor might be contested after illiquidity has occurred, where the contracting third party knew or negligently was not aware of the debtor's illiquidity.

All provisions outlined above secure the debtor's assets prior to the opening of the proceedings. After opening of the insolvency proceedings and appointment of an insolvency administrator, the debtor is solely represented by the insolvency administrator. This does not apply where insolvency proceedings were opened as restructuring proceedings by self-administration of the debtor (*Sanierungsverfahren mit Eigenverwaltung*), which, under certain circumstances is subject to the consent of the insolvency administrator, the court or the creditor's committee. Otherwise, any transaction or disposition of a debtor's property can only be undertaken by the insolvency administrator (and under certain circumstances requires the consent of the court or the creditor's committee) after the opening of insolvency proceedings.

Estate claims (*Masseforderungen*) are generally preferred claims when the general estate (not the preferred estate) is distributed. Such estate claims comprise, e.g., claims for the general continuing of the business, including claims of employees, after opening of the insolvency proceedings.

8.3 Are there any entities that are excluded from bankruptcy proceedings and, if so, what is the applicable legislation?

The Austrian insolvency law is generally not limited to any types of entities. The insolvency ability is rather defined as part of the private law legal capacity. Therefore, generally, any natural person, as well as legal entities (private or public) and inheritances can be a debtor and can become insolvent.

With regard to banks, investment firms, investment services companies and insurance companies it should be noted that such entities may be subject to winding-up but not to bankruptcy procedures.

8.4 Are there any processes other than court proceedings that are available to a creditor to seize the assets of a company in an enforcement?

If no out-of-court seizure of assets is agreed (or even in case such agreement is made but not observed by the debtor), the process for seizure of assets of companies has to be made via court enforcement.

9 Jurisdiction and Waiver of Immunity

9.1 Is a party's submission to a foreign jurisdiction legally binding and enforceable under the laws of your jurisdiction?

The contractual choice of forum is generally permissible and legally binding as defined per Art. 25 of the Brussels Ia Regulation that is applicable for cross-border scenarios in case a party submits to a foreign jurisdiction, although specific form requirements may apply. It is also permissible if expressed and agreed that only one party can choose the forum. It needs to be considered that, for instances where the courts have exclusive jurisdiction pursuant to Art. 24 Brussels Ia Regulation, no choice of forum is permissible. This applies especially to proceedings in respect to rights *in rem*.

The Brussel Ia Regulation may not be applicable in case only one party has its domicile in an EU Member State and the other party also has its domicile in this state or in a non-EU Member State. The choice of jurisdiction clause would then be governed by domestic law. In any case, domestic rules also correspond to the Brussel I Regulation to a large extent.

9.2 Is a party's waiver of sovereign immunity legally binding and enforceable under the laws of your jurisdiction?

Provided it does not conflict with public international law or special immunities, such as diplomatic immunity, a waiver of sovereign immunity is usually legally binding.

10 Licensing

10.1 What are the licensing and other eligibility requirements in your jurisdiction for lenders to a company in your jurisdiction, if any? Are these licensing and eligibility requirements different for a "foreign" lender (i.e. a lender that is not located in your jurisdiction)? In connection with any such requirements, is a distinction made under the laws of your jurisdiction between a lender that is a bank *versus* a lender that is a non-bank? If there are such requirements in your jurisdiction, what are the consequences for a lender that has not satisfied such requirements but has nonetheless made a loan to a company in your jurisdiction? What are the licensing and other eligibility requirements in your jurisdiction for an agent under a syndicated facility for lenders to a company in your jurisdiction?

In order to provide loan financing on a commercial level to companies in Austria, there are three possible options:

Application for a banking licence. Obtaining a banking licence is a rather complicated procedure and requires in-depth preparation over a longer period of time. The legal requirements that have to be fulfilled are especially extensive, as is the creation of an appropriate business plan that has to be reviewed by the regulator.

A credit institute of another EU Member State may establish a branch (requires an existing banking licence, which would need to be notified to the Austrian regulator).

Utilising the EU freedom of service to render services in Austria, which is the most common approach for non-Austrian banks that want to become active in the lending business and wish to avoid establishing a permanent presence.

Non-banks may only engage in the lending business to the extent that such activity is exempted from the requirement to hold a banking licence (e.g. acquisition of loan portfolios by special securitisation purpose entities).

11 Other Matters

11.1 Are there any other material considerations which should be taken into account by lenders when participating in financings in your jurisdiction?

The main body of the Financial Market Anti-Money Laundering Act became applicable as of 1 January 2017. It implemented Directive 2015/849 (EU) of the European Parliament and the Council of 20 May 2015 on the prevention of the use of the financial system for the purposes of money laundering or terrorist financing. Among others, the Financial Market Anti-Money Laundering Act applies to credit and financial institutions under the Austrian Banking Act, including CRR institutions pursuant to Sec. 9 of the Austrian Banking Act, which has a significant impact on KYC checks. Those checks have to be conducted by the respective institutions in relation to their customers. Appropriate steps have to be taken by each institution to identify, access and mitigate risks of money laundering and terrorist financing. Also, risk factors that relate to their customers, geographic areas, products, services, transactions or any delivery channels have to be taken into account. This should prevent the use of the EU financial system for money laundering and terrorist financing.

Another aspect that may need to be observed is the Act on Equity Replacement (*Eigenkaptitalersatz-Gesetz*), according to which shareholders with a controlling interest of more than 25%, who make payments to a company or provide security for third-party loans to the benefit of a company during a crisis of such company, are treated subordinately compared to other lenders, if such company becomes insolvent.

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Chapter 30

Belgium

Werner Van Lembergen

Laga

Laurent Godts

1 Overview

1.1 What are the main trends/significant developments in the lending markets in your jurisdiction?

A new pledge law of 11 July 2013 came into force on 1 January 2018. This new law provides for a short-form and low-cost technique for taking security over (all) moveable assets of a business against very limited cost, thereby bringing about a robust legal framework for (asset-based) lending activities. One major change is that a pledge can now be rendered effective against third parties, not only by way of dispossession but also through recording the pledge in the new electronic pledge registry. Furthermore, the enforcement regime has been made more creditor-friendly and has been significantly simplified, making Belgium a more competitive and attractive jurisdiction for secured finance activities.

1.2 What are some significant lending transactions that have taken place in your jurisdiction in recent years?

We do not comment on specific transactions. Financing conditions have generally been borrower-friendly because of the low interest-rate environment and the increasing activity of alternative lenders on the market. This resulted in the predominance of covenant-lite facilities, with little or no security interests. We also noted an increasing presence of international interest in lending into Belgian companies, resulting in the extension of existing syndicates.

2 Guarantees

2.1 Can a company guarantee borrowings of one or more other members of its corporate group (see below for questions relating to fraudulent transfer/financial assistance)?

A company can guarantee borrowings of other members of its group as long as the guarantee is in the corporate interest/benefit of the guarantor, which is a matter of factual appreciation to be made by the guarantor's competent corporate body.

To pass the factual test of corporate interest/benefit, the following elements are to be taken into account: (i) the direct benefit the guarantor derives from the transaction; (ii) the indirect benefits; and (iii) the balance between the risk relating to the guarantee, its financial capacity and the benefit it derives from granting the guarantee.

Importantly, the concept of "group benefit" is not, as such, recognised under Belgian law, whereby the guarantor will always need to derive a direct benefit from the transaction, which can be harder to demonstrate in case of up-stream and cross-stream guarantees.

2.2 Are there enforceability or other concerns (such as director liability) if only a disproportionately small (or no) benefit to the guaranteeing/securing company can be shown?

The granting of a guarantee without sufficient corporate benefit could lead to civil and criminal liabilities for the director of the Belgian guarantor and to the unenforceability of the guarantee.

2.3 Is lack of corporate power an issue?

Transactions or actions entered into or executed by a Belgian company have to comply with the company's articles of association and, in particular, the corporate purpose clause.

The company would remain liable for transactions or actions entered into without corporate power, save where the third party was aware of such breach. This awareness has to be proven *in concreto*, and depends on the third party's level of professionalism. It would therefore be more complicated for a banker to argue that he was not aware of such breach.

2.4 Are any governmental or other consents or filings, or other formalities (such as shareholder approval), required?

As a general principle, no. However, for certain forms of legal entities (including public companies (*société anonyme/naamloze vennootschap*)), shareholders' approval is required for changes of control restrictions. The articles of association may also provide for specific approvals or consents.

2.5 Are net worth, solvency or similar limitations imposed on the amount of a guarantee?

No; however, the guarantor's financial capacity should be evaluated when assessing its corporate benefit to enter into the guarantee.

It is also market practice in Belgium, in case of up-stream or cross-stream guarantees, to limit the guaranteed amount to a percentage of the guarantor's net assets in order to pass the corporate benefit test.

2.6 Are there any exchange control or similar obstacles to enforcement of a guarantee?

There are no such exchange controls.

3 Collateral Security

3.1 What types of collateral are available to secure lending obligations?

Any element of the debtor's assets (moveable assets (tangible or intangible), real estate, and financial collateral) may be given as collateral to secure its lending obligations. Future assets may also be given as collateral under certain circumstances.

3.2 Is it possible to give asset security by means of a general security agreement or is an agreement required in relation to each type of asset? Briefly, what is the procedure?

There is no general security agreement under Belgian law. It is, however, possible to grant a pledge over the whole business' assets by way of a floating charge pledge.

3.3 Can collateral security be taken over real property (land), plant, machinery and equipment? Briefly, what is the procedure?

A security can be vested over real estate property by means of a mortgage. Contrary to any other security, a mortgage can only be created by means of a notarial deed and needs to be registered at the competent mortgage registry.

Assets such as plant, machinery and equipment can be pledged through a "regular" pledge (private deed). Effectiveness against third parties requires its notification in the National Pledge Registry.

3.4 Can collateral security be taken over receivables? Briefly, what is the procedure? Are debtors required to be notified of the security?

Yes, by means of a pledge. Such a pledge is valid and effective against third parties by means of the mere conclusion of the agreement (private deed). Effectiveness against the underlying debtors requires their notification.

3.5 Can collateral security be taken over cash deposited in bank accounts? Briefly, what is the procedure?

Yes, since cash deposits are considered as receivables held against the account bank, the same procedure as explained in question 3.4 applies.

3.6 Can collateral security be taken over shares in companies incorporated in your jurisdiction? Are the shares in certificated form? Can such security validly be granted under a New York or English law governed document? Briefly, what is the procedure?

Subject to any restrictive provisions in the articles of association, a security interest can be created over the shares in a Belgian company.

The effectiveness of a pledge on registered shares is perfected by recording such pledge in the share register of the company. The effectiveness of a pledge on dematerialised shares requires the registration of the shares in a special financial account.

Parties may opt for foreign law as the law governing the pledge agreement, but the proprietary aspects of the security will be governed by Belgian law if the company is located in Belgium, or if the special account in which the dematerialised shares are registered is opened in Belgium.

3.7 Can security be taken over inventory? Briefly, what is the procedure?

Yes. The former maximum limit of 50% of inventory available for pledge has been lifted. Effectiveness against third parties requires its registration in the National Pledge Registry.

3.8 Can a company grant a security interest in order to secure its obligations (i) as a borrower under a credit facility, and (ii) as a guarantor of the obligations of other borrowers and/or guarantors of obligations under a credit facility (see below for questions relating to the giving of guarantees and financial assistance)?

A Belgian company can grant a security interest in both situations, keeping in mind the limitations of the corporate benefit as mentioned in questions 2.2 and 2.3 and financial assistance as mentioned in question 4.1.

3.9 What are the notarisation, registration, stamp duty and other fees (whether related to property value or otherwise) in relation to security over different types of assets?

The registration of a mortgage triggers a cost of approximately 1.40–1.50% of the secured amount to cover notary fees, registration duties and additional costs.

The registration of a pledge on moveable assets in the National Pledge Registry triggers the payment of a fee capped at 500 EUR. The 0.5% capital duty due in relation to taking a business pledge no longer applies.

3.10 Do the filing, notification or registration requirements in relation to security over different types of assets involve a significant amount of time or expense?

Except for mortgages which require notary involvement, vesting security rights in Belgium is cost-efficient and easily done.

3.11 Are any regulatory or similar consents required with respect to the creation of security?

No such regulatory consents are required.

3.12 If the borrowings to be secured are under a revolving credit facility, are there any special priority or other concerns?

There are no special priority concerns.

3.13 Are there particular documentary or execution requirements (notarisation, execution under power of attorney, counterparts, deeds)?

Besides a mortgage, which needs to be documented by means of a notarial deed, there are no particular documentary or execution requirements for the other types of security vested under Belgian law.

4 Financial Assistance

4.1 Are there prohibitions or restrictions on the ability of a company to guarantee and/or give security to support borrowings incurred to finance or refinance the direct or indirect acquisition of: (a) shares of the company; (b) shares of any company which directly or indirectly owns shares in the company; or (c) shares in a sister subsidiary?

(a) Shares of the company

In general, a Belgian company may only provide security with the view to the acquisition of its shares by a third party under very strict conditions, which render financial assistance difficult in practice.

(b) Shares of any company which directly or indirectly owns shares in the company

This form of financial assistance is generally allowed as long as there is no fraudulent intent.

(c) Shares in a sister subsidiary

There are no prohibitions or restrictions in this regard.

5 Syndicated Lending/Agency/Trustee/Transfers

5.1 Will your jurisdiction recognise the role of an agent or trustee and allow the agent or trustee (rather than each lender acting separately) to enforce the loan documentation and collateral security and to apply the proceeds from the collateral to the claims of all the lenders?

For the tasks as described above, agency is recognised under the new pledge law. Although not recognised yet, there are initiatives to implement a concept of trust in Belgian law.

5.2 If an agent or trustee is not recognised in your jurisdiction, is an alternative mechanism available to achieve the effect referred to above which would allow one party to enforce claims on behalf of all the lenders so that individual lenders do not need to enforce their security separately?

Prior to the new pledge law (which recognised security agency arrangements), the practice was to organise parallel debt mechanisms (by which the agent/trustee was made a joint creditor of all amounts owing to the lender). Such mechanisms remain operative.

5.3 Assume a loan is made to a company organised under the laws of your jurisdiction and guaranteed by a guarantor organised under the laws of your jurisdiction. If such loan is transferred by Lender A to Lender B, are there any special requirements necessary to make the loan and guarantee enforceable by Lender B?

If the loans are transferred by way of assignment, all accessory rights and securities will follow the principal (the loans). However, underlying debtors will have to be notified for the transfer to be made effective.

On the other hand, when the loans are transferred by way of novation, due to the fact that a new debt is created, all securities or other accessory rights attached to the original debt will cease to exist unless expressly stated otherwise.

6 Withholding, Stamp and Other Taxes; Notarial and Other Costs

6.1 Are there any requirements to deduct or withhold tax from (a) interest payable on loans made to domestic or foreign lenders, or (b) the proceeds of a claim under a guarantee or the proceeds of enforcing security?

(a) In principle, a 30% withholding tax applies on interest payments (both to domestic, as well as to foreign lenders). However, Belgian legislation and double-tax treaties provides for numerous exemptions or reductions from withholding taxes. Note that formal conditions may have to be fulfilled in order for some of the exemptions to be applicable.

(b) In principle, no.

6.2 What tax incentives or other incentives are provided preferentially to foreign lenders? What taxes apply to foreign lenders with respect to their loans, mortgages or other security documents, either for the purposes of effectiveness or registration?

There are no specific incentives for foreign lenders, although an exemption from withholding tax might be applicable (see question 6.1).

The same taxes apply to Belgian and foreign lenders (see question 3.9).

6.3 Will any income of a foreign lender become taxable in your jurisdiction solely because of a loan to or guarantee and/or grant of security from a company in your jurisdiction?

The income of a foreign lender does not become taxable in this case.

6.4 Will there be any other significant costs which would be incurred by foreign lenders in the grant of such loan/guarantee/security, such as notarial fees, etc.?

There are no other significant costs.

6.5 Are there any adverse consequences to a company that is a borrower (such as under thin capitalisation principles) if some or all of the lenders are organised under the laws of a jurisdiction other than your own? Please disregard withholding tax concerns for purposes of this question.

In principle, no. However, thin capitalisation rules will be applicable to interest payments if the loan is granted by a related party or the lender is located in a low-tax jurisdiction. Note that, in the future, Belgian thin capitalisation rules will be replaced by the EU rule on interest deduction limitation.

Furthermore, if the lender is located in a "blacklisted" jurisdiction or in a low-tax jurisdiction, the borrower may have to fulfil certain reporting duties and/or may have to prove that the payments were made in the framework of actual and real activities in order for the interest payments to be deductible.

Transfer pricing rules apply to borrowings from foreign affiliated lenders, implying that the borrowings should be in accordance with the "arm's length principle" (as interpreted by the OECD TP Guidelines).

7 Judicial Enforcement

7.1 Will the courts in your jurisdiction recognise a governing law in a contract that is the law of another jurisdiction (a "foreign governing law")? Will courts in your jurisdiction enforce a contract that has a foreign governing law?

Belgian jurisdiction will, in principle, recognise and enforce such foreign governing law. However, mandatory provisions (regarding the safeguarding of public interests) of other jurisdictions, or public policy provisions of the competent jurisdiction, may override the provisions of the foreign governing law and apply directly to the contract.

7.2 Will the courts in your jurisdiction recognise and enforce a judgment given against a company in New York courts or English courts (a "foreign judgment") without re-examination of the merits of the case?

Belgian jurisdiction will, in principle, recognise and enforce such foreign judgment without re-examination of the merits of the case. Nonetheless, certain exceptions to this principle may apply. For instance, the Belgian court will refuse to recognise and enforce a judgment if such judgment is manifestly contrary to the public policy of Belgium or violates the rights of defence.

7.3 Assuming a company is in payment default under a loan agreement or a guarantee agreement and has no legal defence to payment, approximately how long would it take for a foreign lender to (a) assuming the answer to question 7.1 is yes, file a suit against the company in a court in your jurisdiction, obtain a judgment, and enforce the judgment against the assets of the company, and (b) assuming the answer to question 7.2 is yes, enforce a foreign judgment in a court in your jurisdiction against the assets of the company?

In case one or both of the parties is not registered in a European database of enterprises, regular judicial procedures apply. For undisputed debts, it is possible to enter into summary proceedings. This procedure will provide an enforceable judgment in approximately three months. Nevertheless, if the defendant disputes the claim, ordinary proceedings will apply, meaning that obtaining an enforceable judgment will take at least one year. Judgments after trial are, in principle, executable with immediate effect, regardless of any appeal. Note that non-judicial procedure options may also apply, as well as the European Payment order, which may significantly accelerate the obtainment of an enforceable payment order.

Generally, in order to enforce a foreign judgment in Belgium, an exequatur is required. Normally this can be obtained within 15–30 days, assuming no party files any opposition.

When the judgment is enforceable, the lender can attach the assets of the borrower. The timing for attaching assets depends on the goods to be attached. For real estate, more documents and formalities need to be fulfilled (e.g. authorisation by the attachment judge) which may take between approximately one and six months.

In certain situations (mostly pending insolvency), a conservatory attachment of assets is possible before a final judgment or exequatur is rendered. Timing varies as well, depending on the assets and formalities to be fulfilled. In principle, it takes between five days and three months.

7.4 With respect to enforcing collateral security, are there any significant restrictions which may impact the timing and value of enforcement, such as (a) a requirement for a public auction, or (b) regulatory consents?

Enforcing a collateral security requires the permission of the competent attachment judge. Generally, a bailiff or public notary will be appointed to sell the assets covered by the collateral security during a public auction, although a private sale is possible under certain circumstances.

However, regarding financial collateral securities, it is, in certain cases, possible for the security holder to enforce the collateral security in a flexible manner without the prior authorisation of the Belgian courts (Law on Financial Collateral).

In general, no regulatory consents are required.

7.5 Do restrictions apply to foreign lenders in the event of (a) filing suit against a company in your jurisdiction, or (b) foreclosure on collateral security?

Upon the request of the defendant, the foreign (non-EEA) lender/security taker might, in certain circumstances, be obligated to provide a guarantee in order to secure the costs and damages arising from the procedure.

7.6 Do the bankruptcy, reorganisation or similar laws in your jurisdiction provide for any kind of moratorium on enforcement of lender claims? If so, does the moratorium apply to the enforcement of collateral security?

When reorganisation or bankruptcy proceedings are initiated, there is an automatic stay of enforcement. However, both proceedings lead to different results regarding the attachments, it being the case that, during reorganisation proceedings, attachments in conservation will continue to exist whilst the opening of bankruptcy proceedings will result in the automatic annulment of all attachments.

It is important to note that, as from 1 May 2018, new legislation will apply on insolvency proceedings. The main principles remain unchanged, although advanced attachment proceedings may continue under certain circumstances.

7.7 Will the courts in your jurisdiction recognise and enforce an arbitral award given against the company without re-examination of the merits?

Pursuant to the New York Convention on Recognition and Enforcement of Foreign Arbitral Awards, Belgian courts will not re-examine the merits of the case. Nonetheless, there are (i) several grounds on which a Belgian court can decide to refuse to recognise and/or enforce an arbitral award (e.g. conflict with the Belgian public policy), and (ii) certain requirements that need to be met (such as a proper composition of the arbitration authority).

8 Bankruptcy Proceedings

8.1 How does a bankruptcy proceeding in respect of a company affect the ability of a lender to enforce its rights as a secured party over the collateral security?

During bankruptcy proceedings, all attachments will automatically be revoked (*cf.* question 7.6).

Under the new law regarding insolvency proceedings, in effect as of 1 May 2018, advanced attachment proceedings can continue in certain circumstances.

8.2 Are there any preference periods, clawback rights or other preferential creditors' rights (e.g., tax debts, employees' claims) with respect to the security?

The court will determine the "suspect period": a period during which the granting of securities is identified as suspicious. The starting point of this period can be set a maximum of six months prior to the judgment opening the bankruptcy procedure, except in case of fraud, where no time limit applies.

Security interests granted during such suspect period may be declared void if it is proven that the security caused disadvantage to the joint creditors or that the secured party was aware of the insolvency of the company.

Secured claims take priority over *general* statutory liens (applicable to the whole bankruptcy estate). However, secured claims do not necessarily take priority over *specific* statutory liens (applicable to specific assets).

8.3 Are there any entities that are excluded from bankruptcy proceedings and, if so, what is the applicable legislation?

To date, non-merchants and public bodies are excluded from bankruptcy proceedings. As from 1 May 2018, insolvency proceedings will be applicable to any natural person or legal entity which pursues a commercial objective on a long-term basis. Nevertheless, public bodies will remain excluded from bankruptcy proceedings.

8.4 Are there any processes other than court proceedings that are available to a creditor to seize the assets of a company in an enforcement?

It is possible under conditions for the beneficiary of a pledge over financial collateral to directly seize the assets of a company without prior court intervention.

9 Jurisdiction and Waiver of Immunity

9.1 Is a party's submission to a foreign jurisdiction legally binding and enforceable under the laws of your jurisdiction?

A party is, in principle, allowed to choose any foreign jurisdiction to submit its dispute (EU or not). However, certain matters belong to the exclusive jurisdiction of the Belgian courts. Belgian courts will also be competent if the case is closely tied to Belgium and bringing proceedings before a court of a chosen foreign jurisdiction would seem impossible or unreasonable.

9.2 Is a party's waiver of sovereign immunity legally binding and enforceable under the laws of your jurisdiction?

A party's waiver of sovereign immunity from jurisdiction is, in principle, enforceable under Belgian law; however, this does not necessarily result in a waiver of sovereign immunity from execution.

10 Licensing

10.1 What are the licensing and other eligibility requirements in your jurisdiction for lenders to a company in your jurisdiction, if any? Are these licensing and eligibility requirements different for a "foreign" lender (i.e. a lender that is not located in your jurisdiction)? In connection with any such requirements, is a distinction made under the laws of your jurisdiction between a lender that is a bank *versus* a lender that is a non-bank? If there are such requirements in your jurisdiction, what are the consequences for a lender that has not satisfied such requirements but has nonetheless made a loan to a company in your jurisdiction? What are the licensing and other eligibility requirements in your jurisdiction for an agent under a syndicated facility for lenders to a company in your jurisdiction?

Under the Belgian Banking Act, the requirement of a banking licence is only triggered when combining the activity of deposit-taking with lending activities. As a consequence, when only exercising a lending activity, there is no need for any licence.

11 Other Matters

11.1 Are there any other material considerations which should be taken into account by lenders when participating in financings in your jurisdiction?

There are no other material considerations in the context of a typical borrowing-base financing.

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Laga

A top legal practice in Belgium, Laga is a full-service business law firm. Our lawyers specialise in a wide range of disciplines, meaning that Laga can assist business people with a full spectrum of legal matters. By building and maintaining strong long-term business relationships, we help our clients manage their legal risks on a continual basis. Our aim is to provide efficient, practical and innovative legal solutions tailored for the client's specific needs. In that respect, our professionals continuously invest in building knowledge and experience, dealing with a variety of industry sectors.

Besides having several offices within Belgium where appropriate, to ensure a seamless and comprehensive high-quality service, the Laga team works closely on a good friends basis with select local law firms that are prominent in their respective jurisdictions, as well as with financial, assurance and advisory, tax and consulting specialists.

Laga's Banking & Finance department consists of close to fifteen qualified lawyers, with a practice focus on all aspects of banking, project and structured finance, syndicated lending, debt capital markets and debt restructurings and financial law. Our practice is recognised as one of the leading practices in Belgium by *Chambers & Partners* (Global and Europe editions), *The Legal 500* and *IFLR*. Our team acts for the different stakeholders in financing transactions, involving credit institutions, financial institutions, corporates, rating agencies and public (federal and regional) entities.

Bermuda

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1 Overview

1.1 What are the main trends/significant developments in the lending markets in your jurisdiction?

There were no changes to Bermuda's Companies Act 1981 (**Companies Act**) during 2017 affecting the rights of secured parties or Bermuda's reputation as a leading creditor-friendly jurisdiction.

The Bribery Act 2016 came into force in September 2017, providing an overhaul of Bermuda's anti-bribery laws and bringing them in line with those of the UK. The Mortgaging of Aircraft and Aircraft Engines Act 1999 was amended to ensure that aircraft owned by entities in certain jurisdictions outside of Bermuda can be registered in Bermuda together with any mortgage over that aircraft and its engine. This amendment has eliminated the requirement to involve Bermuda companies in aircraft financing structures where the aircraft is registered in Bermuda.

1.2 What are some significant lending transactions that have taken place in your jurisdiction in recent years?

Bermuda's hosting of the 35th America's Cup in 2017 saw an extraordinary increase in the number of lending transactions in tourism related industries, particularly in the areas of acquisition finance and hotel and commercial developments. Bermuda companies continue to be frequently utilised in financing and holding structures, most notably in the mining, oil and gas and shipping sectors.

2 Guarantees

2.1 Can a company guarantee borrowings of one or more other members of its corporate group (see below for questions relating to fraudulent transfer/financial assistance)?

A company may guarantee borrowings of members of its corporate group provided the company has capacity to provide such guarantees and there is a sufficient corporate benefit to the company, which may be in the form of a benefit to the company group.

2.2 Are there enforceability or other concerns (such as director liability) if only a disproportionately small (or no) benefit to the guaranteeing/securing company can be shown?

In these circumstances, there is a risk that the directors are not adequately discharging either their fiduciary duties or statutory directors' duties to act honesty and in good faith with a view to the best interests of the company.

In considering whether to approve such a guarantee, the directors would need to satisfy themselves that a sufficient direct, indirect or group commercial benefit exists. If the company is insolvent, the directors may be liable for wrongful trading and there is a risk that the guarantee may be void on the grounds that it amounted to a fraudulent preference.

2.3 Is lack of corporate power an issue?

The constitutional documents of the guarantor company should be reviewed to ensure the company has capacity to give the contemplated guarantee. A company's memorandum of association may not set out an express power to give guarantees; however, in most cases, the company's objects would typically be sufficiently broad to permit the entry into guarantees that are ancillary to the business of the company.

2.4 Are any governmental or other consents or filings, or other formalities (such as shareholder approval), required?

In most cases, no such consents or filings are required unless the company undertakes regulated activity, such as insurance, in which case consent may be required from the Bermuda Monetary Authority (**BMA**).

Guarantees of loans to directors (and other persons related to directors) are generally prohibited without the consent of members holding 90% of the company's voting rights and if such member consent is not obtained, the directors authorizing the entering into of the guarantee shall be jointly and severally liable to indemnify the company against any loss arising. Member consent to directors' loans or guarantees can be obtained, to mitigate concerns of corporate benefit and breach of fiduciary obligation.

Guarantees are often executed as a deed to avoid disputes concerning due consideration.

2.5 Are net worth, solvency or similar limitations imposed on the amount of a guarantee?

No statutory limitations are imposed; however, directors should consider the solvency of the company to ensure that any guarantee is in the best interests of the company.

2.6 Are there any exchange control or similar obstacles to enforcement of a guarantee?

There are no exchange control restrictions that would act as an obstacle to the enforcement of a guarantee against a company, however, non-Bermuda exchange control and sanctions should be reviewed.

3 Collateral Security

3.1 What types of collateral are available to secure lending obligations?

Both tangible and intangible assets of a company are available to secure lending obligations.

3.2 Is it possible to give asset security by means of a general security agreement or is an agreement required in relation to each type of asset? Briefly, what is the procedure?

In lending transactions, companies typically grant general security agreements, such as debentures, to secure underlying obligations. Where shares of a Bermuda company form part of the asset security, it is usual for a Bermuda law governed share charge to be used. Specific regimes apply for security over Bermuda land and ships, and aircraft and aircraft engines registered in Bermuda.

3.3 Can collateral security be taken over real property (land), plant, machinery and equipment? Briefly, what is the procedure?

Security over real property in Bermuda is typically granted by way of legal or equitable mortgage and by way of fixed charge or chattel mortgage over plant, machinery and equipment.

Different rules apply depending on whether the company is a local or an exempted company. Exempted companies may hold land in Bermuda but only to the extent that the land (a) is designated commercial real estate and used for the company's business purpose or (b) is residential real estate that will be used to accommodate employees of the company and is generally available to be acquired by non-Bermudians. Land holding permissions are required for both freehold and long leasehold acquisitions and the applicant will need to show both a *bona fide* business need and a benefit to Bermuda (most often the creation of local jobs). Local companies may hold land in Bermuda if specifically permitted under the company's constitutional documents, the Minister of Finance has provided its consent and the company requires the land to carry out its business.

Local and exempted companies may enter into land leases for business purposes for up to 50 years. They may also lease residential premises in the company's name for up to 21 years with Ministerial permission.

A legal mortgage transfers title to the land to the mortgagee subject to the requirement that the title be transferred to the mortgagor upon satisfaction of the underlying secured obligations. Legal mortgages must be executed as a deed and will attract stamp duty. The deed and accompanying documents must be filed with the Land Title Registry Office and upon the registration of the mortgage in the Book of Mortgages, the deed will be returned and held by the mortgagee. Priority is based on the date the mortgage was filed for registration. Under an equitable mortgage, the beneficial title in the land is transferred to the secured party, however, legal title remains with the chargor. Equitable mortgages need not be executed as a deed and are typically only used where the requirements for a legal mortgage cannot be met.

There are special rules that apply if an overseas or exempted company wishes to hold a mortgage over Bermuda land, including obtaining the prior consent of the Ministers of Finance and Immigration. If the mortgage is to be enforced, any land obtained by an overseas or exempted company must be sold within five years to either a person/entity having Bermudian status or another licensed party.

In relation to a fixed charge over plant, machinery and equipment, registration is not necessary in Bermuda to perfect the security interest created. However, to ensure the priority in Bermuda of the charge, the charge must be registered at the Registrar of Companies (**ROC**) and upon registration, to the extent that Bermuda law governs the priority of a charge, such charge will have priority in Bermuda over any unregistered charges and over any subsequently registered charge.

3.4 Can collateral security be taken over receivables? Briefly, what is the procedure? Are debtors required to be notified of the security?

Collateral security can be granted over receivables by way of assignment or fixed or floating charge. Assignments can be legal or equitable. Legal assignments must be in writing, signed by the assignor and unconditional and written notice must be provided to the debtor. An equitable assignment will result if any of these requirements are not satisfied.

Under a legal assignment, the assignee can sue in its own name and the debtor can only discharge its obligations as instructed by the assignee.

Although not legally required to perfect the security interest, assignments and charges over receivables should be registered with the ROC to ensure priority.

3.5 Can collateral security be taken over cash deposited in bank accounts? Briefly, what is the procedure?

Companies may grant security over cash in its bank accounts which is typically effected by way of a fixed or floating charge. The amount of control that the chargee will have over the account will determine whether a charge is fixed or floating.

Serving notice on a bank will ensure a chargee's priority in relation to subsequent assignees provided the chargee has no knowledge of an earlier assignment. Service of notice on a bank will perfect the security granted by the chargor regardless if the bank provides an acknowledgment.

Bermuda banks typically require chargees and chargors to enter into a deposit account control agreement to regulate the administration of the account, including restricting withdrawals unless permitted by the chargee and the banks' agreement not to exercise set-off rights.

Although not legally required to perfect the security interest, charges over accounts should be registered with the ROC to ensure priority.

3.6 Can collateral security be taken over shares in companies incorporated in your jurisdiction? Are the shares in certificated form? Can such security validly be granted under a New York or English law governed document? Briefly, what is the procedure?

Security over shares of Bermuda companies is typically granted by way of a share charge. Legal mortgages are uncommon, although share charges usually provide the chargee with the right to create a legal mortgage upon the occurrence of certain events. It is recommended that chargors also be required to deliver certain ancillary documents to strengthen their security, including executed but undated share transfer forms, irrevocable voting proxies and undertakings.

Bermuda companies cannot issue bearer shares. Share certificates do not need to be issued unless required under the company's bye-laws or requested by a shareholder; if issued, share certificates are generally a deliverable under a charge over shares of a Bermuda company.

For efficacy of enforcement, it is recommended that share charges be governed by Bermuda law. However, it is possible for New York or English law to govern the charge if required by the underlying transaction documents.

Bermuda exchange control regulations generally require the consent of the BMA prior to any disposition of shares of a Bermuda company, which would include the creation of a security interest. The BMA has granted a blanket consent where the chargee is a licensed bank or lending institution in certain appointed jurisdictions and the BMA is provided with written notification.

Although not legally required to perfect the security interest, share charges should be registered with the ROC to ensure priority.

3.7 Can security be taken over inventory? Briefly, what is the procedure?

Security is typically taken over inventory by means of a floating charge, due to the fluctuating nature of inventory.

Although not legally required to perfect the security interest, a floating charge should be registered with the ROC to ensure priority.

3.8 Can a company grant a security interest in order to secure its obligations (i) as a borrower under a credit facility, and (ii) as a guarantor of the obligations of other borrowers and/or guarantors of obligations under a credit facility (see below for questions relating to the giving of guarantees and financial assistance)?

There should be no issues in any of these situations, provided there is a demonstrable corporate benefit to the company (which may be in the form of a benefit to the company group, if applicable) and the company is solvent.

3.9 What are the notarisation, registration, stamp duty and other fees (whether related to property value or otherwise) in relation to security over different types of assets?

Stamp duty rarely applies to documents that are executed by Bermuda companies engaged in international business. However, legal mortgages on Bermuda real estate do attract stamp duty at different rates depending on the amount of the sum secured.

With limited exceptions, stamp duty is payable on most documents executed by local Bermuda companies.

A fee of between $180 and $630 will be payable for registering a charge at the ROC, depending on the value secured. There is also a $90 fee for registering a satisfaction of a charge at the ROC.

3.10 Do the filing, notification or registration requirements in relation to security over different types of assets involve a significant amount of time or expense?

Security arrangements can be registered in Bermuda on a same-day basis. Certain prescribed forms need to be filed, however, Bermuda counsel can attend to these requirements.

If a chargee is taking security over shares in a Bermuda company and the chargee is not a licensed bank or lending institution and is not known to the BMA, the BMA may require a few working days to provide its consent to the granting of the charge for exchange control purposes.

3.11 Are any regulatory or similar consents required with respect to the creation of security?

Generally, other than for BMA consent that may be required for exchange control purposes, no regulatory or similar consent is typically required for companies to grant security over their assets.

3.12 If the borrowings to be secured are under a revolving credit facility, are there any special priority or other concerns?

Generally, no.

3.13 Are there particular documentary or execution requirements (notarisation, execution under power of attorney, counterparts, deeds)?

Secured parties will want to receive copies of authorisation board resolutions to ensure corporate formalities have been followed and issues regarding corporate benefit have been considered.

Special rules apply for deeds, including that a deed be in writing, clear that it is intended to be executed as a deed and validly executed as a deed in accordance with the company's bye-laws.

In most cases, powers of attorney must be executed as a deed.

4 Financial Assistance

4.1 Are there prohibitions or restrictions on the ability of a company to guarantee and/or give security to support borrowings incurred to finance or refinance the direct or indirect acquisition of: (a) shares of the company; (b) shares of any company which directly or indirectly owns shares in the company; or (c) shares in a sister subsidiary?

There is no general prohibition or restriction on financial assistance, but loans to directors or security in favour of director loans (or loans to persons connected to a director) are restricted.

(a) Shares of the company

Without the consent of the members of the company holding shares with 90% of the voting rights, it is unlawful for a company to make a loan, enter into a guarantee or provide security in connection with a loan to a director (or to certain persons connected with a director) except in certain limited circumstances.

(b) Shares of any company which directly or indirectly owns shares in the company

See question 4.1 above.

(c) Shares in a sister subsidiary

See question 4.1 above.

5 Syndicated Lending/Agency/Trustee/Transfers

5.1 Will your jurisdiction recognise the role of an agent or trustee and allow the agent or trustee (rather than each lender acting separately) to enforce the loan documentation and collateral security and to apply the proceeds from the collateral to the claims of all the lenders?

A Bermuda court would recognise the role of a security agent or trustee and allow the agent or trustee to enforce the loan documentation and collateral security and to apply the proceeds from the collateral to the claims of all the lenders pursuant to the terms of the intercreditor, loan and security documentation.

5.2 If an agent or trustee is not recognised in your jurisdiction, is an alternative mechanism available to achieve the effect referred to above which would allow one party to enforce claims on behalf of all the lenders so that individual lenders do not need to enforce their security separately?

Agency and trustee relationships are well established in Bermuda.

5.3 Assume a loan is made to a company organised under the laws of your jurisdiction and guaranteed by a guarantor organised under the laws of your jurisdiction. If such loan is transferred by Lender A to Lender B, are there any special requirements necessary to make the loan and guarantee enforceable by Lender B?

There are no special requirements to make the loan and guarantee enforceable by Lender B so long as the transfer or novation procedures are complied with pursuant to the terms of the loan documentation.

6 Withholding, Stamp and Other Taxes; Notarial and Other Costs

6.1 Are there any requirements to deduct or withhold tax from (a) interest payable on loans made to domestic or foreign lenders, or (b) the proceeds of a claim under a guarantee or the proceeds of enforcing security?

Bermuda has no income, corporate, withholding or capital gains tax and no estate duty or inheritance tax. No such taxes or duty are payable to any authority in Bermuda whether on loan interest or proceeds of claim.

6.2 What tax incentives or other incentives are provided preferentially to foreign lenders? What taxes apply to foreign lenders with respect to their loans, mortgages or other security documents, either for the purposes of effectiveness or registration?

There are no tax incentives. Foreign lenders will not be deemed to be resident, domiciled or carrying on business in Bermuda by reason only of the execution, performance and/or enforcement of the loan and security documents.

6.3 Will any income of a foreign lender become taxable in your jurisdiction solely because of a loan to or guarantee and/or grant of security from a company in your jurisdiction?

No income of a foreign lender will become taxable in Bermuda solely because of a loan to or guarantee and/or grant of security from a Bermuda company.

6.4 Will there be any other significant costs which would be incurred by foreign lenders in the grant of such loan/guarantee/security, such as notarial fees, etc.?

Generally, no. Neither notarisation nor registration is necessary to perfect a security interest, but registration with the ROC (for which fees are payable, see question 3.9 above) confers priority ranking over subsequent registered security interests.

6.5 Are there any adverse consequences to a company that is a borrower (such as under thin capitalisation principles) if some or all of the lenders are organised under the laws of a jurisdiction other than your own? Please disregard withholding tax concerns for purposes of this question.

Generally, no.

7 Judicial Enforcement

7.1 Will the courts in your jurisdiction recognise a governing law in a contract that is the law of another jurisdiction (a "foreign governing law")? Will courts in your jurisdiction enforce a contract that has a foreign governing law?

In proceedings to enforce the obligations of a Bermuda company, Bermuda courts generally would give effect to the choice of foreign law as the governing law of the contract, provided that: (i) the point is specifically pleaded; (ii) the choice of law is valid and binding under foreign law; and (iii) recognition would not be contrary to public policy as that term is understood under Bermuda law. Where the foreign governing law is the laws of England and Wales, Bermuda courts are well-practised in enforcing such contracts. Not only are English court judgments automatically enforceable in certain circumstances (see question 7.2 below), but Bermuda courts regularly refer to persuasive English case law, and the ultimate court of appeal in Bermuda is the UK Privy Council.

7.2 Will the courts in your jurisdiction recognise and enforce a judgment given against a company in New York courts or English courts (a "foreign judgment") without re-examination of the merits of the case?

A final and conclusive judgment in the New York courts against a Bermuda company, based on a contract under which a sum of money is payable (not being in respect of multiple damages, or a fine, penalty, tax or other charge of similar nature) (**a Money Claim**) may be enforced in Bermuda under the common law doctrine of obligation for the debt evidenced by the New York court judgment. When considering whether a New York court judgment should be recognised and enforced, such proceeding would likely be successful provided that (a) the New York court was competent to hear the action in accordance with private international law principles as applied in Bermuda, and (b) the judgment is not contrary to public policy in Bermuda, has not been obtained by fraud, or in proceedings contrary to natural justice and is not based on an error in Bermuda law.

A final and conclusive judgment in the superior courts of England against a Bermuda company, based on a Money Claim would, on registration in accordance with the Judgments (Reciprocal Enforcement) Act 1958, be enforceable in Bermuda without the necessity of any retrial of issues or any re-examination of underlying claims, provided that the judgment: (a) is final and conclusive (notwithstanding that any appeal may be pending against it or it may be still subject to an appeal in England); (b) has not been given on an appeal from a court in England which is not a superior court in England; and (c) is duly registered in the Supreme Court of Bermuda.

Additionally, a foreign judgment against a Bermuda company may form the basis of a statutory demand, even if the judgment has not been registered as a judgment under Bermuda law, provided that the jurisdiction of the foreign court is not disputed on genuine grounds. Non-payment of the statutory demand would be sufficient for the secured creditor to seek commencement of liquidation proceedings.

Where a foreign judgment is expressed in a currency other than Bermuda dollars the registration will involve the conversion of the judgment debt into Bermuda dollars on the basis of the exchange rate prevailing at the date of the judgment. The current policy of the BMA is to permit payment in the original judgment currency.

7.3 Assuming a company is in payment default under a loan agreement or a guarantee agreement and has no legal defence to payment, approximately how long would it take for a foreign lender to (a) assuming the answer to question 7.1 is yes, file a suit against the company in a court in your jurisdiction, obtain a judgment, and enforce the judgment against the assets of the company, and (b) assuming the answer to question 7.2 is yes, enforce a foreign judgment in a court in your jurisdiction against the assets of the company?

Bermuda maintains a separate Commercial Court division of its Supreme Court, with judges experienced in commercial matters.

A commercial claim is commenced by issuing a writ of summons in the Registry of the Supreme Court, endorsed with a statement of claim and the relief sought. A Bermuda company respondent generally has 14 days to submit and file a response or contest the jurisdiction of the Bermuda court. It is possible for a suit to be filed and judgment obtained within a few weeks.

If jurisdiction is contested or the respondent disputes the matters which form the statement of claim, the appellant is entitled to respond and proceedings can be prolonged in a similar fashion as they may be in other common law jurisdictions.

If satisfied that a foreign judgment fulfils the requirements for registration, a Bermuda court will register the judgment as a matter of course. However, actual enforcement cannot proceed until the expiry of the judgment debtor's allotted time for challenging registration or any challenge has been determined. Foreign lenders may request summary judgments, interim judgments, costs awards and injunctions, such as Mareva and interlocutory injunctions, which can be obtained on a "same day" basis to prevent dispersal of assets.

7.4 With respect to enforcing collateral security, are there any significant restrictions which may impact the timing and value of enforcement, such as (a) a requirement for a public auction, or (b) regulatory consents?

There are no significant enforcement restrictions under Bermuda law. Most foreign judgment creditors seek the appointment of a receiver, to assist with gathering and realising the assets of a defaulting debtor and speed up the process, or seek to liquidate the defaulting debtor and engage liquidators to undertake collateral realisation.

Additionally, it may be possible to obtain a Bermuda writ of sequestration to have sequestrators appointed to take charge of all the defendant's assets until the defendant complies with the judgment.

There are restrictions in Bermuda regarding the ownership of land and real estate (see question 3.3 above) and shares of a Bermuda company (see question 3.6 above), which may require prior authorisation from Bermuda authorities.

7.5 Do restrictions apply to foreign lenders in the event of (a) filing suit against a company in your jurisdiction, or (b) foreclosure on collateral security?

There are no specific restrictions applicable to foreign lenders in the event of filing suit against a Bermuda company or otherwise applicable to foreclosure on collateral security. However, most foreign lenders prefer to appoint receivers or provisional liquidators to assist with the realisation of assets or foreclosure of collateral security.

7.6 Do the bankruptcy, reorganisation or similar laws in your jurisdiction provide for any kind of moratorium on enforcement of lender claims? If so, does the moratorium apply to the enforcement of collateral security?

After the presentation of a winding-up petition, the Bermuda company or any of its creditors may apply to the Bermuda court for a stay of proceedings.

No moratoriums apply to the enforcement of collateral security, as secured parties generally operate outside of Bermuda's bankruptcy regime.

7.7 Will the courts in your jurisdiction recognise and enforce an arbitral award given against the company without re-examination of the merits?

Bermuda is a party to the New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards and recognises awards made under arbitration agreements in a foreign jurisdiction that is also party to the New York Convention. If a foreign arbitral award is given against a defaulting debtor company as a result of arbitration in a "convention" jurisdiction, Bermuda's International Conciliation and Arbitration Act 1993 (**ICCA**) provides that the award may be enforced in Bermuda either by action or, with leave from the court, in the same way as a judgment or order to the same effect. The enforcing party must make an application for leave (with or without notice) under section 48 of the ICAA, regardless of the jurisdiction in which the award was made and (where leave is given) judgment can be entered in terms of the award, without re-examination of its merits.

On an *ex parte* application where leave has been granted to enforce the award, the order will not allow enforcement until the other party has 14 days to respond and bring an application to set the award aside. The 14-day response period is increased in certain circumstances.

8 Bankruptcy Proceedings

8.1 How does a bankruptcy proceeding in respect of a company affect the ability of a lender to enforce its rights as a secured party over the collateral security?

Bankruptcy proceedings against a Bermuda company may affect the ability of a lender to enforce its rights as underlying transactions may be attacked. See question 8.2 below.

8.2 Are there any preference periods, clawback rights or other preferential creditors' rights (e.g., tax debts, employees' claims) with respect to the security?

Any conveyance or other disposition of property made by or against a Bermuda company within six months prior to the commencement of its winding up will be invalid if it was made with the intent to fraudulently prefer one or more of such company's creditors at a time that the company was unable to pay its debts as they became due.

Under the fraudulent conveyance provisions of the Conveyancing Act 1983, a creditor may seek to set aside a disposition of property (including the creation of a security interest) if the disposition was made in circumstances where the transferor's dominant purpose was to put the property beyond the reach of a person (or class of persons) who is making, or may make, a claim against the transferor and the disposition was at an undervalue. Such a claim can only be made by an "eligible creditor", which is a person who: (i) is owed a debt by the transferor within two years after the disposition; (ii) on the date of the disposition is owed a contingent liability by the transferor, where the contingency giving rise to the obligation has occurred; or (iii) on the date of the action to set aside the disposition, is owed an obligation arising from a cause of action which occurred prior to or within two years after the date of the transfer.

In relation to floating charges, where a Bermuda company is being wound up, a floating charge on the undertaking or property of the Bermuda company created within 12 months of the commencement of the winding up will, unless it is proved that such Bermuda company immediately after the creation of the charge was solvent, be invalid, except to the amount of any cash paid to such Bermuda company at the time of or subsequently to the creation of, and in consideration for, the charge, together with interest on that amount at the statutory rate.

Certain debts are preferred by statute but only over (i) claims of unsecured creditors and (ii) claims of secured creditors who are holders of floating charges. In a winding up of a Bermuda company debts secured by fixed charges retain first priority, followed by: (a) all taxes owing to the Bermuda government and rates owing to a municipality; (b) all wages or salary (up to a maximum of BD$2,500 in respect of any one claimant) of any employee for services rendered to the company during the four months before the winding up; (c) all accrued holiday remuneration payable to any employee on termination of his employment before or following the winding up; (d) certain amounts due by the company as employer of any persons under the Contributory Pensions Act 1970 or any contract of insurance; (e) certain amounts due in respect of any liability for compensation under the Workmen's Compensation Act 1965, being amounts which have accrued before the winding up; (f) secured creditors under floating charges; and (g) unsecured creditors.

8.3 Are there any entities that are excluded from bankruptcy proceedings and, if so, what is the applicable legislation?

Generally, the winding-up and insolvency provisions in the Companies Act apply to all Bermuda companies. Licensed Bermuda banks are governed by a separate insolvency regime under the Banks (Special Resolution Regime) Act 2016, which has been passed but has not yet been brought into effect.

8.4 Are there any processes other than court proceedings that are available to a creditor to seize the assets of a company in an enforcement?

The remedies available to a creditor would generally be set out in the loan and security documents and would include exercising the power of sale, taking possession of assets and appointing a receiver.

Creditors can also reorganise, or reach a compromise with, a Bermuda company under a scheme of arrangement provided that the scheme is approved by the company and a supermajority of its creditors. Although a scheme will bind all creditors (or class of creditors), it must be sanctioned by the Bermuda court to be effective.

9 Jurisdiction and Waiver of Immunity

9.1 Is a party's submission to a foreign jurisdiction legally binding and enforceable under the laws of your jurisdiction?

The submission by a Bermuda company to the jurisdiction of a foreign court under a loan or security agreement would be recognised by a Bermuda court as a legal, valid and binding submission to the jurisdiction of the foreign court, provided that such submission is accepted by the foreign court and is legal, valid and binding under such foreign law.

9.2 Is a party's waiver of sovereign immunity legally binding and enforceable under the laws of your jurisdiction?

Yes, both private and public Bermuda companies can validly waive any claim of sovereign immunity.

10 Licensing

10.1 What are the licensing and other eligibility requirements in your jurisdiction for lenders to a company in your jurisdiction, if any? Are these licensing and eligibility requirements different for a "foreign" lender (i.e. a lender that is not located in your jurisdiction)? In connection with any such requirements, is a distinction made under the laws of your jurisdiction between a lender that is a bank *versus* a lender that is a non-bank? If there are such requirements in your jurisdiction, what are the consequences for a lender that has not satisfied such requirements but has nonetheless made a loan to a company in your jurisdiction? What are the licensing and other eligibility requirements in your jurisdiction for an agent under a syndicated facility for lenders to a company in your jurisdiction?

Foreign lenders, and foreign agents and trustees under syndicated facilities, do not need to be licensed in Bermuda to undertake lending business with Bermuda companies, unless they are otherwise carrying on business within Bermuda.

11 Other Matters

11.1 Are there any other material considerations which should be taken into account by lenders when participating in financings in your jurisdiction?

The information included in this chapter cover the key issues to be considered in secured lending transactions in Bermuda. Specific advice should be sought from Bermuda counsel at the earliest opportunity to ensure security is effective and readily enforceable in Bermuda.

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Bolivia

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1 Overview

1.1 What are the main trends/significant developments in the lending markets in your jurisdiction?

In 2014, several changes regarding financial intermediaries were established by the Financial Services Law, with the objective of creating specialised bodies and aiming to have a stronger government presence in this specific area by means of a regulatory entity. In early July 2014, specific regulations were issued in order to establish loan rates that must be applied by financial intermediaries, especially for lending transactions completed in the industry sector and for social housing loans. These specific regulations are expected to allow portfolio growth in priority sectors defined by the national government, specifically production credits and access to social housing. As of the beginning of the implementation of these changes at the end of 2017, Bolivian financial entities have reported an achievement in the goals settled by the laws and regulations.

According to the Financial System Supervision Authority (ASFI), the credit portfolio of Banks in Bolivia reached US$ 21.800 million in 2017, which means it exceeded the sum reached in July 2016 by approximately US$ 5,000 million, surpassing the required minimum levels for the credit portfolio established by regulations since 2014 and also showing a sustained growth in these levels. Most of the loans that were given by banks in 2017 were granted to the microcredit, followed by the business and housing loans sectors. Loans granted to the consuming sector (credits granted to physical persons) continued growing as well, reaching US$ 15.359. An important consideration is that 79% of the credit portfolio of Bolivian Financial Entities, was granted by "Multiple Banks", showing the consolidation of this kind of entity before others such as the Development Financial Institutions (IFDs) and the Public Bank.

Regarding interest rates, it is important to quote the changes applied since 2014 also. Specific regulations for financial institutions, SME banks, multiple banks and others, and especially Supreme Decrees (DS) 1842 and 2055, both issued in 2014, regulate interest rates for loans for social housing, loans for the industry sector and deposit rates. These regulations also establish minimum levels for the credit portfolio of financial entities operating in Bolivia. This kind of regulation aims to strengthen the industry sector and to improve the quality of life in Bolivian households through more affordable loans and higher returns on their savings.

Concerning social housing loans, new specific regulations oblige financial entities to give the total amount requested by lenders. This change has been made because of the obligation of these entities to constitute a guarantee fund by providing 6% of their profits in order to allow lenders to have access to housing loans without the need of paying in advance 10% or 20% of the final price, which was the way it had to be done in the past. The increase in housing loans in 2017 is proof of the successful results of this change.

Finally, it is important to emphasise that no major changes in the lending markets regulations were issued in Bolivia in 2017.

1.2 What are some significant lending transactions that have taken place in your jurisdiction in recent years?

The Bolivian Financial Services Law distinguishes three types of financial institutions: (i) State-owned or State-controlled financial institutions, which include: (a) development banks, (b) public banks, and (c) financial development institutions; (ii) private financial institutions, which include: (a) private development banks, (b) private banks, (c) small and medium companies-focused banks, (d) savings and loans cooperatives, (e) housing loans-focused financial institutions, (f) financial development institutions and (g) rural communities financial institutions; and (iii) complementary financial services companies, which include: (a) leasing companies; (b) factoring companies; (c) warrant companies; (d) clearing houses; (e) financial information bureaus; (f) money transferal companies; (g) electronic cards administration companies; (h) money exchange companies; and (i) mobile transfer or payment companies.

At the beginning of the fourth quarter of 2017, the financial intermediation system in Bolivia remained strong and stable, with good levels of financial performance as a result of continued deposits and loan portfolio growth, accompanied by the lowest level of credit defaults registered in Bolivian history and adequate patrimonial support.

Public deposits closed at a balance of US$ 23,369,540, an increase of 2,876,540 compared to 2016.

Loans Portfolio

Until December 2017, the loans portfolio closed at US$ 21,847,844, an increase of US$ 2,955,844 compared to the end of 2016.

Industrial, Commercial and Services Sector Portfolios

Up until December 2017, the loan portfolio for the industry sector, which comprises entrepreneurs' credits, micro credits and SMEs credits for all types of activities and industries (such as agriculture, hunting, forestry and fishing, extraction of crude oil and natural gas, metallic and non-metallic mineral mining, manufacturing, electricity, gas, water and construction) amounts to US$ 6,838,362.

Social Housing Sector Portfolio

The Financial Services Law of Bolivia No. 393 dated August 21st 2013, introduced Social Interest Housing loans as a new category for bank loans, which is targeted at middle income families or individuals that want to buy or build their first house or apartment. One of the main conditions required in order to apply for this type of loan is that the cost of said house must not exceed the US$ 120,000 price barrier, or US$ 100,000 in the case of apartments.

This particular type of loan has a State-regulated fixed interest rate, which can only vary from 5.5% to 6.5%, depending on the amount of the specific loan.

Another particular characteristic of this type of loan is that no down payment or guarantee is required. In order to guarantee these loans, the Bolivian government issued a regulation that forces private banks to invest 6% of their annual earnings into special guarantee funds created by them for that sole purpose.

As of December 2017, the social housing sector portfolio in Bolivia reached US$ 5,561,063.

2 Guarantees

2.1 Can a company guarantee borrowings of one or more other members of its corporate group (see below for questions relating to fraudulent transfer/financial assistance)?

In Bolivia, companies within a corporate group can secure loans from their companies provided that they belong to the same group and the same category (e.g. electricity); however, companies that belong to a different business group cannot guarantee loans to any of their members. On the other hand, companies that belong to financial groups are prohibited from securing loans unless they are companies dedicated to investments.

2.2 Are there enforceability or other concerns (such as director liability) if only a disproportionately small (or no) benefit to the guaranteeing/securing company can be shown?

If the company is dedicated to guaranteeing investment, the responsibility lies with those who have approved the transaction. In general, however, directors also have responsibility as the operation is guaranteed by the goods of the company.

If the directors of a company ensure an operation and such directors do not have the authority to perform such act, they are also responsible for their own assets.

2.3 Is lack of corporate power an issue?

Indeed; the lack of authority enabling a person or persons to act on behalf of a company is a grave and a serious problem. There are certain powers that enable people to carry out the activities and business of a company, and any person who acts without such authority is liable to penalties which are provided by law. All further acts performed by those people and the company might be void or voidable.

2.4 Are any governmental or other consents or filings, or other formalities (such as shareholder approval), required?

Bolivian law does not provide for State authorisation and credit approval for the creation of securities, except concerning State-owned companies.

However, when a company applies for a loan, the application must have the appropriate support, such as financial analysis of the company demonstrating the need for a loan, and, overall, approval of the shareholders of the company.

In the stock market, it is necessary to have the approval of the shareholders in order to issue bonds.

For the granting of guarantees, such guarantees must be fully sanitised and free from all liens. If the security has a lien, the creditor will require permission for the property to be used as security for other creditors.

2.5 Are net worth, solvency or similar limitations imposed on the amount of a guarantee?

It depends on the amount requested. If the company has some financial indicators that are not in line with the credit policy of the entity, it may request the granting of additional collateral to support the operation.

2.6 Are there any exchange control or similar obstacles to enforcement of a guarantee?

For the enforcement of a guarantee there are no exchange controls in Bolivia. The main obstacle is the time it takes to enforce a guarantee in the judicial system; such time frame depends on the individual case (please see the answers in section 8).

For the enforcement of a security with no exchange controls, the obstacles encountered are the extended time frames required for the judicial system and the processing of its guarantees.

3 Collateral Security

3.1 What types of collateral are available to secure lending obligations?

In Bolivia, lending obligations are secured by mortgages, collateral and unsecured personal guarantees.

3.2 Is it possible to give asset security by means of a general security agreement or is an agreement required in relation to each type of asset? Briefly, what is the procedure?

The creation of securities depends on the type of loan requested. The procedure is to sign a contract, and each contract must be guaranteed. The contract also specifies the kind of guarantee given by the borrower, its characteristics, its value, its usefulness and for how long the collateral will be in force.

3.3 Can collateral security be taken over real property (land), plant, machinery and equipment? Briefly, what is the procedure?

Yes, it can. Once the loan has been approved, the borrower delivers all relevant documents pertaining to the guarantee. These documents remain in the custody of the lender, which is usually a bank. The appropriate authorities then keep track of whether the property is collateral for a bank or institutional lender. However, this does not mean that the borrower transfers his ownership of the property to the bank, except where there is breach of property ownership, in which case it may be transferred to third parties to honour the debt.

3.4 Can collateral security be taken over receivables? Briefly, what is the procedure? Are debtors required to be notified of the security?

Bolivian law does not provide for this.

3.5 Can collateral security be taken over cash deposited in bank accounts? Briefly, what is the procedure?

Generally not, but most loan agreements in Bolivia provide that the borrower has to keep a bank account where there is enough money to cover the monthly loan instalments; if the account is declared to have no money, the bank has the power to debit the money from other accounts that the borrower may have with the bank, after communicating these actions to the debtor.

3.6 Can collateral security be taken over shares in companies incorporated in your jurisdiction? Are the shares in certificated form? Can such security validly be granted under a New York or English law governed document? Briefly, what is the procedure?

Bolivian law does not allow companies to give its shares in warranty as in other countries. What is usually done is that the shareholders of a company must agree to be guarantors of the credit operations of the company and they guarantee the loan with their shares.

In Bolivia, shares have to be issued certificates and such certificates must be registered in the books of the company's shareholders.

As part of a loan agreement, a clause allowing the resolution of disputes and enforcement of a security to be resolved under the laws of another country may be included. This is not a usual practice in Bolivia, but it is allowed, depending on the terms of the agreement between parties.

3.7 Can security be taken over inventory? Briefly, what is the procedure?

Yes, it can. Collateral may be taken over goods in process, finished goods or raw materials. The debtor must request a warrant from the company storing the materials. The bank has control of such materials and each time the debtor needs to access the materials it has to apply for the bank's authorisation. Therefore, the bank has control over the debtor's production and is satisfied that the debtor will honour its debt.

3.8 Can a company grant a security interest in order to secure its obligations (i) as a borrower under a credit facility, and (ii) as a guarantor of the obligations of other borrowers and/or guarantors of obligations under a credit facility (see below for questions relating to the giving of guarantees and financial assistance)?

No it cannot. In Bolivia, this is regulated by the Supervisory Authority of the Financial System (ASFI) and is punishable under the law.

3.9 What are the notarisation, registration, stamp duty and other fees (whether related to property value or otherwise) in relation to security over different types of assets?

Notary fees on guarantees are 4/1,000 of the loan amount for warranty registration in the office of property rights. Further legal costs of around US$ 150 also apply, along with the cost of registration at the Commercial Register in Bolivia, which is US$ 25.

3.10 Do the filing, notification or registration requirements in relation to security over different types of assets involve a significant amount of time or expense?

For the registration of a guarantee, on average a time period of 30 to 45 days is required. On top of this, notary processes will also take between 10 and 15 days. A total of 60 days, on average, is required, and the costs vary in relation to the amount of each loan.

3.11 Are any regulatory or similar consents required with respect to the creation of security?

No regulatory or similar consents are required for the creation of a security.

3.12 If the borrowings to be secured are under a revolving credit facility, are there any special priority or other concerns?

The priority on the enforcement of a guarantee is given by the number of loans that were requested in that line, taking into account that the line of credit has a limit and that limit defines how many loans can be requested. This also dictates if the warranty covers all of the borrowing in that line of credit.

The priority is given predominantly by the order in which the loans were requested; if the guarantee is executed, the amount collected will first cover the oldest operations and then operations that were requested at a later date.

3.13 Are there particular documentary or execution requirements (notarisation, execution under power of attorney, counterparts, deeds)?

For the enforcement of a security, financial institutions have to give their representatives power of attorney, enabling them to pursue the enforcement of the security. These powers must be registered in the Commercial Register of Bolivia, which is also responsible for their validation.

4 Financial Assistance

4.1 Are there prohibitions or restrictions on the ability of a company to guarantee and/or give security to support borrowings incurred to finance or refinance the direct or indirect acquisition of: (a) shares of the company; (b) shares of any company which directly or indirectly owns shares in the company; or (c) shares in a sister subsidiary?

(a) Shares of the company

In Bolivia, it is expressly forbidden by law for a company to acquire its own shares.

(b) Shares of any company which directly or indirectly owns shares in the company

Cross shareholding is not legally possible in Bolivia.

(c) Shares in a sister subsidiary

Bolivian law does not provide any restrictions in this case.

5 Syndicated Lending/Agency/Trustee/Transfers

5.1 Will your jurisdiction recognise the role of an agent or trustee and allow the agent or trustee (rather than each lender acting separately) to enforce the loan documentation and collateral security and to apply the proceeds from the collateral to the claims of all the lenders?

In Bolivia, the law does not prohibit the role of an agent or trustee and thus its capacity to enforce the loan documentation and collateral security and to apply the proceeds from the collateral to the claims of a group of lenders of the same borrower.

The Bolivian Civil Code states that all of the assets of a multiple debtor constitute their common guarantee.

5.2 If an agent or trustee is not recognised in your jurisdiction, is an alternative mechanism available to achieve the effect referred to above which would allow one party to enforce claims on behalf of all the lenders so that individual lenders do not need to enforce their security separately?

In Bolivia, agents are recognised as long as they have a written legal mandate from the lenders, so they are responsible for performing the collection and enforcement of security granted by banks to borrowers. This does not mean, however, a transfer of the portfolio of the banks to the agent.

5.3 Assume a loan is made to a company organised under the laws of your jurisdiction and guaranteed by a guarantor organised under the laws of your jurisdiction. If such loan is transferred by Lender A to Lender B, are there any special requirements necessary to make the loan and guarantee enforceable by Lender B?

No, there are not, because the lender has cancelled the amount due. The requirement for this transfer is that Lender A has to lift the lien on the collateral, so that Lender B can record the loan and have the right to charge his debt and the guarantee.

6 Withholding, Stamp and Other Taxes; Notarial and Other Costs

6.1 Are there any requirements to deduct or withhold tax from (a) interest payable on loans made to domestic or foreign lenders, or (b) the proceeds of a claim under a guarantee or the proceeds of enforcing security?

No, there are not, since the legislation does not provide this figure, the only thing that sets the tax law is that, if a borrower is foreign, payments made by the debtor for interest are taxed at a rate of 12.5%, as long as the loan agreement was signed in Bolivia. If a loan agreement was not signed in Bolivia, the rate of 12.5% applies to the total amount, including the debt amount and its interest, as it is considered a remittance abroad.

The debtor is liable to pay agent retention and replacement of tax liability.

6.2 What tax incentives or other incentives are provided preferentially to foreign lenders? What taxes apply to foreign lenders with respect to their loans, mortgages or other security documents, either for the purposes of effectiveness or registration?

Bolivian tax legislation does not provide any tax incentives or benefits; the taxes that apply are detailed in question 6.1.

6.3 Will any income of a foreign lender become taxable in your jurisdiction solely because of a loan to or guarantee and/or grant of security from a company in your jurisdiction?

Applicable taxes are detailed in question 6.1.

6.4 Will there be any other significant costs which would be incurred by foreign lenders in the grant of such loan/guarantee/security, such as notarial fees, etc.?

No, there will not, just those listed in question 3.9.

6.5 Are there any adverse consequences to a company that is a borrower (such as under thin capitalisation principles) if some or all of the lenders are organised under the laws of a jurisdiction other than your own? Please disregard withholding tax concerns for purposes of this question.

If the loan agreement is made under the laws of a foreign country (e.g. U.S.A.), and under such legislation consequences exist for lenders, such adverse consequences apply in Bolivia.

On the contrary, if the loan is carried out under Bolivian legislation, there are no consequences because Bolivia does not have experience and jurisprudence in such cases.

7 Judicial Enforcement

7.1 Will the courts in your jurisdiction recognise a governing law in a contract that is the law of another jurisdiction (a "foreign governing law")? Will courts in your jurisdiction enforce a contract that has a foreign governing law?

Bolivian courts recognise and enforce contracts subject to foreign law, provided they contain two elements: first, that the benefits arising out of these contracts are to be utilised in Bolivia; and second, that the foreign law under which the contract was created is not contrary to Bolivian laws.

7.2 Will the courts in your jurisdiction recognise and enforce a judgment given against a company in New York courts or English courts (a "foreign judgment") without re-examination of the merits of the case?

The courts in Bolivia execute foreign judgments as long as there is a treaty in place with the country concerned. Following the principle of reciprocity, and in the absence of treaties on the matter, Bolivian courts will grant these judgments the same force that the nation in question gives to Bolivian judgments. However, if a foreign judgment was enforceable, it would be necessary to follow a procedure in which the concerned party must seek the enforcement of the judgment at the Supreme Court, and later request the answers of the other party within 10 days. With or without such answers, and after a fiscal opinion (which involves additional time), the court will determine whether or not to enforce the judgment. The enforcement of the judgment shall correspond to the tribunal which would have been the case at first instance in Bolivia.

The new Bolivian Procedure Code (which has come fully into force in February 2016) maintains the same principles and procedure on this matter that were established in the previous Procedure Code. However, it specifies that even though it is not necessary for courts in Bolivia to re-examine the merits of the case, it is necessary for the Supreme Court to recognise the foreign judgment (to determine whether the judgment meets the requirements and procedural basic principles) in order to proceed to its execution (only if the judgment concerns the compliance of an obligation or if it is the intention of a party to validate its probative effects).

7.3 Assuming a company is in payment default under a loan agreement or a guarantee agreement and has no legal defence to payment, approximately how long would it take for a foreign lender to (a) assuming the answer to question 7.1 is yes, file a suit against the company in a court in your jurisdiction, obtain a judgment, and enforce the judgment against the assets of the company, and (b) assuming the answer to question 7.2 is yes, enforce a foreign judgment in a court in your jurisdiction against the assets of the company?

A suit for non-payment can be filed as soon as the deadline the parties have agreed has expired. Generally, it will be possible to act by the way of an executive process, which is quite quick (the suit is filed, the judge examines the procedural requirements of executive judgment, and if appropriate he shall issue a formal notice to be fulfilled within three days, besides having the injunction of the debtor's assets). The executive process should take about one to two months (depending on which exceptions shall be made, also counting the evidence term which will take 10 additional days). In case the loan agreement included a waiver clause regarding the executive procedure, the obligation may also be required by way of coercive procedure, which takes less time than the executive procedure. In all cases, the enforcement of the judgment will depend on if it is enforceable, and, if it is enforceable, the court will execute the judgment within the time established or, failing that, within three days.

7.4 With respect to enforcing collateral security, are there any significant restrictions which may impact the timing and value of enforcement, such as (a) a requirement for a public auction, or (b) regulatory consents?

It depends on the guarantee. In general, a public auction is required. This involves a procedure that might take over a month. However, no regulatory consents are needed to enforce collateral securities.

7.5 Do restrictions apply to foreign lenders in the event of (a) filing suit against a company in your jurisdiction, or (b) foreclosure on collateral security?

No. If the requirements are met, there is no restriction on the lender to filing a law suit against the borrower or the guarantee it has granted.

7.6 Do the bankruptcy, reorganisation or similar laws in your jurisdiction provide for any kind of moratorium on enforcement of lender claims? If so, does the moratorium apply to the enforcement of collateral security?

Please see the answer to question 8.1.

7.7 Will the courts in your jurisdiction recognise and enforce an arbitral award given against the company without re-examination of the merits?

Bolivia has signed and ratified the New York Convention on the enforcement of arbitral awards. In this sense, the Bolivian courts do recognise such decisions without needing to re-examine their merits. Moreover, the new civil procedure code prescribes that arbitral awards enable a lender to initiate a coercive enforcement of a debt, and it is not necessary for the judge to re-examine the merits of such arbitral award.

The procedure to enforce a foreign arbitral award is the same as described in question 7.2 for foreign judgments.

8 Bankruptcy Proceedings

8.1 How does a bankruptcy proceeding in respect of a company affect the ability of a lender to enforce its rights as a secured party over the collateral security?

The ability of a lender is affected because the entire bankruptcy process is handled by a judge. In this sense, the affected lender cannot seek the enforcement of its security as freely as in the case of not being subject to the debtor company's bankruptcy. However, bankruptcy does not involve any other violation of the right of the lender to make a debt enforceable and the debt shall be paid by means of the security given by the debtor.

8.2 Are there any preference periods, clawback rights or other preferential creditors' rights (e.g., tax debts, employees' claims) with respect to the security?

All guarantees have priorities on the enforcement of the goods or assets given as such. However, tax debts and employee claims are always taken as preferential creditors' rights in the case of bankruptcy of the borrower.

8.3 Are there any entities that are excluded from bankruptcy proceedings and, if so, what is the applicable legislation?

Yes; financial intermediaries, for example, are only subject to a process of "intervention", after which it is to be decided whether to give it a solution or to proceed to compulsory liquidation.

8.4 Are there any processes other than court proceedings that are available to a creditor to seize the assets of a company in an enforcement?

The only way other than court proceedings to seize the assets of a company in enforcement is a process called "*dación en pago*", which consists of a new transaction between the creditor and the debtor through which the creditor receives a new asset, or the asset given as a guarantee, as payment of his credit.

9 Jurisdiction and Waiver of Immunity

9.1 Is a party's submission to a foreign jurisdiction legally binding and enforceable under the laws of your jurisdiction?

Please see the answer to question 7.1. However, a party cannot submit to a foreign jurisdiction on its own, for it takes both parties to choose the jurisdiction that will rule the contract and its enforcement.

9.2 Is a party's waiver of sovereign immunity legally binding and enforceable under the laws of your jurisdiction?

If the sovereign immunity was awarded to a party in Bolivia, it would be by means of a law; therefore it would not be a disposable right, which implies that a party's waiver of sovereign immunity would not be legally binding and enforceable under the laws of Bolivia. Nevertheless, in the event a party's sovereign immunity was awarded in a country the laws of which allow the waiver of sovereign immunity, then it would be legally binding and enforceable in Bolivia.

10 Licensing

10.1 What are the licensing and other eligibility requirements in your jurisdiction for lenders to a company in your jurisdiction, if any? Are these licensing and eligibility requirements different for a "foreign" lender (i.e. a lender that is not located in your jurisdiction)? In connection with any such requirements, is a distinction made under the laws of your jurisdiction between a lender that is a bank *versus* a lender that is a non-bank? If there are such requirements in your jurisdiction, what are the consequences for a lender that has not satisfied such requirements but has nonetheless made a loan to a company in your jurisdiction? What are the licensing and other eligibility requirements in your jurisdiction for an agent under a syndicated facility for lenders to a company in your jurisdiction?

Bolivian law provides that a bank or financial institution is of domestic or foreign origin, and dedicated to perform financial intermediation and financial services to the public, both in the country and outside the country.

The financial intermediation and auxiliary financial services will be carried out by financial institutions authorised by the Supervisory Authority of the Financial System (ASFI). No person, natural or legal, will perform regularly in the territory of Bolivia the activities of financial intermediaries and financial auxiliaries services described by law, without prior permission of incorporation and operation granted by ASFI, with the formalities established by law.

Any natural or legal person, domestic or foreign, domiciled in the country or not, who does not meet the requirements and formalities concerning the organisation and functioning of financial intermediaries and financial auxiliaries services under the Act is prohibited from making announcements, publications and circulating papers, written or printed, the terms of which imply that such person has legal authorisation to perform activities reserved by law to the said banks. In the same way, any natural or legal person may not use in its name, in Spanish or another language, terms that may lead the public to be confused with legally authorised financial institutions.

The requirements for the establishment of a financial institution in Bolivia and for obtaining the operating licence are as follows:

A) Founders may not:
   1. Be declared legally incapable to engage in commerce.
   2. Have an indictment or conviction for committing crimes.
   3. Have outstanding debts related to the financial system or running off loans.

B) In order to obtain an operating licence, a financial institution must:
   1. Have conducted a study of economic and financial feasibility.
   2. Have drafted articles of incorporation and bylaws of a corporation.
   3. Have a certified personal history for individuals – issued by competent authority.
   4. Have a certificate of fiscal solvency and disclosure of assets of the founders.

Additionally, in August 2015, ASFI issued a regulation establishing the criteria to determine if a loan, a financial intermediation activity or any activity reserved for financial institutions exclusively, is made in a "massive" or in a "regular" way. Those criteria are based on the frequency of the activities aforementioned (weekly, monthly, quarterly, semi-annually and annually) and/or on the gross incomes earned monthly, quarterly, semi-annually and annually by the lender. According to this regulation, if a natural or legal person acts as a lender or as a financial intermediary meeting the criteria set out in the regulation, such activity is considered illegal and has the following consequences: a) ASFI will issue a stopping order for the person performing the illegal activity; b) if an unauthorised lender has any office in Bolivia, ASFI will be able to close it permanently; and finally c) unauthorised financial intermediation activities can be prosecuted as crimes before Bolivian courts.

11 Other Matters

11.1 Are there any other material considerations which should be taken into account by lenders when participating in financings in your jurisdiction?

The considerations that should be taken into account are those that are provided by law and detailed in this chapter.

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Criales & Urcullo
ABOGADOS

Criales & Urcullo is a full-service law firm serving the needs of businesses, governmental entities, non-profit organisations and individual clients in Bolivia and other Latin American countries. At Criales & Urcullo we measure our success by the success of our clients and the longevity of their relationships with us.

Our law firm is the most significant legal services provider to the securities market in Bolivia. Our clients in this sector are the Bolivian Stock Exchange, the Bolivian Central Depository, and the country´s biggest stock exchange brokers and investment funds.

Brazil

Ricardo Simões Russo

Pinheiro Neto Advogados

Leonardo Baptista Rodrigues Cruz

1 Overview

1.1 What are the main trends/significant developments in the lending markets in your jurisdiction?

Brazil has a highly sophisticated financial system, with a set of detailed and specific rules and regulations that must be observed, on the one hand, by local lenders (banks and financial institutions) and creditors (investment funds, securitisation vehicles and market investors) and, on the other hand, by borrowers and/or issuers of debt instruments (in terms of disclosure rules, registration requirements, exposure regarding specific lenders, collateral creation requirements, among others).

Given a stable and promising economic scenario in the early 2000s, the level of debt incurred by local companies over the past 10 years doubled. Such growth in debt transactions was also verified due to the creation by the local government of a set of rules which provided better security to creditors such as: the creation of types of collateral with a more expeditious foreclosure proceedings (fiduciary sale/assignment of immovable and movable assets); better clarification on the rules governing extrajudicial and in-court debt reorganisations; the creation of new debt instruments better evidencing credit transactions (such as banking credit notes – *cédulas de crédito bancário* – and banking financial notes – *letras financeiras*); and the enactment of incentives for the use of the local capital markets for the private funding of local companies (through the issuance of debentures, for instance).

During such period, an increase of lending/credit transactions was verified in a number of local market segments, including: typical commercial lending transactions, the proceeds of which being used for the short/medium-term cash needs of local companies; foreign currency denominated bond offerings, implemented by companies whose revenues are indexed to foreign currency (such as agribusiness and the oil & gas sector, as well as large exporters); and syndicated loan transactions (local and international lenders), in which short-term debt of local companies was converted into long-term ones with better conditions.

Given the shortage of infrastructure in Brazil, the local government is promoting a number of public bids to try to bring local and foreign private investors to manage a number of infrastructure sectors, including energy generation and transmission, renewable energy projects, state and federal highways, ports, airports, logistics and urban mobility, among others. The funding needs of such long-term infrastructure projects is being provided not only by the local federal Exim bank (BNDES), but also by private banks (granting of bank guarantees and bridge loans) and the local capital markets (in this regard, a specific debt instrument was created by the government in 2011 – infrastructure debentures – which granted tax exemptions to local and foreign investors).

As from 2013, the crisis affecting emerging markets globally had a relevant impact on the Brazilian economy which was evidenced in a decrease in lending transactions and a rise in interest rates, promoting a scenario in which lenders became more selective and companies began to try to renegotiate previous transactions (as opposed to entering into new debt).

Until December 2016, given the economic scenario, local lending markets were: implementing structures aimed at providing credit transactions with more attractive interest rates (such as capital markets transactions, with comprehensive collateral packages); renegotiating or exchanging lending transactions that will mature within a short-/medium-term period; and using mechanisms or implementing structured transactions that may have a lower impact in the debt obligations of local companies (such as securitisation transactions).

The Brazilian economy has been recovering since the latest political events and the local lending market is becoming even more attractive to foreign and local investors. Some Brazilian companies started looking offshore for lending opportunities, followed by several debt issuances by Petrobras throughout 2016 and 2017.

As an indication of the recent recovery of the Brazilian economy, it is worth mentioning the several equity and debt capital market transactions which occurred throughout 2017 (e.g., IPOs of Carrefour (*Atacadão*), Movida, Biotoscana and the follow-on of Azul and many other that are currently in the pipeline of investment banks to be launched in 2018.

1.2 What are some significant lending transactions that have taken place in your jurisdiction in recent years?

Recently, certain relevant lending transactions were completed in the local markets, such as: the issuance of US$ 6.75bn five- and 10-year dollar-denominated bonds by Petrobras (May 2016) and US$ 2bn (January 2018); the switch made by USJ of bonds in April, replacing US$ 246 million of its 9.875% 2019 bond with a US$ 197 million 9.875%/12% payment-in-kind toggle note due in 2021; the issuance by Marfrig Holdings (Europe) BV, European subsidiary of Marfrig Global Foods S.A., of a seven-year single-tranche bond, raising US$ 750 million at a yield of 8.25%; the R$ 5bn issuance of Tier I perpetual bonds by Banco Itaú Unibanco; JSL Europe issuance of bonds in the amount of US$ 300 million; the US$ 1bn issuance of notes by Cemig; US$ 400 million issuance of bonds by Azul; and US$ 1bn issuance of notes by BNDES.

In the infrastructure sector only, it is expected that over the next five years an amount of approximately R$ 70bn to R$ 100bn will be needed by local companies, given their long-term financial needs.

2 Guarantees

2.1 Can a company guarantee borrowings of one or more other members of its corporate group (see below for questions relating to fraudulent transfer/financial assistance)?

Yes. Pursuant to Brazilian laws and regulations, there is no limitation for a company to guarantee borrowings of one or more other members of its corporate group.

2.2 Are there enforceability or other concerns (such as director liability) if only a disproportionately small (or no) benefit to the guaranteeing/securing company can be shown?

There are no enforceability concerns if all the required corporate approvals (as required by the companies' by-laws or articles of association) are in place. Brazilian law defines personal guarantees, such as surety (*fiança)* as an accessory personal obligation which depends on a main obligation to which it is bound. If the main obligation ceases to exist, the *fiança* will not endure.

It is important to bear in mind, however, that such guarantees are usually granted without any consideration to be received by the guarantor and, in the event that a guarantor were to become insolvent or subject to a reorganisation proceeding (*recuperação judicial ou extrajudicial*) or to bankruptcy, the guarantees, if granted up to two years before the declaration of bankruptcy, may be deemed to have been fraudulent and declared void, based upon such guarantor being deemed not to have received fair consideration in exchange for its guarantee.

2.3 Is lack of corporate power an issue?

Yes. In order to execute a legal, valid and enforceable guarantee, the representative of the guarantor, executing the appropriate document, must have all corporate powers, pursuant to the company's by-laws or articles of association and power-of-attorney; otherwise the guarantee can be declared null and void.

2.4 Are any governmental or other consents or filings, or other formalities (such as shareholder approval), required?

Generally, depending on the amount of the guarantee, it will be necessary to obtain approval from a shareholders' or management's meeting of the company, pursuant to its by-laws or articles of association.

2.5 Are net worth, solvency or similar limitations imposed on the amount of a guarantee?

No. The amount of a guarantee can be established freely by the parties.

2.6 Are there any exchange control or similar obstacles to enforcement of a guarantee?

There are no specific exchange controls for the enforcement of a guarantee. Brazilian exchange controls are focused on remittances from and to outside Brazil, registering such remittances on the Brazilian Central Bank's system. Additionally, it is worth noting that remittances abroad can only be made by financial institutions.

3 Collateral Security

3.1 What types of collateral are available to secure lending obligations?

Under Brazilian law, collateral arrangements (*in rem* guarantees) are usually created by either a pledge (*penhor*), a fiduciary sale/assignment (*alienação/cessão fiduciária*) or a mortgage (*hipoteca*).

A pledge is an *in rem* guarantee and consists of the delivery of transferable movable property by a debtor (or by a third party on his behalf) to its creditor (or to the creditor's representative) in guarantee of the debt. It is important to note that a pledge generally requires *tradição*, i.e., the actual physical transfer of possession of the asset from the pledgor to the pledgee. A pledge creates a lien on movable property upon delivery thereof by the pledgor to the pledgee, with the express understanding that the asset shall be retained solely as security for a certain debt. Accordingly, the pledgee has the right to retain possession over the pledged asset, but it is not allowed to create any other type of interest over it. The pledge does not transfer title over the assets to the pledgee.

The fiduciary sale/assignment is a type of security interest, pursuant to which the debtor assigns to the creditor the title to ("*resolutory property*") and the "*indirect possession*" of a certain asset, holding, therefore, only its physical possession (or "*direct possession*"). The debtor has direct possession of the property and is liable for the duties of a bailee, or a trust, in relation to it. The debtor will have full title and indirect possession of the asset back when he has fulfilled all of its obligations under the guaranteed credit (that is why title of the creditor is called "*resolutory property*"). Such guarantee mechanisms have the effect of transferring to the creditor title to certain fungible movable assets (fiduciary sale) or to certain fungible rights over movable assets (fiduciary assignment), as the case may be.

Mortgage is an *in rem* guarantee lying over real estate granted by a debtor (or by a third party on its behalf) in favour of its creditor to secure payment of a relevant debt.

3.2 Is it possible to give asset security by means of a general security agreement or is an agreement required in relation to each type of asset? Briefly, what is the procedure?

Pledge and *alienação/cessão fiduciária* agreements and deeds of mortgages are formal documents which must comply with certain requirements for purposes of the perfection of the security interest created thereby, having specific formalities for each type. In this sense, the relevant security documents must, generally: (i) be in writing; (ii) be executed by both creditor and debtor and attested by two witnesses; (iii) contain, at a minimum, information pertaining to the amount, maturity and interest rate (whenever applicable) of the underlying obligation, as well as a description (including particulars) of the collateral; and (iv) be registered with the appropriate Brazilian Public Registry of the domicile of the debtor (e.g., the Registry of Deeds and Documents in the case of common pledges and of *alienação/cessão fiduciária* and the Real Estate Registry in case of mortgages or *alienação fiduciária* of real estate properties). Registration is a mandatory requirement for the perfection of the security interest.

3.3 Can collateral security be taken over real property (land), plant, machinery and equipment? Briefly, what is the procedure?

Yes. Please refer to the answers to questions 3.1 and 3.2 above.

3.4 Can collateral security be taken over receivables? Briefly, what is the procedure? Are debtors required to be notified of the security?

Yes, it is possible to take a collateral security over receivables, pursuant to Brazilian law. The collateral is usually formalised through a fiduciary assignment of the receivables, together with a fiduciary assignment over the accounts that will receive such receivables. As for the procedure, please refer to the answer to question 3.2 above.

3.5 Can collateral security be taken over cash deposited in bank accounts? Briefly, what is the procedure?

Yes, it is possible to take a collateral security over cash deposited in bank accounts, pursuant to Brazilian law. The collateral is usually formalised through a fiduciary assignment over the accounts. As for the procedure, please refer to the answer to question 3.2 above.

3.6 Can collateral security be taken over shares in companies incorporated in your jurisdiction? Are the shares in certificated form? Can such security validly be granted under a New York or English law governed document? Briefly, what is the procedure?

Yes, it is possible to take collateral security over shares/quotas in companies incorporated in Brazil. The most common type of collateral over shares is *alienação fiduciária*. As the *alienação/cessão fiduciária* transfers the ownership of the shares to the creditor, the creditor, in general, will have priority in case of insolvency of the debtor, as provided by the Brazilian Bankruptcy Law. The creation of the security interest over shares is evidenced by formal documents which must comply with certain requirements for purposes of the perfection of the security interest created thereby. In this sense, the security documents must, generally: (i) be in writing; (ii) be executed by both creditor and debtor (as well as by the custodian, as the case may be) and attested by two witnesses; (iii) contain, at a minimum, information pertaining to the amount (either the exact, estimate or maximum amount), maturity and interest rate (whenever applicable) of the underlying obligation, as well as a description (including particulars) of the collateral; and (iv) be registered with the Registry of Deeds and Documents of the domicile of the debtor and creditor.

In addition to the registration before the Registry of Deeds and Documents, the security interest of registered shares is only created and perfected when the security interest is duly noted in the Share Registry Book. The security interest over shares held in custody with the stock exchange or other agent, in order to be valid in Brazil, must be duly registered in such system.

As regards quotas of limited liability companies, the most common type of collateral is pledge. Such collateral is usually registered through an amendment to the company's articles of association and filing of the respective quota pledge agreement before the Registry of Deeds and Documents.

In Brazil, shares are not usually issued in certificated form, despite the fact that the Brazilian Corporations Law allows such issuances. Shares are commonly issued as book entry records in the share registry book of the company issuer of the shares or registered with a bookkeeping entity.

Considering that the abovementioned types of collaterals are Brazilian types of collateral, the agreements creating such liens must be governed by Brazilian law; nevertheless, the main agreement, with terms and conditions of the credit being secured, can be governed by New York or English law.

Finally, it is worth mentioning that since January 2016 BM&FBOVESPA has been operating a new collateral system over shares of publicly held companies. Such new system enhanced the foreclosure procedures of collateral over shares of publicly held companies.

3.7 Can security be taken over inventory? Briefly, what is the procedure?

Yes, it is possible to take security over inventory. For the procedures involved, please refer to the answer to question 3.2 above.

3.8 Can a company grant a security interest in order to secure its obligations (i) as a borrower under a credit facility, and (ii) as a guarantor of the obligations of other borrowers and/or guarantors of obligations under a credit facility (see below for questions relating to the giving of guarantees and financial assistance)?

Yes, under Brazilian law, a company can grant a security interest in order to secure its obligations (i) as a borrower under a credit facility, and (ii) as a guarantor of the obligations of other borrowers and/or guarantors of obligations under a credit facility. It is worth mentioning that a thorough analysis of the company's by-laws or articles of association is required in order to assess, for each specific company, what are the required corporate approvals.

3.9 What are the notarisation, registration, stamp duty and other fees (whether related to property value or otherwise) in relation to security over different types of assets?

Usually, regardless of the type of assets being given as collateral, the registration fees (either for the Real Estate Registry or Registry of Deeds and Document) involve a percentage of the amount being secured by the collateral, limited to a cap. There are also notarisation fees; nevertheless, neither the notarisation nor the registration fees vary according to the region the competent registry is located.

3.10 Do the filing, notification or registration requirements in relation to security over different types of assets involve a significant amount of time or expense?

The period for registering security over different types of assets can vary from one to 30 days if there are no requirements made by the competent registry. Please note that registrations before the Real Estate Registry take longer than before the Registry of Deeds and

Documents. It is also worth noting that registrations before registry offices located in smaller cities may take longer.

3.11 Are any regulatory or similar consents required with respect to the creation of security?

Generally, no regulatory or similar consent is required with respect to the creation of securities, except for companies that operate in regulated business such as energy, telecoms, etc., which may need authorisation from the regulatory agencies regulating such sectors.

3.12 If the borrowings to be secured are under a revolving credit facility, are there any special priority or other concerns?

No. The amount secured will always be the amount (or maximum amount) established on the respective agreement that formalises the collateral.

3.13 Are there particular documentary or execution requirements (notarisation, execution under power of attorney, counterparts, deeds)?

No particular documentary or execution requirements are needed, with the exception of mortgages which must be made through a public deed. It is also worth mentioning that if the agreements are in the English language, they must be translated into Portuguese before being registered. If the document is executed abroad, in order to be registered in Brazil, it must be notarised and legalised by the nearest Brazilian consulate of the place of execution. However, Brazil is about to adopt the apostille system in the next months.

4 Financial Assistance

4.1 Are there prohibitions or restrictions on the ability of a company to guarantee and/or give security to support borrowings incurred to finance or refinance the direct or indirect acquisition of: (a) shares of the company; (b) shares of any company which directly or indirectly owns shares in the company; or (c) shares in a sister subsidiary?

(a) Shares of the company

Until 2015, there was an overall restriction for publicly held companies becoming (by means of succession – i.e. merger) a debtor of financial obligations initially incurred by its controlling shareholder. Since June 2015, this restriction is no longer applicable.

(b) Shares of any company which directly or indirectly owns shares in the company

Generally, there are no restrictions for this hypothetical situation. However, please note the following: (i) it is not uncommon to find provisions in by-laws that prevent corporations from giving guarantees or security for the benefit of third parties; and (ii) in case the so-called company (guarantor) is a Brazilian financial institution, insurance company or pension plan corporation, there could be a restriction depending on the amount of equity interest held by the beneficiary of the collateral/guarantee in the guarantor. Basically, such entities are not allowed to extend loans or give guarantees/security for the benefit of certain persons (e.g. controlling shareholders and managers).

(c) Shares in a sister subsidiary

The same comments mentioned in item (b) above apply to this item. Also, generally, publicly held companies shall not offer collateral to secure obligations of a third party, especially if such third party is in any way related to the controlling shareholder of the said publicly held company.

5 Syndicated Lending/Agency/Trustee/Transfers

5.1 Will your jurisdiction recognise the role of an agent or trustee and allow the agent or trustee (rather than each lender acting separately) to enforce the loan documentation and collateral security and to apply the proceeds from the collateral to the claims of all the lenders?

As lenders are not the direct beneficiaries of collateral agreements, should the lenders unilaterally file a lawsuit in Brazil to enforce the security interests created thereunder, it could be alleged that, by not being direct beneficiary under the collateral agreements, such party does not have legitimacy (*legitimidade*) to file a lawsuit and, if such allegation prevails, the lenders would not be able to enforce their security interest in courts on a unilateral basis; however, we understand that there are good arguments to sustain that the onshore collateral agent (trustee) has legitimacy (*legitimidade*) to represent the lenders, and any successor in lawsuits against the borrower and the guarantor, if the onshore collateral agent (trustee) is appointed as such by the lenders in the financing document governed by a foreign law.

5.2 If an agent or trustee is not recognised in your jurisdiction, is an alternative mechanism available to achieve the effect referred to above which would allow one party to enforce claims on behalf of all the lenders so that individual lenders do not need to enforce their security separately?

Please refer to the answer to question 5.1 above.

5.3 Assume a loan is made to a company organised under the laws of your jurisdiction and guaranteed by a guarantor organised under the laws of your jurisdiction. If such loan is transferred by Lender A to Lender B, are there any special requirements necessary to make the loan and guarantee enforceable by Lender B?

Unless there is an express prohibition in the loan agreement, credit assignments are valid under the laws of Brazil so long as the debtor is notified of the assignment. Generally, the collateral agreement is deemed as an ancillary obligation of the loan agreement (main obligation), which means that when the latter is assigned, the former is assigned too. From a practical perspective, it is advisable to amend both the loan agreement and respective collateral document with the names of the new debtor/guarantor to simplify the enforcement and avoid disputes on formal issues. Please note that, if a debt of a Brazilian company in relation to a foreign lender is assigned, in order to allow the remittance of funds to the new creditor, the registration of such debt before the Brazilian Central Bank must be updated.

6 Withholding, Stamp and Other Taxes; Notarial and Other Costs

6.1 Are there any requirements to deduct or withhold tax from (a) interest payable on loans made to domestic or foreign lenders, or (b) the proceeds of a claim under a guarantee or the proceeds of enforcing security?

(a) Interest payable by a Brazilian debtor to a foreign lender is generally subject to the withholding of income tax at a rate of 15% or 25% if the creditor is located in a blacklisted low-tax jurisdictions as defined in the applicable regulations. Interest payable by a Brazilian debtor to a local lender is also generally subject to the withholding of the income tax (not applicable to financial institutions) based on a regressive rates regime that vary from 22.5% to 15% according to the days elapsed since the loan was granted and the payment date. Note that, in this case, the tax withheld will be deemed a payment in advance of the corporate income tax locally due by the lender (at a general 34% rate for corporations and at a current 45% rate for financial institutions).

(b) The proceeds of a claim under a guarantee or enforcing security shall observe the same rules above, that is, the interest component paid by the lender would be subject to taxation, whereas principal should not be impacted by taxes. Other taxes may apply to either onshore and offshore loans transactions, although not under a withholding systematic.

6.2 What tax incentives or other incentives are provided preferentially to foreign lenders? What taxes apply to foreign lenders with respect to their loans, mortgages or other security documents, either for the purposes of effectiveness or registration?

One can highlight that cross-border loans whose proceeds are destined to the financing of Brazilian exports benefit from the 0% withholding income tax on interest. Offshore fundraising executed by means of the issuance of the so-called infrastructure debentures also benefit from the 0% rate of the withholding income tax, provided certain requirements are met. On top of that, certain tax treaties entered into by Brazil with other jurisdictions also provide a beneficial tax treatment for interest income paid out to foreign lenders.

Moreover, another tax advantage of foreign lender regards to the different treatment of the Tax on Financial Transactions in these cases. In effect, as a general rule, onshore loans with principal previously defined by the parties are impacted by the assessment of the Tax on Financial Transactions ("IOF/Credit"), which is generally levied at a daily 0.0041% rate, capped to 365 days, plus a flat 0.38%, thus leading to a combined 1.88% rate for transactions older than one year. On the other hand, cross-border loans whose average maturity term is set for a term longer than 181 days benefit from the 0% rate of the so-called IOF/FX – another modality of the Tax on Financial Transactions, which is triggered upon the execution of inbound/outbound FX transactions. However, the IOF/FX rate is increased to 6% if the loan average maturity term is lower than 181 days. Please note that FX transactions executed in connection with the payment of principal and interest by a Brazilian debt under a cross-border loan benefit from the 0% rate of the IOF/FX. Cross-border loans are not subject to the IOF/Credit.

6.3 Will any income of a foreign lender become taxable in your jurisdiction solely because of a loan to or guarantee and/or grant of security from a company in your jurisdiction?

As a general rule, no, since Brazilian tax rules concerning permanent establishments do not encompass cross-border lending transactions.

6.4 Will there be any other significant costs which would be incurred by foreign lenders in the grant of such loan/guarantee/security, such as notarial fees, etc.?

No. The tax impact to foreign lenders is generally limited to the withholding tax on income derived from the loans.

6.5 Are there any adverse consequences to a company that is a borrower (such as under thin capitalisation principles) if some or all of the lenders are organised under the laws of a jurisdiction other than your own? Please disregard withholding tax concerns for purposes of this question.

Under Brazilian tax regulations, certain tax constraints in respect to the tax-deductibility of interest expense at the level of the Brazilian debtor may apply, if the foreign lender is: (i) a related party to the Brazilian borrower; or (ii) located in a blacklisted (tax haven) or greylisted (privileged tax regime) low-tax jurisdiction. Such tax limitations mays apply due to (a) thin capitalisation, and (b) transfer pricing regulations.

Pursuant to current thin capitalisation rules, interest paid by sources located in Brazil to individuals or legal entities resident abroad will only be deductible for corporate tax purposes (IRPJ/CSL) if: (i) the debt with a related party (not located in a blacklisted jurisdiction) does not exceed two times the net equity of the Brazilian borrower (if the debt exceeds the threshold, the interest assessed on the excess amount will not be deductible); or (ii) the debts with entities located in a blacklisted jurisdiction does not exceed 30% (thirty per cent) of the net equity value of the legal entity resident in Brazil (if the debt exceeds the threshold, the interest assessed on the excess amount will not be deductible).

Cumulatively, one should also observe transfer pricing limits for the tax-deductibility expense arising from interest payments made to foreign lenders that are a related party to the borrower or located in black/greylisted jurisdictions. Under transfer pricing rules, depending on certain features of the relevant cross-border loan agreement, different tax-deductibility thresholds based on the interest of the contract shall apply: (i) for transactions denominated in US dollars at a fixed rate, the market rate for Brazilian government bonds issued in the foreign market, also in US dollars, will be adopted, plus a 3.5% spread; (ii) for transactions denominated in BRL at a fixed rate, the market rate for Brazilian government bonds issued in the foreign market in Brazilian Reais will be adopted, plus a 3.5% spread; and (iii) in other cases, the six-month LIBOR will be adopted, plus a 3.5% spread.

7 Judicial Enforcement

7.1 Will the courts in your jurisdiction recognise a governing law in a contract that is the law of another jurisdiction (a "foreign governing law")? Will courts in your jurisdiction enforce a contract that has a foreign governing law?

Yes, Brazilian courts would recognise a foreign governing law in an agreement, provided that such law does not offend Brazilian national sovereignty, public policy or good morals.

7.2 Will the courts in your jurisdiction recognise and enforce a judgment given against a company in New York courts or English courts (a "foreign judgment") without re-examination of the merits of the case?

If any final judgment of a court outside Brazil is rendered, such judgment would be recognised and enforced by the courts in Brazil without any retrial or re-examination of the merits of the original action, upon confirmation of that judgment by the Brazilian Superior Court of Justice (*Superior Tribunal de Justiça*). In order to be recognised by the Superior Court of Justice of Brazil, a foreign judgment must meet the following conditions: (i) it must comply with all formalities necessary for its enforcement under the laws of the jurisdiction where it was rendered; (ii) it must have been issued by a competent court after proper service of process on the parties, which service must comply with Brazilian Law if made in Brazil, or after sufficient evidence of the parties' absence has been given, as required by applicable law; (iii) it must be final and therefore not subject to appeal; (iv) it must not offend Brazilian national sovereignty, dignity of human being and/or public policy; (v) it must not violate a final and unappealable decision issued by a Brazilian court; (vi) it must not violate the exclusive jurisdiction of Brazilian courts; and (vii) it must be duly authenticated by the competent Brazilian consulate (except in case there is a bilateral agreement with the relevant country to waive such authentication by the Brazilian consulate or if apostilled in case the relevant country is signatory to the Hague Convention of 5 October 1961 Abolishing the Requirement of Legalisation for Foreign Public Documents and accompanied by a translation thereof into Portuguese, made by a certified translator in Brazil, except if waived by treaty.

7.3 Assuming a company is in payment default under a loan agreement or a guarantee agreement and has no legal defence to payment, approximately how long would it take for a foreign lender to (a) assuming the answer to question 7.1 is yes, file a suit against the company in a court in your jurisdiction, obtain a judgment, and enforce the judgment against the assets of the company, and (b) assuming the answer to question 7.2 is yes, enforce a foreign judgment in a court in your jurisdiction against the assets of the company?

In Brazil it is very difficult to predict how long it takes for a court to render a decision over a lawsuit, as it varies between each city and, even in the same court, varies between each judge; nevertheless, it possible to estimate that, on average, in case of (a) above, it would take between two and three years and, in case of (b) above, around two years.

7.4 With respect to enforcing collateral security, are there any significant restrictions which may impact the timing and value of enforcement, such as (a) a requirement for a public auction, or (b) regulatory consents?

As regards pledges and fiduciary sale/assignment, if the debtor defaults pursuant to the security documents or the main agreement, the trustee owner, security trustee or creditor should notify him of the delay (through a simple registered letter, by a registered letter issued by the Registry of Deeds and Documents or bill of protest) and may sell the assets to third parties, irrespective of public sale, auction or any other judicial or extrajudicial measure.

As regards mortgages, in case the debtor defaults under the debt, in the absence of an insolvency scenario, the foreclosure proceeding for mortgages shall be the following: (i) upon default, the debtor is summoned to pay the debt plus interest, monetary correction, court costs and attorneys' fees within the cure period determined by the relevant security agreement. If the debtor does not perform its payment obligations within said period, the attached property shall be foreclosed; (ii) the next step is the appraisal of the attached property; (iii) at this stage, creditor may opt for adjudication (i.e. judicially transferring the asset's property and possession to the creditor) of the property for the value of appraisal (if the appraisal amount is lower than debt amount, the creditor would still have an unsecured claim over the remaining amount); (iv) if the creditor does not opt for adjudication, the next step is the out-of-court sale; (v) the out-of-court sale shall take place through two public auctions: (a) in the 1st public auction, real estate property must be sold by at least its appraisal value; or (b) in the 2nd public auction, real estate property must be sold by at least a fair (non-vile) amount; (vi) if the property is not sold in the first and second auctions a new option of adjudication of the property by creditor may be determined (at the discretion of the court); and (vii) no "mutual release" event is verified in mortgage foreclosures. Thus, if upon the sale of the real estate property or its adjudication the debt amount is not totally repaid to the creditor, the creditor still has an unsecured claim against the debtor for the remaining amounts due under the credit transaction (and other guarantees may be foreclosed).

7.5 Do restrictions apply to foreign lenders in the event of (a) filing suit against a company in your jurisdiction, or (b) foreclosure on collateral security?

Any plaintiff not resident in Brazil will be required to place a bond as security for court costs and for third party attorneys' fees if it does not possess any real property in Brazil, except in case of collection claims based on an instrument that may be enforced in Brazilian courts without review of its merits (*título executivo extrajudicial*) or counterclaims.

7.6 Do the bankruptcy, reorganisation or similar laws in your jurisdiction provide for any kind of moratorium on enforcement of lender claims? If so, does the moratorium apply to the enforcement of collateral security?

Within the context of bankruptcy proceedings, there is an automatic stay which derives from the decision which actually declares the bankruptcy. In this sense, bankruptcy declaration stays the course for all judicial actions and enforcements against the guarantor. Accordingly, to the extent bankruptcy proceedings – in principle

– attach to all the guarantor's creditors, the secured party holding the collateral will be affected by the automatic stay of bankruptcy proceedings. In this scenario, the assets constituting the collateral will not be delivered to the secured party for payment of the secured debt. More significantly, the secured party will not be able to take any legal action to enforce and liquidate the collateral. The assets given in collateral will be gathered by the trustee for subsequent liquidation and payment of creditors that eventually hold a privilege or preference.

Within the context of judicial reorganisation proceedings, the automatic stay derives from the court decision that grants the processing of the judicial reorganisation application filed by the guarantor. Granting of the judicial reorganisation proceedings stays the course for all legal actions and enforcements proceedings against the guarantor related to all creditors subject to/affected by the judicial reorganisation proceedings. Under no circumstances can the automatic stay in judicial reorganisation proceedings exceed 180 days.

Within the context of extra-judicial reorganisation proceedings, the mere filing of such procedure does not entail the suspension of any court proceedings against the guarantor.

7.7 Will the courts in your jurisdiction recognise and enforce an arbitral award given against the company without re-examination of the merits?

Yes. Please refer to the answer to question 7.2.

8 Bankruptcy Proceedings

8.1 How does a bankruptcy proceeding in respect of a company affect the ability of a lender to enforce its rights as a secured party over the collateral security?

Under judicial reorganisation, upon the filing, the Court will eventually accept the filing and grant the processing order ("Processing Order"). As a result of the Processing Order, the debtor enjoys a stay period of 180 calendar days ("Stay Period"). During the Stay Period, all actions, enforcement and foreclosure proceedings against the debtor are generally stayed (or cannot be commenced). The Stay Period is designed to provide the debtor with breathing room to formulate, negotiate and eventually obtain creditors' support and approval of a Plan of Reorganisation. During the Stay Period, creditors holding collateral in the form of a fiduciary lien (a bankruptcy-remote collateral) are not entitled to remove the respective asset from the debtor's possession in case such asset is deemed to be essential to the debtor's activities.

Further, in case bankruptcy liquidation is adjudicated, as a rule all assets should be scheduled by the court-appointed trustee to be subsequently sold. Creditors holding securities in the form of a fiduciary lien should be entitled to remove the respective asset from the bankrupt estate through the filing of a claim for restitution, as the case may be.

8.2 Are there any preference periods, clawback rights or other preferential creditors' rights (e.g., tax debts, employees' claims) with respect to the security?

The Brazilian Bankruptcy Law ("BBL") regulates scenarios where antecedent transactions are deemed ineffective or voidable. Indeed, certain specific acts and contracts performed under a statutory period before the adjudication of the debtor's bankruptcy liquidation (*falência*) are considered ineffective. Further, acts performed with the intent to hinder or defraud creditors may also be declared null and void.

Section 129 of the BBL establishes that certain acts performed during a claw-back (look–back) period (*termo legal*) shall be declared ineffective in relation to the estate. The claw-back can generally retroactively apply up to 90 days prior to: (a) the filing of a bankruptcy liquidation (involuntary) request by the debtor's creditor; (b) the filing for court-protection under judicial reorganisation (in case judicial reorganisation has been subsequently converted into bankruptcy liquidation proceedings); or (c) outstanding protest of a debtor's title due to lack of payment.

Ineffectiveness declaration should apply regardless of whether the involved parties were aware of the financial condition of the debtor or had the intention to defraud creditors. The following actions (*inter alia*), if consummated during the claw-back period, shall be considered objectively ineffective: (i) payment of unmatured obligations (i.e. preferred payment); (ii) payment of matured obligations in a different manner than originally established by the parties in the relevant contracts; and (iii) creation of collateral (security) to secure an existing unsecured debt. The transfer of substantially all of a debtor's assets shall also be ineffective if consummated without consent or payment of all creditors existing at the time of the transfer.

In addition, transactions implemented before or after the debtor's bankruptcy liquidation adjudication (including the implementation of a security) may be revoked through the filing of a claw-back lawsuit (*ação recocatória*) if they were performed fraudulently, irrespective of whether they were committed during the claw-back period. Indeed, section 130 of the BBL establishes that acts performed with the intent to defraud creditors may be revoked, provided there is evidence of (i) fraudulent collusion between the debtor and the contracting third party, and (ii) actual loss suffered by the estate.

8.3 Are there any entities that are excluded from bankruptcy proceedings and, if so, what is the applicable legislation?

The BBL (which regulates bankruptcy liquidation proceedings) does not apply to government-owned entities, mixed-capital companies, public or private financial institutions, credit unions, consortia, supplementary pension companies, healthcare plan companies, insurance companies and special saving companies.

Financial institutions' insolvency (except federal institutions) is regulated by Law No. 6,024/74, which contemplates the intervention and extrajudicial liquidation regimes. Ultimately, both the intervention and extrajudicial liquidation may be converted to bankruptcy liquidation as regulated by the BBL, as the case may be.

Other regulated entities, such as healthcare plan companies and insurance companies, will follow insolvency proceedings as established before the respective regulatory framework, as applicable.

8.4 Are there any processes other than court proceedings that are available to a creditor to seize the assets of a company in an enforcement?

Although certain types of fiduciary lien collaterals may be foreclosed in an extra judicial basis, in a contested case a creditor should necessarily resort to in-court proceedings to seize and expropriate assets of the debtor in the context of an enforcement proceeding.

9 Jurisdiction and Waiver of Immunity

9.1 Is a party's submission to a foreign jurisdiction legally binding and enforceable under the laws of your jurisdiction?

The submission of a party to the non-exclusive jurisdiction of a foreign jurisdiction is legal, valid and binding under the laws of Brazil and will be accepted by the Brazilian courts, subject to certain assumptions and qualifications.

9.2 Is a party's waiver of sovereign immunity legally binding and enforceable under the laws of your jurisdiction?

Generally, no non-public owned entities have immunity from suit, proceedings, the enforcement of any judgment, any attachment or from any other legal process (whether on the grounds of sovereign immunity or otherwise) under Brazilian law in respect of their respective obligations under the pledge agreements.

10 Licensing

10.1 What are the licensing and other eligibility requirements in your jurisdiction for lenders to a company in your jurisdiction, if any? Are these licensing and eligibility requirements different for a "foreign" lender (i.e. a lender that is not located in your jurisdiction)? In connection with any such requirements, is a distinction made under the laws of your jurisdiction between a lender that is a bank *versus* a lender that is a non-bank? If there are such requirements in your jurisdiction, what are the consequences for a lender that has not satisfied such requirements but has nonetheless made a loan to a company in your jurisdiction? What are the licensing and other eligibility requirements in your jurisdiction for an agent under a syndicated facility for lenders to a company in your jurisdiction?

Any individual or legal entity may enter into a loan agreement subject to certain interest limitations in case the lender is not a financial entity under the supervision of the Central Bank. Therefore, only financial entities have the authorisation to extend loans without pre-defined limits on interest rates. It is a criminal offence in Brazil to carry out any activity that is reserved exclusively for financial institutions. Generally, no specific requirements apply for agents (*trustees*) in syndicated facilities.

Treatment for corporate lending activities under Brazilian law is different depending on whether the transactions are domestic or made offshore.

If the corporate lending transaction is entered into by a Brazilian counterparty with an offshore financial institution, such transactions (direct foreign loans) shall observe Law No. 4131, of September 3, 1962, Brazilian Monetary Council Resolution No. 3.844, of March 23, 2010, and Central Bank Circular No. 3.491, of March 24, 2010.

Such regulations expressly allow legal entities located in Brazil to contract loans with legal entities located abroad. In this case, the funds raised abroad by Brazilian entities should be necessarily invested in "economic activities", although the regulations have not defined such a concept. It is, however, generally understood that such funds obtained abroad should not be used for speculative purposes in Brazil.

Considering that, as long as the loan is contracted in accordance with the applicable regulation, it will not constitute the carrying on of the business of banking in Brazil, nor will it subject the lender (or any of its affiliates) to any oversight by the Brazilian regulatory authorities.

Apart from that mentioned herein, loan transactions do not require any approval from, or notice to, any Brazilian regulatory authority. However, it is important to mention that although no physical documents are involved in the Central Bank registration process, the Brazilian debtor shall keep the loan agreement (and guarantees, if any) in its files for five years as from the date when the loan is granted.

11 Other Matters

11.1 Are there any other material considerations which should be taken into account by lenders when participating in financings in your jurisdiction?

There are no further considerations that need to be mentioned.

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British Virgin Islands

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1 Overview

1.1 What are the main trends/significant developments in the lending markets in your jurisdiction?

The British Virgin Islands continues to be a jurisdiction of choice for corporate vehicles entering into secured finance transactions, and remains a markedly creditor-friendly jurisdiction. Recent amendments to the key corporate legislation, the BVI Business Companies Act (as amended) (the "**Act**") have enhanced the protection of secured creditors including on a continuation of the domicile of a BVI company out of the BVI and into another jurisdiction, and on a liquidation, where the liquidator now has an express statutory obligation to give effect to the rights and priority of the claims of the company's secured creditors. In line with commercial practice, the amendments to the Act have also provided greater flexibility and certainty for the execution of deeds, which from a practical perspective will assist virtual closings. The amendments to the Act also tightened record-keeping obligations on companies. The jurisdiction has implemented the OECD Common Reporting Standards.

1.2 What are some significant lending transactions that have taken place in your jurisdiction in recent years?

British Virgin Islands obligors continue to feature prominently in financed holding structures and joint ventures, notably: in the oil and gas and mining sectors; in development finance and infrastructure projects throughout Africa, Asia and Eastern Europe, CIS, Latin America and elsewhere; in high-end property developments in London; and in shipping, drillships and other asset finance facilities.

2 Guarantees

2.1 Can a company guarantee borrowings of one or more other members of its corporate group (see below for questions relating to fraudulent transfer/financial assistance)?

The giving of a guarantee by a British Virgin Islands company is governed by the Act, and the company's memorandum and articles of association. Subject to its memorandum and articles of association, the powers of a company include (among other things) the power to guarantee a liability or obligation of any person and secure any obligations by mortgage, pledge or other charge of any of its assets for that purpose.

2.2 Are there enforceability or other concerns (such as director liability) if only a disproportionately small (or no) benefit to the guaranteeing/securing company can be shown?

Under the Act, and subject to its memorandum and articles of association, a company has, irrespective of corporate benefit, full capacity to carry on or undertake any business or activity, do any act or enter any transaction and, for those purposes, full rights, powers and privileges.

The directors of a company have fiduciary and statutory duties to act honestly and in good faith and in the best interests of the company. A director who is in breach of his duties may be liable to the company for the resulting loss to the company.

In the event that there is a disproportionately small (or no) benefit to the company, the transaction may be open to challenge, for example, as a transaction at an undervalue, in the event of the insolvency of the company (see below).

2.3 Is lack of corporate power an issue?

Under the Act, no act of a company and no transfer of an asset by or to a company is invalid by reason only of the fact the company did not have the capacity, right or power to perform the act or to transfer or receive the asset.

It should be noted that members' remedies have been codified in the Act, and, for example, if a company or a director of a company engages in, proposes to engage in, or has engaged in conduct that contravenes the Act or the memorandum or articles of the company, the British Virgin Islands court may, on the application of a member or a director of the company, make an order directing the company or director to comply with, or restraining the company or director from engaging in conduct that contravenes the Act or the memorandum or articles.

2.4 Are any governmental or other consents or filings, or other formalities (such as shareholder approval), required?

It is not necessary to ensure the legality, validity, enforceability or admissibility in evidence of a guarantee that any document be filed, recorded or enrolled with any governmental authority or agency or any official body in the British Virgin Islands. Shareholder approval would be required only in the event the company's memorandum and articles of association require it.

2.5 Are net worth, solvency or similar limitations imposed on the amount of a guarantee?

To the extent that, under the applicable governing law, the guarantee is characterised as a debt incurred on behalf of a member of the company, it may be deemed to be a distribution and accordingly be subject to the requirement of the directors to determine that the company will pass the basic solvency test immediately after the deemed distribution. Under the solvency test, the company's assets must exceed its liabilities and the company must be able to pay its debts as they fall due. For former International Business Companies that still have a share capital, the requirements for satisfying the solvency test differ.

2.6 Are there any exchange control or similar obstacles to enforcement of a guarantee?

There is no exchange control legislation under British Virgin Islands law and accordingly there are no exchange control regulations imposed under British Virgin Islands law.

3 Collateral Security

3.1 What types of collateral are available to secure lending obligations?

There are no limits under British Virgin Islands law on the types of collateral that a company may give.

3.2 Is it possible to give asset security by means of a general security agreement or is an agreement required in relation to each type of asset? Briefly, what is the procedure?

A company may enter into a general security agreement such as a debenture.

3.3 Can collateral security be taken over real property (land), plant, machinery and equipment? Briefly, what is the procedure?

It should be noted that assets would typically be held outside the British Virgin Islands and collateral instruments would typically be governed by a governing law relevant to the jurisdiction in which the asset is sited. In the event that the company holds an interest in real estate or other assets physically located in the British Virgin Islands, there are certain licensing, registration and stamp duty considerations.

3.4 Can collateral security be taken over receivables? Briefly, what is the procedure? Are debtors required to be notified of the security?

British Virgin Islands law does not make statutory provision for an assignment by way of security. An assignment of receivables governed by British Virgin Islands law would require the written agreement of the debtor in order to take effect as a legal assignment, failing which the assignee would likely take an equitable assignment only.

3.5 Can collateral security be taken over cash deposited in bank accounts? Briefly, what is the procedure?

A company may give security over cash held in its bank accounts in any jurisdiction. British Virgin Islands law does not make statutory provision for collateral security over cash deposited in bank accounts located in the British Virgin Islands, and the cooperation of the account holding branch would be required.

3.6 Can collateral security be taken over shares in companies incorporated in your jurisdiction? Are the shares in certificated form? Can such security validly be granted under a New York or English law governed document? Briefly, what is the procedure?

Collateral security may be taken over shares in companies incorporated in the British Virgin Islands and this is a popular and frequently used type of security. Such security can validly be granted under a foreign law-governed document, and New York or English law-governed security is common. In the case of an English law-governed document, the application of the Financial Collateral Arrangements (No 2) Regulations 2003 to shares in a British Virgin Islands company has been confirmed by the Privy Council in *Cukurova Finance International Limited and Cukurova Holdings A.S (Appellants) v Alfa Telecom Turkey Ltd (Respondent)* [2013] UKPC 2. Shares are in registered form and share security is typically taken by way of an equitable mortgage. The Act provides a mechanism for particulars of a charge over shares to be noted on the register of members, a copy of which the company may file publicly at the Registry of Corporate Affairs in order for a person carrying out a company search to be on notice of the equitable security. The Act now enables a chargee to enforce immediately upon an event of default. The Act also provides for the powers of the chargee or a receiver which may be modified or supplemented by the security instrument.

3.7 Can security be taken over inventory? Briefly, what is the procedure?

A company may give security over inventory. The applicable procedure would be driven by the jurisdiction in which the inventory is located.

3.8 Can a company grant a security interest in order to secure its obligations (i) as a borrower under a credit facility, and (ii) as a guarantor of the obligations of other borrowers and/or guarantors of obligations under a credit facility (see below for questions relating to the giving of guarantees and financial assistance)?

Subject to its memorandum and articles of association, a company may grant a security interest to secure its obligations as a borrower, or the obligations of others.

3.9 What are the notarisation, registration, stamp duty and other fees (whether related to property value or otherwise) in relation to security over different types of assets?

No steps are required as a matter of British Virgin Islands law to perfect a security interest where assets are not located in the British Virgin Islands. It is a requirement of the Act that a company keep a register of all relevant charges created by the company, either at the company's registered office, or at the office of the company's registered agent. For the purposes of priority, an application may be made to the Registrar to register the charges created, providing an advantage to secured creditors that is not available in some offshore jurisdictions. Subject to such registration, and any prior security interests registered on the applicable register, the security interest will, as a matter of British Virgin Islands law, have priority over any claims by third parties (other than those preferred by law) including any liquidator or a creditor of the company, subject in the case of a winding up of the company in a jurisdiction other than the British Virgin Islands to any provisions of the laws of that jurisdiction as to priority of claims in a winding up. A floating charge will rank behind a subsequently registered fixed charge unless the floating charge contains a prohibition or restriction on the power of the company to create any future security interest ranking ahead in priority to or equally with the floating charge.

No taxes, fees or charges (including stamp duty) are payable (either by direct assessment or withholding) to the government or other taxing authority in the British Virgin Islands under the laws of the British Virgin Islands in respect of the execution or delivery, or the enforcement, of security documentation. In the event that the company holds an interest in real estate or other assets physically located in the British Virgin Islands, there are certain perfection, licensing, registration and stamp duty considerations.

3.10 Do the filing, notification or registration requirements in relation to security over different types of assets involve a significant amount of time or expense?

The Registry of Corporate Affairs fee for registering a register of charges is US$200. A small amount of time will be required for the preparation of the particulars of the registration.

3.11 Are any regulatory or similar consents required with respect to the creation of security?

No, they are not.

3.12 If the borrowings to be secured are under a revolving credit facility, are there any special priority or other concerns?

No, there are not.

3.13 Are there particular documentary or execution requirements (notarisation, execution under power of attorney, counterparts, deeds)?

No, there are not.

4 Financial Assistance

4.1 Are there prohibitions or restrictions on the ability of a company to guarantee and/or give security to support borrowings incurred to finance or refinance the direct or indirect acquisition of: (a) shares of the company; (b) shares of any company which directly or indirectly owns shares in the company; or (c) shares in a sister subsidiary?

(a) Shares of the company

Subject to its memorandum or articles, the powers of a company include the power to give financial assistance to any person in connection with the acquisition of its own shares.

(b) Shares of any company which directly or indirectly owns shares in the company

There are no restrictions on the giving of financial assistance to any person in connection with the acquisition of shares of any company which directly or indirectly owns shares in the company.

(c) Shares in a sister subsidiary

There are no restrictions on the giving of financial assistance to any person in connection with the acquisition of shares in a sister subsidiary.

5 Syndicated Lending/Agency/Trustee/Transfers

5.1 Will your jurisdiction recognise the role of an agent or trustee and allow the agent or trustee (rather than each lender acting separately) to enforce the loan documentation and collateral security and to apply the proceeds from the collateral to the claims of all the lenders?

The British Virgin Islands courts will recognise the role of an agent or trustee and allow the agent or trustee (rather than each lender acting separately) to enforce the loan documentation and collateral security and to apply the proceeds from the collateral to the claims of all the lenders, where that is provided for pursuant to the provisions of the applicable security documentation.

5.2 If an agent or trustee is not recognised in your jurisdiction, is an alternative mechanism available to achieve the effect referred to above which would allow one party to enforce claims on behalf of all the lenders so that individual lenders do not need to enforce their security separately?

This is not necessary in the British Virgin Islands.

5.3 Assume a loan is made to a company organised under the laws of your jurisdiction and guaranteed by a guarantor organised under the laws of your jurisdiction. If such loan is transferred by Lender A to Lender B, are there any special requirements necessary to make the loan and guarantee enforceable by Lender B?

This would be dependent on the applicable governing laws of the loan and the assignment documentation. British Virgin Islands law does not make statutory provision for the assignment of intangibles. An assignment of receivables governed by British Virgin Islands law would require the written agreement of the debtor in order to take effect as a legal assignment, failing which the assignee would likely take an equitable assignment only. A deed of novation would more typically be used to transfer a loan governed by British Virgin Islands law.

6 Withholding, Stamp and Other Taxes; Notarial and Other Costs

6.1 Are there any requirements to deduct or withhold tax from (a) interest payable on loans made to domestic or foreign lenders, or (b) the proceeds of a claim under a guarantee or the proceeds of enforcing security?

No taxes are required to be deducted or withheld under the laws of the British Virgin Islands from (a) interest payable on loans made to domestic or foreign lenders, or (b) the proceeds of a claim under a guarantee or the proceeds of enforcing security. The British Virgin Islands complies with the EU Taxation of Savings Directive through the automatic exchange of information on savings income with tax authorities in EU Member States.

6.2 What tax incentives or other incentives are provided preferentially to foreign lenders? What taxes apply to foreign lenders with respect to their loans, mortgages or other security documents, either for the purposes of effectiveness or registration?

No taxes are payable to the government or other taxing authority in the British Virgin Islands under the laws of the British Virgin Islands in respect of the execution or delivery, or the enforcement, of security documentation. In the event that the company holds an interest in real estate or other assets physically located in the British Virgin Islands, there are certain perfection, licensing, registration and stamp duty considerations.

6.3 Will any income of a foreign lender become taxable in your jurisdiction solely because of a loan to or guarantee and/or grant of security from a company in your jurisdiction?

No income of a foreign lender will become taxable in the British Virgin Islands solely because of a loan to, or guarantee and/or grant of security from, a company in the British Virgin Islands.

6.4 Will there be any other significant costs which would be incurred by foreign lenders in the grant of such loan/guarantee/security, such as notarial fees, etc.?

There are no significant costs such as notarial fees which would be incurred by foreign lenders in a loan to or guarantee and/or grant of security from a company in the British Virgin Islands.

6.5 Are there any adverse consequences to a company that is a borrower (such as under thin capitalisation principles) if some or all of the lenders are organised under the laws of a jurisdiction other than your own? Please disregard withholding tax concerns for purposes of this question.

No, there are not.

7 Judicial Enforcement

7.1 Will the courts in your jurisdiction recognise a governing law in a contract that is the law of another jurisdiction (a "foreign governing law")? Will courts in your jurisdiction enforce a contract that has a foreign governing law?

The British Virgin Islands courts will recognise a governing law that is the law of another jurisdiction, subject to the considerations applicable generally to choice of law provisions.

The British Virgin Islands courts may decline to exercise jurisdiction in relation to substantive proceedings brought under or in relation to a contract that has a foreign governing law in matters where they determine that such proceedings may be tried in a more appropriate forum.

7.2 Will the courts in your jurisdiction recognise and enforce a judgment given against a company in New York courts or English courts (a "foreign judgment") without re-examination of the merits of the case?

Any final and conclusive monetary judgment obtained against a company in the courts of England and Wales, for a definite sum, may be registered and enforced as a judgment of the British Virgin Islands court if application is made for registration of the judgment within 12 months or such longer period as the court may allow, and if the British Virgin Islands court considers it just and convenient that the judgment be so enforced. Alternatively, the judgment may be treated as a cause of action in itself so that no retrial of the issues would be necessary. In either case, it will be necessary that in respect of the foreign judgment:

(a) the foreign court issuing the judgment had jurisdiction in the matter and the judgment debtor either submitted to such jurisdiction or was resident or carrying on business within such jurisdiction and was duly served with process;

(b) the judgment given by the foreign court was not in respect of penalties, taxes, fines or similar fiscal or revenue obligations of the company;

(c) in obtaining judgment there was no fraud on the part of the person in whose favour judgment was given, or on the part of the foreign court;

(d) recognition or enforcement of the judgment in the British Virgin Islands would not be contrary to public policy;

(e) the proceedings pursuant to which judgment was obtained were not contrary to natural justice; and

(f) the judgment given by the foreign court is not the subject of an appeal.

Any final and conclusive monetary judgment obtained against a company in the courts of New York, for a definite sum, may be treated by the British Virgin Islands courts as a cause of action in itself so that no retrial of the issues would be necessary, provided that in respect of the foreign judgment:

(a) the foreign court issuing the judgment had jurisdiction in the matter and the company either submitted to such jurisdiction or was resident or carrying on business within such jurisdiction and was duly served with process;

(b) the judgment given by the foreign court was not in respect of penalties, taxes, fines or similar fiscal or revenue obligations of the company;

(c) there was no fraud on the part of the person in whose favour judgment was given or on the part of the court, in obtaining judgment;

(d) recognition or enforcement of the judgment in the British Virgin Islands would not be contrary to public policy; and

(e) the proceedings pursuant to which judgment was obtained were not contrary to natural justice.

7.3 Assuming a company is in payment default under a loan agreement or a guarantee agreement and has no legal defence to payment, approximately how long would it take for a foreign lender to (a) assuming the answer to question 7.1 is yes, file a suit against the company in a court in your jurisdiction, obtain a judgment, and enforce the judgment against the assets of the company, and (b) assuming the answer to question 7.2 is yes, enforce a foreign judgment in a court in your jurisdiction against the assets of the company?

There is no set timetable for such proceedings, and the time involved will depend on the nature of the enforcement proceedings (for example, an application to appoint liquidators on the ground of insolvency may be quicker than an action of judgment on the debt claim). If there is no defence to the claim and it is unopposed, judgment may be obtained in proceedings against a British Virgin Islands company in approximately one month from the commencement of proceedings. If the proceedings are defended, then the time involved will depend upon the facts and circumstances of the case. Broadly, the same considerations apply to an application to enforce a foreign judgment in the British Virgin Islands.

7.4 With respect to enforcing collateral security, are there any significant restrictions which may impact the timing and value of enforcement, such as (a) a requirement for a public auction, or (b) regulatory consents?

No, there are not.

7.5 Do restrictions apply to foreign lenders in the event of (a) filing suit against a company in your jurisdiction, or (b) foreclosure on collateral security?

There are no restrictions applicable to foreign lenders.

7.6 Do the bankruptcy, reorganisation or similar laws in your jurisdiction provide for any kind of moratorium on enforcement of lender claims? If so, does the moratorium apply to the enforcement of collateral security?

The appointment of liquidators against a company under the BVI Insolvency Act, 2003 (as amended) (the "**Insolvency Act**") brings about a moratorium on claims against the company, but this does not prevent the enforcement of security.

7.7 Will the courts in your jurisdiction recognise and enforce an arbitral award given against the company without re-examination of the merits?

Under the Arbitration Act 2013, the United Kingdom and British Virgin Islands arbitral awards will now be treated in the British Virgin Islands as New York Convention awards. The British Virgin Islands is a party to the New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards 1958 (the "**Convention**"). A court in the British Virgin Islands is required by law to enforce, without re-examination of the merits of the case or re-litigation of the matters arbitrated upon, a Convention award. However, enforcement of a Convention award may be refused if the person against whom it is invoked proves:

(a) that a party to the arbitration agreement was, under the law applicable to him, under some incapacity;

(b) that the arbitration agreement was not valid under the law to which the parties subjected it or, failing any indication thereon, under the law of the country where the award was made;

(c) that he was not given proper notice of the appointment of the arbitrator or of the arbitration proceedings or was otherwise unable to present his case;

(d) that the award deals with a difference not contemplated by or not falling within the terms of the submission to arbitration or contains decisions on matters beyond the scope of the submission to arbitration;

(e) that the composition of the arbitral authority or the arbitral procedure was not in accordance with the agreement of the parties or failing such agreement, with the law of the country where the arbitration took place; or

(f) that the award has not yet become binding on the parties, or has been set aside or suspended by a competent authority of the country in which, or under the law of which, it was made.

Enforcement of a Convention award may also be refused if the award is in respect of a matter which is not capable of settlement by arbitration under the laws of the British Virgin Islands, or if it would be contrary to public policy to enforce the award.

A Convention award which contains decisions on matters not submitted to arbitration may be enforced to the extent that it contains decisions on matters submitted to arbitration which can be separated from those on matters not so submitted.

8 Bankruptcy Proceedings

8.1 How does a bankruptcy proceeding in respect of a company affect the ability of a lender to enforce its rights as a secured party over the collateral security?

Security over the assets of a company in liquidation may be enforced by the chargee directly over those assets, which fall outside the custody and control of the liquidator.

8.2 Are there any preference periods, clawback rights or other preferential creditors' rights (e.g., tax debts, employees' claims) with respect to the security?

In the event of the insolvency of a company, there are four types of voidable transaction provided for in the Insolvency Act:

1. Unfair Preferences: Under section 245 of the Insolvency Act, a transaction entered into by a company, if it is entered into within the hardening period (see below) at a time when the company is insolvent, or it causes the company to become insolvent (an "**insolvency transaction**"), and which has the effect of putting the creditor into a position which, in the event of the company going into insolvent liquidation, will be better than the position it would have been in if the transaction had not been entered into, will be deemed an unfair preference. A transaction is not an unfair preference if the transaction took place in the ordinary course of business. It should be noted that this provision applies regardless of whether the payment or transfer is made for value or at an undervalue.
2. Undervalue Transactions: Under section 246 of the Insolvency Act, the making of a gift or the entering into of a transaction on terms that the company is to receive no consideration, or where the value of the consideration for the transaction, in money or money's worth, is significantly less than the value, in money or money's worth, of the consideration provided by the company will (if it is an insolvency transaction entered into within the hardening period) be deemed an undervalue transaction. A company does not enter into a transaction at an undervalue if it is entered into in good faith and for the purposes of its business and, at the time the transaction was entered into, there were reasonable grounds for believing the transaction would benefit the company.
3. Voidable Floating Charges: Under section 247 of the Insolvency Act a floating charge created by a company is voidable if it is an insolvency transaction created within the hardening period. A floating charge is not voidable to the extent that it secures:

   (a) money advanced or paid to the company, or at its direction, at the same time as, or after, the creation of the charge;

(b) the amount of any liability of the company discharged or reduced at the same time as, or after, the creation of the charge;

(c) the value of assets sold or supplied, or services supplied, to the company at the same time as, or after, the creation of the charge; and

(d) the interest, if any, payable on the amount referred to in (a) to (c) pursuant to any agreement under which the money was advanced or paid, the liability was discharged or reduced, the assets were sold or supplied or the services were supplied.

4. Extortionate Credit Transactions: Under section 248 of the Insolvency Act, an insolvency transaction entered into by a company for, or involving the provision of, credit to the company, may be regarded as an extortionate credit transaction if, having regard to the risk accepted by the person providing the credit, the terms of the transaction are or were such to require grossly exorbitant payments to be made in respect of the provision of the credit, or the transaction otherwise grossly contravenes ordinary principles of fair trading and such transaction takes place within the hardening period.

The hardening period (known in the Insolvency Act as the vulnerability period) in respect of each voidable transaction provision set out above is as follows:

(a) for the purposes of sections 245, 246 and 247 of the Insolvency Act, the period differs depending on whether the person(s) that the transaction is entered into with, or the preference is given to, are connected persons of the company within the meaning of the Insolvency Act. In the case of connected persons, the hardening period is the period beginning two years prior to the onset of insolvency (see below) and ending on the appointment of a liquidator of the company. In the case of any other person, the hardening period is the period beginning six months prior to the onset of insolvency and ending on the appointment of a liquidator of the company; and

(b) for the purposes of section 248 of the Insolvency Act, the hardening period is the period beginning five years prior to the onset of insolvency and ending on the appointment of a liquidator of the company regardless of whether the person(s) that the transaction is entered into with is a connected person.

The onset of insolvency for these purposes is the date on which an application for the appointment of a liquidator was filed (if the liquidator was appointed by the Court) or the date of the appointment of the liquidator (where the liquidator was appointed by the members).

A conveyance made by a person with intent to defraud creditors is voidable at the instance of the person thereby prejudiced. There is no requirement that the relevant transaction was entered into at a time when one party was insolvent or became insolvent as a result of the transaction, and there is no requirement that the transferring party subsequently went into liquidation. However, no conveyance entered into for valuable consideration and in good faith to a person who did not have notice of the intention to defraud may be impugned.

There are limited preferential creditors under British Virgin Islands law.

8.3 Are there any entities that are excluded from bankruptcy proceedings and, if so, what is the applicable legislation?

Certain sovereign entities and treaty-based organisations are protected. For example, the State Immunity (Overseas Territories) Order 1979 extended the State Immunity Act 1978 to the British Virgin Islands, and the International Finance Corporation Order 1955 extends to the British Virgin Islands.

8.4 Are there any processes other than court proceedings that are available to a creditor to seize the assets of a company in an enforcement?

Enforcement of a charge over the shares in a British Virgin Islands company could be effected without recourse to the courts, where the necessary documentation has been provided by the chargor, the issuer company and the registered agent prior to the date of enforcement. As stated above, the remedy of appropriation that may be contained in an English law-governed share charge has been upheld by the Privy Council as applicable to shares in a British Virgin Islands company.

9 Jurisdiction and Waiver of Immunity

9.1 Is a party's submission to a foreign jurisdiction legally binding and enforceable under the laws of your jurisdiction?

The British Virgin Islands courts will recognise that a foreign jurisdiction may be the more appropriate forum for enforcement.

9.2 Is a party's waiver of sovereign immunity legally binding and enforceable under the laws of your jurisdiction?

A relevant entity may waive immunity pursuant to the State Immunity Act 1978.

10 Licensing

10.1 What are the licensing and other eligibility requirements in your jurisdiction for lenders to a company in your jurisdiction, if any? Are these licensing and eligibility requirements different for a "foreign" lender (i.e. a lender that is not located in your jurisdiction)? In connection with any such requirements, is a distinction made under the laws of your jurisdiction between a lender that is a bank *versus* a lender that is a non-bank? If there are such requirements in your jurisdiction, what are the consequences for a lender that has not satisfied such requirements but has nonetheless made a loan to a company in your jurisdiction? What are the licensing and other eligibility requirements in your jurisdiction for an agent under a syndicated facility for lenders to a company in your jurisdiction?

Assuming that the lender is not doing business in the British Virgin Islands, it will not be caught by the regulatory legislation, or requirements for licensing, in the jurisdiction. Significantly, business is not carried on "in the British Virgin Islands" by a lender by reason only of it being carried on with a company or limited partnership incorporated or registered in the British Virgin Islands.

A "foreign" lender, which does not carry on business in the British Virgin Islands, would not be required to be licensed in order to lend to a British Virgin Islands company.

There is no distinction between a lender that is a bank *versus* a lender that is a non-bank.

In the unlikely event that, based on the facts of a specific scenario, a foreign lender is found to be carrying on business in the British Virgin Islands without holding the requisite licence, the loan may be unenforceable by the lender.

As above, assuming that the agent is not conducting business in the British Virgin Islands, there are no licensing and eligibility requirements for an agent under a syndicated facility.

11 Other Matters

11.1 Are there any other material considerations which should be taken into account by lenders when participating in financings in your jurisdiction?

The British Virgin Islands is a dependable common law jurisdiction, and other attractions for lenders not mentioned above include, for example, the statutory recognition of netting, set off and subordination arrangements, and the ability for a creditor to restore a dissolved company where it is just to do so.

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Canada

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1 Overview

1.1 What are the main trends/significant developments in the lending markets in your jurisdiction?

Canadian banks have been widely recognised internationally as well-capitalised, well-managed and well-regulated, and a major contributing force in the Canadian economy. The lending market in Canada is characterised by a wide range of domestic banks, pension funds, credit unions and insurance companies, as well as major foreign banks and finance companies, offering a range of commercial lending services and financial products on par with those offered anywhere else in the world.

In recent years, there has been increasing growth of the private debt investor market in Canada. A number of newer non-bank funds and institutions have become active in mid-market leveraged lending and other lines of business. These opportunities have arisen in large part due to the increased regulatory burden and capital requirements faced by banks following the financial crisis. With continued active participation by Canadian banks as well as foreign lenders, and the increasing presence of non-bank lending funds, the Canadian lending market remains very competitive and lending margins remain tight.

Fintech lending also continues to grow in the Canadian market. At present the regulation of fintech in Canada is generally fragmented and siloed. No single central authority regulates the wide variety of functions associated with fintech. In general, regulation is entity-based rather than function-based and is split between federal and provincial jurisdictions. Federal law covers banking and anti-money laundering, while provincial law governs such matters as securities, consumer protection and privacy. Both federal and provincial authorities are working towards developing more unified fintech strategies and are experimenting with such innovations as the regulatory sandbox to ease the regulatory burden for startups.

1.2 What are some significant lending transactions that have taken place in your jurisdiction in recent years?

One of the largest and most complex finance transactions in recent years was the restructuring of Pacific Exploration & Production Corporation, which involved, among other things, the conversion of approximately $5.4 billion of existing indebtedness into equity. Cross-border lending into Canada, particularly from the United States, remains active in 2017, including the financing of the acquisition of Trader Corporation, Canada's largest digital automotive marketplace and software solutions provider to automobile dealers, valued at approximated $1.6 billion. Lending in the public-private partnership (P3) space continues to gain momentum, especially as more provinces and municipalities are turning to the P3 model for funding their infrastructure projects.

2 Guarantees

2.1 Can a company guarantee borrowings of one or more other members of its corporate group (see below for questions relating to fraudulent transfer/financial assistance)?

Yes, it can.

2.2 Are there enforceability or other concerns (such as director liability) if only a disproportionately small (or no) benefit to the guaranteeing/securing company can be shown?

In some circumstances, the enforceability of a guarantee could be challenged by stakeholders on the basis that it was granted in a manner that was oppressive, unfairly prejudicial or that unfairly disregards the interest of creditors or minority shareholders under the oppression provisions of applicable corporate legislation. A guarantee could also be subject to challenge under provisions of applicable insolvency legislation dealing with transactions at under value or preference claims. Directors and officers would only be subject to personal liability in such cases if specific facts were pleaded to justify such a remedy (e.g. wrongdoing).

2.3 Is lack of corporate power an issue?

If the guarantor is a corporation, it must have the corporate power and capacity to give guarantees. Most business corporations have the powers and capacity of a natural person and it is unusual to see restrictions on the power to issue guarantees in the guarantor's constating documents. However, certain corporations created by statute for a public purpose (such as school boards) may still be subject to the doctrine of *ultra vires* and therefore may require express legislative authority to give guarantees.

2.4 Are any governmental or other consents or filings, or other formalities (such as shareholder approval), required?

Other than typical corporate authorising resolutions, no formal approvals are generally required. Where a corporation provides financial assistance by way of guarantee or otherwise, in some provinces the corporation is required to disclose the financial assistance to its shareholders after such assistance is given.

2.5 Are net worth, solvency or similar limitations imposed on the amount of a guarantee?

Not for corporations incorporated federally or under the laws of most provinces. However, the corporate laws in a few Atlantic Provinces and in two territories continue to prohibit financial assistance to members of an intercompany group if there are reasonable grounds to believe that the corporation would be unable to meet prescribed solvency tests after giving the assistance, subject to specific exceptions.

2.6 Are there any exchange control or similar obstacles to enforcement of a guarantee?

No; subject to the provisions of applicable Canadian federal money laundering and anti-terrorism legislation.

3 Collateral Security

3.1 What types of collateral are available to secure lending obligations?

Most types of personal property and real property are available to secure lending obligations, subject to certain limitations by contract (e.g. contractual restrictions on assignment) or by law (e.g. government receivables, permits, licences and quotas).

Provincial legislation generally governs the creation and enforcement of security. All Canadian provinces (except Québec) have adopted comprehensive personal property security acts (PPSAs) conceptually similar to Article 9 of the United States *Uniform Commercial Code* (UCC). The PPSAs govern the creation, perfection and enforcement of security interests in a debtor's personal property, and create a scheme for determining the priority of competing interests in the same collateral. The PPSAs apply to any transaction that in substance creates a security interest in personal property, regardless of the form of document used to grant the interest.

Québec, Canada's only civil law jurisdiction, has a European style Civil Code (the *Civil Code of Québec*) that governs the creation and enforcement of security on movable (personal) and immovable (real) property.

Certain types of property continue to be subject to additional federal registration and filing regimes (examples include intellectual property and assets in shipping, aircraft and railways). The federal *Bank Act* also has a special security regime available as an option available only to federally chartered banks for certain classes of debtors and collateral.

3.2 Is it possible to give asset security by means of a general security agreement or is an agreement required in relation to each type of asset? Briefly, what is the procedure?

A general security agreement (GSA) can be and often is used to grant security over all of the debtor's present and after-acquired personal property of every type and description. Separate agreements are not required for each type of asset. The GSA or other security agreement must contain a description of the collateral sufficient to enable it to be identified. However, a GSA typically does not extend to real property and separate requirements apply to registration and documentation of security against land, as described under question 3.3 below.

In most cases, the secured party perfects the security interest by registering a financing statement under the PPSA filing regime in the applicable province. Where the financing statement should be registered depends on the type of collateral. In general, security interests in most tangible personal property are registered in the province in which the collateral is located at the time of attachment. Security interests in most intangibles and certain types of goods normally used in more than one jurisdiction must be registered in the province in which the debtor is deemed to be located under the relevant debtor location rules. Except in Ontario, a debtor with multiple places of business is deemed to be located at its "chief executive office". Under amendments to Ontario's PPSA that came into force on December 31, 2015, most debtors are deemed to be located in the jurisdictions in which they were incorporated or organised, similar to the more generally applicable debtor location rules under Article 9 of the UCC.

The hypothec, Québec's only form of consensual security, may be granted by a debtor to secure any obligation, and may create a charge on existing and after-acquired movable (personal) or immovable (real) property, although there are certain additional formalities that must be met when taking security on immovable (real) property. It may be made with or without delivery, allowing the grantor of the hypothec to retain certain rights to use the property. In most cases a hypothec must be published (registered) in Québec's Register of Personal and Movable Real Rights in accordance with applicable formalities in order to enable it to be set up against third parties (i.e., perfected).

3.3 Can collateral security be taken over real property (land), plant, machinery and equipment? Briefly, what is the procedure?

A lender may take collateral security over land or real property by way of a mortgage of the land, a mortgage of lease, a debenture, or, if the real property charged is in Québec, an immovable deed of hypothec. Interests in real property are registered in the land registry system of the relevant province. In Québec, the immovable hypothec is usually registered by a Québec notary in accordance with applicable formalities.

It should be noted that a higher rate of interest on amounts in arrears secured by a real property mortgage may be unenforceable under the *Interest Act* (Canada).

The procedure for taking security over plant, machinery and equipment that constitutes personal property under the PPSA or movables under the *Civil Code of Québec* is described in question 3.2 above.

Personal property may include "fixtures" (goods that become affixed to real property), but if the security interest has not attached prior to affixation, the creditors registered against the land gain priority, with limited exceptions. What constitutes a fixture is a factual question and the common law has taken a contextual approach. To protect the priority of its interest in a fixture, a secured party must both 1) perfect its security interest under the PPSA, and 2) register its interest in the land registry system. Under the *Civil Code of Québec*, the rules for determining what constitutes movable or immovable property are different – but the end results are comparable.

3.4 Can collateral security be taken over receivables? Briefly, what is the procedure? Are debtors required to be notified of the security?

Yes. The procedure for taking security over receivables is the same as described in question 3.2 above.

Notice to account debtors is not required to create a perfected security interest in accounts receivable under the PPSA. However, account debtors for the receivables are obligated to pay the receivable directly to the secured party only after receiving notice from the secured party that the receivable has been assigned to it. In addition, an absolute assignment of receivables constitutes a "security interest" regardless of whether it secures any obligations.

Under the *Civil Code of Québec*, if assigned receivables constitute a "universality of claims", the assignment must be registered for such assignment to be set up against third parties (i.e. perfected). However, account debtors must still be notified of such assignment before an account debtor is obligated to pay the receivable directly to the secured party. If the receivables do not constitute a universality of claims, the assignment may be perfected with respect to Québec obligors only by actual notice of the assignment to such obligors.

Under Canadian federal legislation, subject to prescribed exceptions, receivables owed by the federal government can be assigned only absolutely (not as security) and only with appropriate notice to the appropriate official of the government of Canada, which must be acknowledged. Some provinces have similar legislation covering receivables owed by the provincial government. In Canada, asset-based lenders frequently exclude government receivables from the borrowing base.

3.5 Can collateral security be taken over cash deposited in bank accounts? Briefly, what is the procedure?

The PPSA and *Civil Code of Québec* permit a lender to take security over deposit accounts. Under the PPSA, deposits in bank accounts are treated as "accounts" or receivables owed by the depository bank to the depositor and under the *Civil Code of Québec* as claims against the bank. Accordingly, in PPSA jurisdictions, security interests in deposit accounts are perfected by registering a financing statement in the province where the debtor is deemed to be located under the applicable debtor location rules (see question 3.2 above). Traditionally, a bank lender that maintained deposit accounts for its debtor and wished to take security in such accounts would do so by way of set off and a "flawed asset" approach. However, in light of recent Canadian case law that poses a risk of recharacterisation, the lender should also register a PPSA financing statement against the debtor.

No PPSA jurisdiction has yet adopted control as a means of perfecting security interests in deposit accounts. However, as of January 1, 2016, certain amendments to the *Civil Code of Québec* came into force whereby it is now possible to perfect hypothecs over cash deposits in bank accounts (referred to as monetary claims) by "control". Where the creditor is also the account bank, the creditor obtains control by the debtor (i.e. the account holder) consenting to such monetary claims securing performance of its obligations to the creditor. Where the creditor is not the account bank, the creditor obtains control by either: (i) entering into a control agreement with the account bank and the debtor, pursuant to which the account bank agrees to comply with the creditor's instructions, without the additional consent of the debtor; or (ii) becoming the account holder.

3.6 Can collateral security be taken over shares in companies incorporated in your jurisdiction? Are the shares in certificated form? Can such security validly be granted under a New York or English law governed document? Briefly, what is the procedure?

A security interest in shares issued by companies incorporated in any jurisdiction is typically documented by way of a standalone pledge agreement or included in a general security agreement. While the jurisdiction governing validity, perfection or non-perfection of the pledge will be determined under applicable conflict of laws rules, the security interest may be granted under a document governed by New York or English law, subject to the principles discussed in question 7.1 below.

Under the PPSA and the *Securities Transfer Act, 2006* (STA), versions of which are in force in most Canadian PPSA jurisdictions (harmonised legislation is in force in Québec), a secured party can perfect its security interest in shares by registering under the PPSA or by taking control under the STA (or both). An interest perfected by control has priority over one perfected only by registration or simple delivery of the unendorsed share certificates.

Shares may be either certificated or uncertificated. For certificated shares, taking physical possession of the share certificates, together with a suitable endorsement (which can be on a separate instrument such as a stock power of attorney), meets the STA requirement for control. For uncertificated shares, control is obtained by being registered as the shareholder or through a control agreement with the issuer. Control over securities held indirectly through securities accounts can be achieved by other means (for example, a control agreement with the relevant intermediary).

It should also be noted that under securities legislation, a private company's constating documents must include a restriction on the right to transfer its shares. This restriction usually states that each transfer of the company's shares requires approval by the company's directors or shareholders.

3.7 Can security be taken over inventory? Briefly, what is the procedure?

Yes. The procedure is generally the same as described in question 3.2.

The security interest may be perfected by registering a financing statement in the province or territory in which the inventory is situated at the time the security interest attaches, except that inventory of a type normally used in more than one jurisdiction that is leased or held for lease by the debtor to others requires registration in the province in which the debtor is deemed to be located.

The purchase of inventory is often financed by way of a purchase money security interest (or PMSI). A PMSI in collateral is, in substance, a security interest given by either the seller or a third party to finance the purchase of the collateral by the debtor. The PPSA provides that a PMSI in inventory and other types of collateral (other than investment property or its proceeds) has priority over any other security interest in the same collateral given by the same debtor (even if that other security interest was registered first) so long as certain timing and (and, in the case of inventory) third party notice requirements are satisfied. The *Civil Code of Québec* does not offer a comparable approach and subordination or cession of rank is required from any prior ranking secured creditor.

3.8 Can a company grant a security interest in order to secure its obligations (i) as a borrower under a credit facility, and (ii) as a guarantor of the obligations of other borrowers and/or guarantors of obligations under a credit facility (see below for questions relating to the giving of guarantees and financial assistance)?

Yes, it can.

3.9 What are the notarisation, registration, stamp duty and other fees (whether related to property value or otherwise) in relation to security over different types of assets?

Registration fees are payable in connection with the filing of PPSA financing statements, increasing with the length of the registration period. These are relatively modest – for example, in Ontario it is $8.00 for each year of the registration period or $500 for a perpetual registration.

A modest tax is payable upon registering real property security in certain Canadian jurisdictions. The tax is based on a fee and where the face amount of the registration exceeds the value of the lands, one is permitted to pay on the basis of a percentage of the property value.

No Canadian jurisdiction imposes stamp taxes or duties in relation to security. In Québec, if a notarial deed of hypothec is used, the notary will generally charge a fee for execution, keeping it in its notarial records and for issuing copies; however, there is no additional material cost.

3.10 Do the filing, notification or registration requirements in relation to security over different types of assets involve a significant amount of time or expense?

The registration requirements in most cases are relatively straightforward and inexpensive. As noted above in question 3.7, a PMSI in inventory requires prior notice to certain secured parties in order to ensure priority.

3.11 Are any regulatory or similar consents required with respect to the creation of security?

For certain special types of regulated property, consents or approvals may be required by governmental authorities or agencies for both the creation and enforcement of security. Governmental licences, permits and quotas are subject to specific regimes requiring notice or consent in many cases. See question 3.4 regarding government receivables.

3.12 If the borrowings to be secured are under a revolving credit facility, are there any special priority or other concerns?

A security interest and hypothec in personal property or movable property may secure both present and future advances under a revolving credit facility. Where future advances are made while a security interest is perfected, the security interest has the same priority with respect to each future advance as it has with respect to the first advance, with certain limited exceptions in favour of unsecured execution and other creditors that seize the collateral if the secured party makes the advance after receiving notice of their interests. A security interest in personal property is not automatically discharged by reason of the fact that the outstanding balance under a revolving line of credit has been paid down to zero and subsequently re-advanced.

Generally, advances on a real property mortgage made without actual notice of a subsequent claim will typically have priority over such subsequent claims and, accordingly, mortgages securing revolving credit normally provide that subsequent liens are prohibited. Certain priority exceptions apply such as in respect of construction liens. Real property mortgages securing revolving credit should be properly worded to address situations where the borrowing is fully or partially repaid and thereafter re-advanced.

3.13 Are there particular documentary or execution requirements (notarisation, execution under power of attorney, counterparts, deeds)?

In Québec, security over immovable property or in favour of a collateral agent on behalf of multiple secured parties (referred to as "hypothecary representative") requires execution of the deed of hypothec before an authorised Québec notary.

Each province has different requirements with respect to real property, including specific registration forms, evidence of corporate authority, affidavits and, in some jurisdictions, originals for registration.

4 Financial Assistance

4.1 Are there prohibitions or restrictions on the ability of a company to guarantee and/or give security to support borrowings incurred to finance or refinance the direct or indirect acquisition of: (a) shares of the company; (b) shares of any company which directly or indirectly owns shares in the company; or (c) shares in a sister subsidiary?

Most Canadian corporations are not subject to such restrictions, except those created under the laws of a few Atlantic Provinces (New Brunswick, Prince Edward Island and Newfoundland) and certain territories (the Northwest Territories and Nunavut). Certain provinces (Alberta, British Columbia, Ontario and Saskatchewan) require that financial assistance be disclosed to shareholders, but failure to disclose does not invalidate the transaction.

5 Syndicated Lending/Agency/Trustee/Transfers

5.1 Will your jurisdiction recognise the role of an agent or trustee and allow the agent or trustee (rather than each lender acting separately) to enforce the loan documentation and collateral security and to apply the proceeds from the collateral to the claims of all the lenders?

Yes. The agency concept is recognised in Canadian common law and agents are commonly used in syndicated lending for both administration of loans and holding collateral security in Canada. Indenture trustees are typically used in public bond transactions.

5.2 If an agent or trustee is not recognised in your jurisdiction, is an alternative mechanism available to achieve the effect referred to above which would allow one party to enforce claims on behalf of all the lenders so that individual lenders do not need to enforce their security separately?

For purposes of holding collateral security in the province of Québec, the mechanism commonly used requires the appointment of the collateral agent as a "hypothecary representative", together with a notarial deed of hypothec in favour of such hypothecary representative.

5.3 Assume a loan is made to a company organised under the laws of your jurisdiction and guaranteed by a guarantor organised under the laws of your jurisdiction. If such loan is transferred by Lender A to Lender B, are there any special requirements necessary to make the loan and guarantee enforceable by Lender B?

Assignments of debt, guarantees and security can be effected by contract pursuant to a standard assignment and assumption agreement. Where the assignor is also the secured party of record (whether as collateral agent or otherwise), PPSA financing statements (and the Québec equivalent) are typically amended to record the assignment, although such amendments are not required for enforceability (except in Québec). Mortgage or security assignments are required to be filed under the applicable land registry to give effect to the assignment. In the case of Québec, where the security is in favour of the hypothecary representative and there is a substitution of hypothecary representative (as a result of the assignment or otherwise), the new hypothecary representative cannot exercise recourse under the hypothec until such substitution is registered where applicable.

6 Withholding, Stamp and Other Taxes; Notarial and Other Costs

6.1 Are there any requirements to deduct or withhold tax from (a) interest payable on loans made to domestic or foreign lenders, or (b) the proceeds of a claim under a guarantee or the proceeds of enforcing security?

There are generally no requirements to deduct or withhold tax on payments of interest by a debtor or guarantor (whether by voluntary payment, enforcement or otherwise) made to domestic lenders.

Conventional interest payments made to arm's length lenders that are non-residents of Canada are generally not subject to Canadian withholding tax, regardless of their country of residence. In addition, conventional interest payments made to certain non-arm's length US resident lenders may qualify for an exemption from Canadian withholding tax under the Canada-US Tax Treaty.

Certain interest payments made in respect of back-to-back loans, including loans between related parties, which are channelled through an independent third-party intermediary, may be subject to Canadian withholding tax.

In the absence of any applicable exemptions under treaties or under the *Income Tax Act* (Canada), withholding tax on interest payments may apply at rates of up to 25%.

6.2 What tax incentives or other incentives are provided preferentially to foreign lenders? What taxes apply to foreign lenders with respect to their loans, mortgages or other security documents, either for the purposes of effectiveness or registration?

Generally, there are no material tax or other incentives provided preferentially to foreign investors or creditors and no taxes apply to security documents for the purposes of effectiveness or registration.

6.3 Will any income of a foreign lender become taxable in your jurisdiction solely because of a loan to or guarantee and/or grant of security from a company in your jurisdiction?

While each lender's tax position must be examined individually, generally the non-resident lender's income should not be taxable in Canada solely because of a single secured loan transaction in the absence of a fixed presence in Canada or other connecting factors.

6.4 Will there be any other significant costs which would be incurred by foreign lenders in the grant of such loan/guarantee/security, such as notarial fees, etc.?

(See questions 3.9 and 3.10 for a discussion of the filing and notarial fees.) There are no stamp taxes, registration taxes or documentary taxes that are generally applicable in connection with authorisation, delivery or performance of loans, guarantees or security.

6.5 Are there any adverse consequences to a company that is a borrower (such as under thin capitalisation principles) if some or all of the lenders are organised under the laws of a jurisdiction other than your own? Please disregard withholding tax concerns for purposes of this question.

Thin capitalisation rules under the *Income Tax Act* (Canada) determine whether a Canadian corporation may deduct interest on the amount borrowed from a "specified non-resident shareholder" of the corporation or from a non-resident person who does not deal at arm's length with a "specified shareholder" (collectively "specified non-residents"). A "specified shareholder" of a corporation is, in general terms, a person who, either alone or together with persons with whom they do not deal at arm's length, owns 25% or more of the voting shares, or the fair market value of the issued and outstanding shares of the corporation.

Under the thin capitalisation rules, Canadian corporations are effectively prevented from deducting interest on the portion of loans from specified non-residents that exceeds one-and-a-half times the corporation's specified equity (in highly simplified terms, retained earnings, share capital and contributed surplus attributable to specified non-residents). In addition, any interest expenses that are disallowed under these rules are deemed to be dividends paid to the lender for non-resident withholding tax purposes, and subject to withholding tax.

In addition, the thin capitalisation rules may apply in respect of interest paid or payable on back-to-back loans. However, most traditional forms of commercial collateralisation or guarantees should not attract the application of these rules, especially where any loans made by the third-party are clearly made from the third party's own sources.

The thin capitalisation rules also apply (with appropriate modifications) to (i) Canadian resident trusts, (ii) non-resident corporations or trusts that carry on business in Canada (in respect of loans that are used in the course of that Canadian business), and (iii) partnerships in which a Canadian resident corporation or trust or a non-resident corporation or trust is a member.

7 Judicial Enforcement

7.1 Will the courts in your jurisdiction recognise a governing law in a contract that is the law of another jurisdiction (a "foreign governing law")? Will courts in your jurisdiction enforce a contract that has a foreign governing law?

Subject to certain exceptions and conditions, Canadian courts will recognise and apply the parties' choice of governing law if it is specifically pleaded and proven by expert testimony.

Canadian courts will not apply the foreign law if the choice of law is not *bona fide* or is contrary to public policy or if so doing would be considered enforcement of foreign revenue, or expropriatory or penal law. Additionally, Canadian courts will apply Canadian procedural law and certain provincial and federal laws that have overriding effect, such as bankruptcy and insolvency statutes, federal crime legislation, employment legislation and consumer protection legislation.

7.2 Will the courts in your jurisdiction recognise and enforce a judgment given against a company in New York courts or English courts (a "foreign judgment") without re-examination of the merits of the case?

A foreign monetary judgment may be enforced in Canada if the judgment is final and the foreign court properly assumed jurisdiction. As long as these requirements are met, a Canadian court will not examine whether the foreign court correctly applied its own substantive and procedural laws.

In considering the issue of jurisdiction, Canadian courts will apply their own principles of jurisdiction. Generally a contractual submission to the jurisdiction of the foreign court will be sufficient, but in the absence of such submission, the Canadian court will examine whether there was a "real and substantial connection" between the foreign court and the cause of action or the defendant. While the test is often applied generously and flexibly by the courts, a fleeting or relatively unimportant connection will not support a foreign court's assumption of jurisdiction.

There are certain limited defences which preclude recognition related to circumstances under which the foreign judgment was obtained (such as by fraud or in a manner breaching principles of natural justice) and whether there is any reason it would be improper or contrary to public policy to recognise the foreign judgment. In practice, these defences rarely succeed.

7.3 Assuming a company is in payment default under a loan agreement or a guarantee agreement and has no legal defence to payment, approximately how long would it take for a foreign lender to (a) assuming the answer to question 7.1 is yes, file a suit against the company in a court in your jurisdiction, obtain a judgment, and enforce the judgment against the assets of the company, and (b) assuming the answer to question 7.2 is yes, enforce a foreign judgment in a court in your jurisdiction against the assets of the company?

(a) In Ontario, if no defence is filed in response to a claim, default judgment may be obtained between 20 and 60 days after the claim has been served on the defendant, depending on where service is effected. After any judgment is obtained, and subject to it being stayed by the filing of a notice of appeal, enforcement proceedings may be commenced immediately.

(b) An application hearing to enforce a foreign judgment in Ontario may generally be obtained within approximately two to three months.

Procedural and substantive law differs by province, but the timing described above is similar in most other provinces.

7.4 With respect to enforcing collateral security, are there any significant restrictions which may impact the timing and value of enforcement, such as (a) a requirement for a public auction, or (b) regulatory consents?

A secured creditor must give the debtor reasonable time to pay following demand, before taking action to enforce against its collateral security (even if the debtor purported to waive these rights).

Where a secured creditor intends to enforce security over substantially all of an insolvent debtor's inventory, accounts receivable or other property used in relation to the debtor's business, in addition to delivering a demand, the secured creditor must also deliver a notice of intention to enforce security in the form prescribed under the *Bankruptcy and Insolvency Act* (BIA) at least 10 days before such enforcement, unless the debtor consents to an earlier enforcement. A slightly longer notice period may be required if collateral is located in the Province of Québec.

If a secured creditor intends to deal with the collateral itself or through a privately appointed receiver (where applicable), it must also give advance notice to the debtor and other interested parties of its intention to dispose of the collateral or accept the collateral as final settlement of the debtor's obligations. This notice period is typically 15–20 days depending on the applicable PPSA and can run concurrently with the BIA enforcement notice.

Although there is no requirement for a public auction, a secured creditor (and any receiver) must act in good faith and in a commercially reasonable manner when selling or otherwise disposing of the collateral. However, if a lender wishes to buy the collateral, it may only do so at a public sale, unless otherwise permitted by a court. Generally speaking, no regulatory consents are required to enforce on collateral security.

7.5 Do restrictions apply to foreign lenders in the event of (a) filing suit against a company in your jurisdiction, or (b) foreclosure on collateral security?

To maintain an action in certain provinces, foreign lenders may be required to become extra-provincially registered.

There are no specific restrictions on a foreign lender's ability to enforce security in Canada. However, if the lender chooses to exercise those remedies to either foreclose on the collateral security or to credit-bid its debt, such that the foreign lender ends up owning the debtor's Canadian assets, the foreign lender may be subject to restrictions imposed by the *Investment Canada Act* or the *Competition Act*.

7.6 Do the bankruptcy, reorganisation or similar laws in your jurisdiction provide for any kind of moratorium on enforcement of lender claims? If so, does the moratorium apply to the enforcement of collateral security?

Yes, a stay of proceedings may affect the rights of secured and unsecured creditors in some circumstances to the extent set out in question 8.1.

7.7 Will the courts in your jurisdiction recognise and enforce an arbitral award given against the company without re-examination of the merits?

Provincial arbitration acts provide for the enforcement of arbitral awards by application to the court. Canadian courts will not re-examine the merits of an arbitral award; however, the award may be set aside on specified grounds including, but not limited to, an invalid arbitration agreement, an award outside of the jurisdiction of the arbitrator, or a reasonable apprehension of bias on the part of the arbitrator.

The Convention on the Recognition and Enforcement of Foreign Arbitral Awards and the *UNCITRAL Model Law on International Commercial Arbitration* have been adopted in all Canadian provinces and provide rules for the enforcement of international arbitral awards. Subject to limited grounds on which enforcement of an international arbitral award may be refused, the awards are generally enforceable in Canada.

8 Bankruptcy Proceedings

8.1 How does a bankruptcy proceeding in respect of a company affect the ability of a lender to enforce its rights as a secured party over the collateral security?

Bankruptcy and insolvency in Canada are primarily governed by two federal statutes: the BIA; and the *Companies' Creditors Arrangement Act* (CCAA). The BIA provides a comprehensive liquidation scheme for companies and individuals, along with a streamlined reorganisation regime. The CCAA is Canada's large company reorganisation statute. Although some aspects of creditors' rights are determined by provincial statutes, bankruptcy and insolvency law is mostly uniform across Canada. Insolvency proceedings under the BIA or CCAA will result in the imposition of a stay of proceedings either by a Canadian court or pursuant to the relevant statute.

Under the BIA liquidation proceedings, the automatic stay of proceedings imposed upon commencement will not prevent a secured creditor from realising or otherwise dealing with its collateral. By contrast, in a court-appointed receivership (an alternative form of liquidation proceeding governed by the BIA), receivership orders routinely contain language staying the actions of secured creditors.

If a debtor files a notice of intention to make a proposal (NOI) or a proposal to creditors under the BIA (a reorganisation proceeding), a secured creditor's enforcement rights will be automatically stayed during the reorganisation proceeding, unless: (i) the secured creditor took possession of the collateral before the filing; (ii) the secured creditor delivered its BIA enforcement notice more than 10 days prior to the filing of the NOI; or (iii) the debtor consents to the secured creditor exercising its enforcement rights.

Reorganisation proceedings under the CCAA are commenced when an initial order is granted by the court. The CCAA explicitly empowers a court to grant a stay of proceedings against the debtor on any terms that it may impose. The stay provision in the CCAA initial order typically prohibits secured creditors from enforcing their security interests against the debtor's property during the proceeding.

8.2 Are there any preference periods, clawback rights or other preferential creditors' rights (e.g., tax debts, employees' claims) with respect to the security?

(a) Avoidance actions

Under the BIA and the CCAA, certain transactions, including the granting of security, the transfer of property and other obligations are voidable if incurred during specified pre-bankruptcy time periods. Subject to certain conditions and exemptions, if such transactions are made with a view to giving one creditor a preference over others, they may be set aside if entered into during the period that is: (i) three months before the initial bankruptcy event for transactions at arm's length; and (ii) one year before the initial bankruptcy event for transactions not at arm's length.

Transfers of property (or services sold), in which the consideration the debtor receives is less than the fair market value, subject to certain other conditions and exemptions, may be set aside under the BIA or CCAA if entered into during the period that is (i) one year before the initial bankruptcy event for transactions at arm's length, and (ii) five years before the initial bankruptcy event for transactions not at arm's length.

There is also provincial legislation providing for setting aside other fraudulent conveyances or preferential transactions.

(b) Statutory priority claims

In Canada, a number of statutory claims may "prime" or take priority over a secured creditor. Priming liens commonly arise from a debtor's obligation to remit amounts collected or withheld on behalf of the government. Such amounts include unremitted employee deductions for income tax, government pension plan contributions, government employment insurance premiums and unremitted federal goods and services taxes, provincial sales taxes, municipal taxes and workers' compensation assessments. In Ontario, statutory deemed trusts may give rise to a priority claim for certain unpaid claims of employees, including, in some circumstances, a deemed trust arising upon wind-up of a defined benefit pension plan for any deficiency amounts. In addition, there are a number of statutes that create priming liens in specific industries (for example, repair and storage liens, construction liens and brokerage liens). These priming liens may attach to all of the property of the debtor. In some cases, the priority of statutory claimants and secured creditors is sometimes reversed by the commencement of an insolvency proceeding against the debtor.

(c) Priority claims – insolvency

An insolvency proceeding in respect of the debtor may give rise to a number of additional liens that would rank in priority to a secured creditor's claims.

The BIA provides employees of a bankrupt employer or an employer in receivership with a priority charge on the employer's "current assets" for unpaid wages and vacation pay (but not for severance or termination pay) for the six-month period prior to bankruptcy or receivership to a maximum of $2,000 per employee (plus up to $1,000 for certain travelling expenses). The priority charge ranks ahead of all other claims, including secured claims, except unpaid supplier rights.

The BIA also grants a priority charge in bankruptcies and receiverships for outstanding current service pension plan contributions, subject only to the wage earners' priority. The pension contribution priority extends to all assets, not just current assets, and is unlimited in amount.

The pension charge secures (i) amounts deducted as pension contributions from employee wages but not contributed to the plan prior to a bankruptcy or receivership, and (ii) amounts required to be contributed by the employer to a pension plan for "normal costs". The charge does not extend to unfunded deficits arising upon a wind-up of a defined benefit plan and should not include scheduled catch-up or special payments required to be made by an employer because of the existence of a solvency deficiency.

The CCAA and the reorganisation provisions of the BIA expressly prohibit a court from sanctioning a proposal, compromise or arrangement or a sale of assets, unless it is satisfied that the debtor has arranged to pay an amount equal to the amounts secured by the wage and pension priority charges discussed above.

(d) Priority claims – court charges

In CCAA and BIA reorganisations, debtors may obtain interim financing (often referred to as debtor in possession (DIP) financing). Both the CCAA and the BIA expressly authorise the court to grant fresh security over a debtor's assets to DIP lenders in priority to existing security interests up to a specified amount approved by the court.

In addition to the priming liens noted above, in a CCAA or BIA reorganisation, the court has the authority to order priming charges to secure payment of directors' post-filing liabilities and to secure the fees and disbursements of experts, court-appointed officials and certain other "interested parties" in the court's discretion. The court may also order priming charges to secure payment to designated "critical suppliers", typically restricted to securing payment for post-filing supply.

The priority of the DIP charge, directors' charge, expense charge and any critical supplier charge in respect of the debtor's assets is determined by the court.

(e) Unpaid suppliers' rights

The BIA provides certain unpaid suppliers with a right to repossess goods sold and delivered to a purchaser within 30 days before the date of bankruptcy or receivership of such purchaser. The unpaid supplier's right to repossess goods effectively ranks ahead of a secured creditor.

An unpaid supplier claim is rarely successful as the supplier has the burden of demonstrating that all requirements have been met, including: (i) that the debtor has possession of the goods; (ii) that the goods are identifiable; (iii) that the goods are in the same state; and (iv) that the goods have not yet been sold.

8.3 Are there any entities that are excluded from bankruptcy proceedings and, if so, what is the applicable legislation?

Banks (including the Canadian business of foreign banks authorised to do business in Canada), insurance companies and trust corporations are excluded from the BIA and CCAA and their wind up is governed by the *Winding-Up and Restructuring Act* (Canada). The BIA and CCAA also exclude railway and telegraph companies. However, in a recent case a court granted a railway company relief under the CCAA.

8.4 Are there any processes other than court proceedings that are available to a creditor to seize the assets of a company in an enforcement?

Upon default, a secured creditor may exercise "self-help" remedies to take possession and control of collateral individually or through the appointment of a private receiver (if provided in its security documents). Secured creditors may also seek court appointment of an interim receiver to preserve and protect collateral on an expedited basis.

9 Jurisdiction and Waiver of Immunity

9.1 Is a party's submission to a foreign jurisdiction legally binding and enforceable under the laws of your jurisdiction?

The submission by a party to the non-exclusive jurisdiction of the courts of a foreign jurisdiction should be recognised as valid, provided that service of process requirements are complied with. The submission by a party to the exclusive jurisdiction of the courts of a foreign jurisdiction is generally recognised unless there is "strong cause" not to do so.

9.2 Is a party's waiver of sovereign immunity legally binding and enforceable under the laws of your jurisdiction?

The *State Immunity Act* (Canada) governs sovereign immunity of foreign states and any separate agency of a foreign state (e.g. state trading corporations). Private corporations that are not "organs" of a foreign state are not entitled to sovereign immunity.

Sovereign immunity may be waived if the state or agency submits to the jurisdiction of the Canadian court by agreement, either before or after commencement of the proceedings. Sovereign immunity is subject to certain exceptions (e.g. commercial activities and property damage actions, terrorist activities and certain maritime claims).

10 Licensing

10.1 What are the licensing and other eligibility requirements in your jurisdiction for lenders to a company in your jurisdiction, if any? Are these licensing and eligibility requirements different for a "foreign" lender (i.e. a lender that is not located in your jurisdiction)? In connection with any such requirements, is a distinction made under the laws of your jurisdiction between a lender that is a bank *versus* a lender that is a non-bank? If there are such requirements in your jurisdiction, what are the consequences for a lender that has not satisfied such requirements but has nonetheless made a loan to a company in your jurisdiction? What are the licensing and other eligibility requirements in your jurisdiction for an agent under a syndicated facility for lenders to a company in your jurisdiction?

There are no specific eligibility requirements for lenders solely as a result of entering into a secured lending transaction as lender or agent.

Under the *Bank Act* (Canada), a "foreign bank" is generally not permitted to engage in or carry on business in Canada except through a foreign bank subsidiary, an authorised foreign branch or other approved entity. A "foreign bank" is broadly defined in the Act and includes any foreign entity that (i) is a bank under the laws of a foreign country in which it carries on business or carries on business in a foreign country which would be considered the business of banking, (ii) provides financial services and uses the word "bank" in its name, (iii) is in the business of lending money and accepting deposit liabilities transferable by cheque or other instrument, (iv) provides financial services and is affiliated with a foreign bank, or (v) controls a foreign bank or a Canadian bank.

However, the *Bank Act* would not prohibit a foreign bank from making a loan to a Canadian borrower as long as the nature and extent of its activities in Canada do not amount to engaging in or carrying on business in Canada. Whether a foreign bank would be considered to be engaging in or carrying on business in Canada by reason of making a particular loan to a Canadian borrower will depend on the relevant facts and circumstances.

A non-bank lender may be required to obtain an extra-provincial licence in each province in which it is considered to be carrying on business under provincial corporate law. Such determination may vary somewhat in each province; however similar factors to those above will be relevant. A corporation which owns or leases real property in, or has an employee or agent that is resident in, such province will generally be considered to be carrying on business in that province.

In the case of either a bank or non-bank lender, a loan transaction involving a Canadian borrower would not be void or voidable by reason of such lender's failure to comply with applicable regulatory requirements in Canada.

11 Other Matters

11.1 Are there any other material considerations which should be taken into account by lenders when participating in financings in your jurisdiction?

The Criminal Code (Canada) makes it a criminal offence to receive interest at a criminal rate, defined as an effective annual rate of interest that exceeds 60%. Interest in the Criminal Code (Canada) is broadly defined to include interest, fees, fines, penalties, commission and similar charges and expenses that a borrower pays in connection with the credit advanced. This section has been considered almost exclusively in civil (not criminal) cases where the borrower seeks to avoid repayment by arguing that the contract was illegal. Courts have struggled with deciding which, if any, contractual provisions should be enforced when a contract imposes a criminal rate of interest.

Note

Please note that the answers in this chapter are up to date as of October 31, 2017. Readers are cautioned against making decisions based on this material alone. Rather, any proposal to do business in Canada should be discussed with qualified professional advisors.

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Cayman Islands

Maples and Calder

Tina Meigh

1 Overview

1.1 What are the main trends/significant developments in the lending markets in your jurisdiction?

The Cayman Islands continues to be a jurisdiction of choice for the establishment of investment funds, portfolio investment companies and corporate vehicles, each of which utilise secured lending arrangements in a variety of forms. We continue to see an increase in the use of subscription financing and hybrid facilities by investment funds and their Cayman Islands investment companies. We have also seen a sizeable increase in the use of Cayman Islands "orphan" vehicles to address US bankruptcy concerns of lenders. While the exempted company and limited partnership are each well recognised and utilised vehicles, entrenched in the market, the new limited liability company has also quickly become a favoured vehicle as a result of advantageous hybrid features taken from both the company and limited partnership regimes.

The Cayman Islands continues to be a very creditor-friendly jurisdiction and favoured by many lending houses and financial institutions for all secured lending transactions.

1.2 What are some significant lending transactions that have taken place in your jurisdiction in recent years?

The most significant lending transactions continue to occur in the investment funds space, especially to Cayman Islands domiciled private equity funds. These transactions tend to be governed by New York and English law finance documents with security taken over Cayman Islands assets being governed by both Cayman Islands law and non-Cayman Islands law. Although the courts in the Cayman Islands generally recognise foreign law documents, lenders often prefer, for commercial purposes, to have dual Cayman Islands law governed security.

The main types of security are, in the case of funds established in the form of exempted limited partnerships, security over capital calls (the right to call such capital and the right to receive the proceeds of such calls) and, more generally, security over Cayman Islands equity interests, either in the form of registered shares or exempted limited partnership interests. This is particularly common where there is a "master-feeder" structure or underlying blocker entities are used to hold assets and those structures are looking to utilised subscription and hybrid facilities.

2 Guarantees

2.1 Can a company guarantee borrowings of one or more other members of its corporate group (see below for questions relating to fraudulent transfer/financial assistance)?

Yes, a company can grant a guarantee in these circumstances assuming there is sufficient commercial rationale and benefit to the company.

2.2 Are there enforceability or other concerns (such as director liability) if only a disproportionately small (or no) benefit to the guaranteeing/securing company can be shown?

The directors of the company providing a guarantee must ensure that any proposed transaction is in the best interests of the company as a whole. Guarantee arrangements may be construed as not being in the best interests of a company (and not for the company's corporate benefit) if the granting company receives no commercial benefit from the underlying financing arrangements.

The directors of the company giving the guarantee should approve the terms and execution of the guarantee by way of board resolution in accordance with the company's articles of association. If there is any question of lack of corporate benefit or a potential breach of the director's duties, it is recommended that the company also obtain a shareholders' resolution approving the grant of the guarantee.

2.3 Is lack of corporate power an issue?

In accordance with the Companies Law (2016 Revision), the lack of capacity of a company to enter into a transaction by reason of anything in the company's memorandum will not affect the validity of the transaction. However, where the company is acting without the necessary capacity, shareholders may issue proceedings prohibiting the company from performing its obligations under the transaction (including disposing of any property) and proceedings may be brought against present and past directors or officers of the company for loss or damage caused by them binding the company in this manner contrary to the objects in the memorandum.

If a shareholder brings proceedings to restrict the company from performing its obligations, we believe such action would not affect the other party's rights under the transaction. If the company fails to perform, the other party would have the usual remedies.

2.4 Are any governmental or other consents or filings, or other formalities (such as shareholder approval), required?

Subject to any licensing restrictions that may apply to a regulated entity, no authorisations or consents are required by law from any governmental authorities or agencies or other official bodies in the Cayman Islands in connection with the grant of a guarantee. In addition, it is not necessary to ensure the enforceability or admissibility in evidence of a guarantee that any document be filed, recorded or enrolled with any governmental authority or agency or any official body in the Cayman Islands.

The directors of the company giving the guarantee should approve the terms and execution of the guarantee by way of board resolution in accordance with the company's articles of association. If there is any question of lack of corporate benefit or a potential breach of the director's duties, it is recommended that the company also obtain a shareholders' resolution approving the grant of the guarantee.

2.5 Are net worth, solvency or similar limitations imposed on the amount of a guarantee?

There are no legislative restrictions imposed on the amount of any guarantee due to net worth or the solvency of a company. However, the directors of a company should, as part of fulfilling their fiduciary duties, consider the terms of any guarantee, particularly in the context of the company's asset base.

2.6 Are there any exchange control or similar obstacles to enforcement of a guarantee?

There are no exchange control regulations imposed under Cayman Islands law that would act as an obstacle to enforcement of a guarantee.

3 Collateral Security

3.1 What types of collateral are available to secure lending obligations?

There are no legislative restrictions on the form of collateral and, accordingly, all property of a company is potentially available as security for lending obligations.

3.2 Is it possible to give asset security by means of a general security agreement or is an agreement required in relation to each type of asset? Briefly, what is the procedure?

It is possible for security to be taken by means of a general security agreement, such as a debenture, over a range of asset types. The main types of security under Cayman Islands law are mortgages (legal and equitable), charges (fixed and floating), liens and assignments of rights by way of security (albeit that this is deemed to be a form of mortgage). Formalities and perfection of such security interests will depend upon the nature of the underlying collateral and the applicable *lex situs* of such collateral.

Special regimes apply to the taking of security over certain assets, including ships, aircraft and land.

3.3 Can collateral security be taken over real property (land), plant, machinery and equipment? Briefly, what is the procedure?

Security over land is usually granted by way of legal or equitable mortgage and by way of fixed charge over plant, machinery and equipment. In relation to chattels, security can also be created by a conditional bill of sale which must be recorded in accordance with the Bills of Sale Law (2016 Revision).

A legal mortgage is granted by execution of a mortgage agreement between the mortgagor and the secured creditor. The terms of the mortgage will vary, but essentially a mortgage (i) requires transfer of legal title in the land to the secured creditor, subject to a requirement to re-transfer the land upon satisfaction of the underlying secured obligations, and (ii) grants the secured creditor certain powers to deal with the land upon a default.

An equitable mortgage can be created by (i) the execution of an equitable mortgage, (ii) an agreement to create a legal mortgage, (iii) a transfer of land which is not perfected by registering the secured creditor in the Land Registry in accordance with the Registered Lands Law, and (iv) the deposit of the relevant title deeds by way of security.

Fixed and floating charges are usually evidenced by an agreement between the parties reflecting the grant of the security interest and setting out the commercial terms.

A company must make an entry in its register of mortgages and charges in respect of any security interest created by it in order to comply with section 54 of the Companies Law (2016 Revision). An LLC must make an entry on its register of mortgages and charges in a similar manner to an exempted company incorporated or referenced under the Companies Law, in accordance with Section 62(1) of the LLC Law. However, failure to comply with these requirements does not invalidate the security interests created by either a company or LLC.

3.4 Can collateral security be taken over receivables? Briefly, what is the procedure? Are debtors required to be notified of the security?

Receivables arising under contract are examples of "choses in action", being a right which can only be asserted by bringing an action and not by taking possession of a physical thing. Receivables can be mortgaged or charged where that mortgage or charge takes the form of an assignment with an express or implied provision for reassignment on redemption. If a chose in action is charged, the charge can be either fixed or floating.

An assignment can be either legal or equitable, depending on the circumstances. The key requirements of a legal assignment are that it is: (i) an absolute assignment of the whole of a present (not future) chose in action; and (ii) the assignment must be both in writing and signed by the assignor and notified in writing to the debtor. An equitable assignment generally only relates to part of a chose in action and/or does not involve the notification of the debtor.

A company and LLC must make an entry in its register of mortgages and charges in respect of any security interest created by it. See question 3.3 above.

3.5 Can collateral security be taken over cash deposited in bank accounts? Briefly, what is the procedure?

A security interest over cash deposits is most commonly created by either a fixed or floating charge, depending on the commercial intention of the parties and the level of control maintained over such cash deposits. The secured creditor should ensure that there is an agreement (usually a deed). Cash deposits are classified as chose in action. Accordingly, the analysis in question 3.4 above applies.

In accordance with Cayman Islands conflict of law rules, the appropriate law to govern any security over cash deposited with a bank will be the law applicable where the bank is located (or the location of the bank branch with which the deposit is made).

3.6 Can collateral security be taken over shares in companies incorporated in your jurisdiction? Are the shares in certificated form? Can such security validly be granted under a New York or English law governed document? Briefly, what is the procedure?

Security over shares in Cayman Islands companies, where the register of members is maintained in the Cayman Islands, is usually taken in the form of a legal or equitable mortgage, depending on whether the secured party wishes to take legal title to the shares prior to a default of the secured obligation. Different rules may apply if the register of members is maintained outside of the Cayman Islands or if the shares are in bearer form.

In accordance with Cayman Islands conflict of law rules, the appropriate law to govern any security over registered shares in a Cayman Islands company is determined according to the law applicable to the location of the register of members. Whilst it is possible to grant security over shares as a matter of other laws, enforcement of such security may prove problematic or difficult.

It is not possible to pledge registered shares under Cayman Islands law because title to the shares cannot be transferred by physical delivery. Any grant of security over registered shares that is called a "pledge" will typically fall into one of the mortgage categories, depending on its terms, or it may be entirely ineffective.

3.7 Can security be taken over inventory? Briefly, what is the procedure?

Security can be taken over inventory or stock by way of a fixed or floating charge. A floating charge is more common given the changing nature of inventory in the usual course of a grantor's business.

3.8 Can a company grant a security interest in order to secure its obligations (i) as a borrower under a credit facility, and (ii) as a guarantor of the obligations of other borrowers and/or guarantors of obligations under a credit facility (see below for questions relating to the giving of guarantees and financial assistance)?

A company can grant a security interest in order to secure its obligations as a borrower under a credit facility or as a guarantor of the obligations of other parties (see Section 2). Usual fiduciary duties applicable to directors' actions will apply in each case.

3.9 What are the notarisation, registration, stamp duty and other fees (whether related to property value or otherwise) in relation to security over different types of assets?

No stamp duties or other similar taxes are payable, unless the applicable security document is executed in or brought into the Cayman Islands. The amount of any applicable stamp duty will vary depending on the type of security document and the identity of the assets subject to the security interest. Unless the document needs to be executed in the Cayman Islands, it is common practice to execute documents outside of the Cayman Islands so that stamp duty is not levied. Court fees (of a nominal value) will fall due as part of any enforcement process.

3.10 Do the filing, notification or registration requirements in relation to security over different types of assets involve a significant amount of time or expense?

A company must make an entry in its register of mortgages and charges in respect of any security interest created by it in order to comply with section 54 of the Companies Law (2016 Revision). An LLC must make an entry on its register of mortgages and charges in a similar manner to an exempted company incorporated or referenced under the Companies Law, in accordance with Section 62(1) of the LLC Law. This step is usually undertaken by the registered office service provider of the company or LLC and can be completed in a very short time period.

Charges over certain assets, such as land, intellectual property rights, ships and aircraft, need to be registered at other specialist registries related to the asset in question.

3.11 Are any regulatory or similar consents required with respect to the creation of security?

Subject to any licensing restrictions that may apply to a regulated entity, no authorisations or consents are required by law from any governmental authorities or agencies or other official bodies in the Cayman Islands in connection with the grant of a security interest.

The directors of the company (or manager, as the case may be) or of an LLC granting the security interest should approve the terms and execution of the security document by way of board resolution in accordance with the company's articles of association or LLC's limited liability company agreement. If there is any question of lack of corporate benefit or a potential breach of directors' duties, it is recommended that the company also obtain a shareholders' resolution approving the grant of the security interest.

3.12 If the borrowings to be secured are under a revolving credit facility, are there any special priority or other concerns?

There are no special priority concerns regarding a revolving credit facility.

3.13 Are there particular documentary or execution requirements (notarisation, execution under power of attorney, counterparts, deeds)?

A number of key documentation issues exist, each of which depend on the form of the security document, whether the document contains a power of attorney and if the document is to be executed by way of deed. The key issues of note are: (i) an agreement to create a legal mortgage over land should be executed and delivered as a deed; (ii) a legal assignment must be in writing and signed by both parties; (iii) any power of attorney or security document containing a power of attorney must be executed by way of a deed to ensure compliance with the Powers of Attorney Law (1996 Revision); and (iv) where a deed is required, the relevant execution formalities are set out in the Companies Law (2016 Revision) and the LLC Law.

4 Financial Assistance

4.1 Are there prohibitions or restrictions on the ability of a company to guarantee and/or give security to support borrowings incurred to finance or refinance the direct or indirect acquisition of: (a) shares of the company; (b) shares of any company which directly or indirectly owns shares in the company; or (c) shares in a sister subsidiary?

(a) Shares of the company

No, there are no legislative prohibitions or restrictions under Cayman Islands law equivalent to the English law financial assistance rule.

(b) Shares of any company which directly or indirectly owns shares in the company

No, there are no legislative prohibitions or restrictions under Cayman Islands law equivalent to the English law financial assistance rule.

(c) Shares in a sister subsidiary

No, there are no legislative prohibitions or restrictions under Cayman Islands law equivalent to the English law financial assistance rule.

5 Syndicated Lending/Agency/Trustee/Transfers

5.1 Will your jurisdiction recognise the role of an agent or trustee and allow the agent or trustee (rather than each lender acting separately) to enforce the loan documentation and collateral security and to apply the proceeds from the collateral to the claims of all the lenders?

Cayman Islands law recognises the role of an agent or trustee, acting on behalf of all lenders, assuming the transaction documents provide for the relevant trust mechanics and the trust is properly constituted.

5.2 If an agent or trustee is not recognised in your jurisdiction, is an alternative mechanism available to achieve the effect referred to above which would allow one party to enforce claims on behalf of all the lenders so that individual lenders do not need to enforce their security separately?

This is not applicable.

5.3 Assume a loan is made to a company organised under the laws of your jurisdiction and guaranteed by a guarantor organised under the laws of your jurisdiction. If such loan is transferred by Lender A to Lender B, are there any special requirements necessary to make the loan and guarantee enforceable by Lender B?

There are no special requirements under Cayman Islands law to make the loan and guarantee enforceable by Lender B, provided that the novation/transfer mechanics in the applicable facility agreement are adhered to as a matter of the applicable governing law.

6 Withholding, Stamp and Other Taxes; Notarial and Other Costs

6.1 Are there any requirements to deduct or withhold tax from (a) interest payable on loans made to domestic or foreign lenders, or (b) the proceeds of a claim under a guarantee or the proceeds of enforcing security?

The Cayman Islands currently have no form of income, corporate or capital gains tax and no estate duty, inheritance tax or gift tax. Accordingly, no taxes, fees or charges (other than stamp duty) are payable either by direct assessment or withholding to the government or another taxing authority in the Cayman Islands under the laws of the Cayman Islands.

6.2 What tax incentives or other incentives are provided preferentially to foreign lenders? What taxes apply to foreign lenders with respect to their loans, mortgages or other security documents, either for the purposes of effectiveness or registration?

There are no tax incentives or other incentives under Cayman Islands law. See question 6.1.

6.3 Will any income of a foreign lender become taxable in your jurisdiction solely because of a loan to or guarantee and/or grant of security from a company in your jurisdiction?

No income of a foreign lender will become taxable in the Cayman Islands.

6.4 Will there be any other significant costs which would be incurred by foreign lenders in the grant of such loan/guarantee/security, such as notarial fees, etc.?

Other than, potentially, the payment of stamp duty and applicable court fees on enforcement, no other significant costs should be incurred by foreign lenders in the grant of any loan or the taking of the benefit of any guarantee or security interest.

6.5 Are there any adverse consequences to a company that is a borrower (such as under thin capitalisation principles) if some or all of the lenders are organised under the laws of a jurisdiction other than your own? Please disregard withholding tax concerns for purposes of this question.

Assuming that the lenders are not connected to the borrower, in principle there are no adverse consequences if the lenders are organised in a jurisdiction other than the Cayman Islands.

7 Judicial Enforcement

7.1 Will the courts in your jurisdiction recognise a governing law in a contract that is the law of another jurisdiction (a "foreign governing law")? Will courts in your jurisdiction enforce a contract that has a foreign governing law?

The courts of the Cayman Islands will observe and give effect to the choice of the applicable governing law (the "**Relevant Law**") of a contract assuming that the choice of the Relevant Law as the governing law of the applicable contract has been made in good faith and would be regarded as a valid and binding selection which will be upheld by the courts of that jurisdiction and any other relevant jurisdiction as a matter of the Relevant Law and all other relevant laws.

7.2 Will the courts in your jurisdiction recognise and enforce a judgment given against a company in New York courts or English courts (a "foreign judgment") without re-examination of the merits of the case?

Assuming that the choice of the Relevant Law (as defined in question 7.1 above) as the governing law of the applicable contract has been made in good faith and would be regarded as a valid and binding selection which will be upheld by the courts of the applicable jurisdiction (the "**Relevant Jurisdiction**") and any other relevant jurisdiction (other than the Cayman Islands) as a matter of the Relevant Law and all other relevant laws (other than the laws of the Cayman Islands), then although there is no statutory enforcement in the Cayman Islands of judgments obtained in the Relevant Jurisdiction, a judgment obtained in such jurisdiction will be recognised and enforced in the courts of the Cayman Islands at common law, without any re-examination of the merits of the underlying dispute, by an action commenced on the foreign judgment debt in the Grand Court of the Cayman Islands, provided such judgment is given by a foreign court of competent jurisdiction and is final, for a liquidated sum, not in respect of taxes or a fine or a penalty, and was not obtained in a manner, and is not of a kind, the enforcement of which is contrary to the public policy of the Cayman Islands.

7.3 Assuming a company is in payment default under a loan agreement or a guarantee agreement and has no legal defence to payment, approximately how long would it take for a foreign lender to (a) assuming the answer to question 7.1 is yes, file a suit against the company in a court in your jurisdiction, obtain a judgment, and enforce the judgment against the assets of the company, and (b) assuming the answer to question 7.2 is yes, enforce a foreign judgment in a court in your jurisdiction against the assets of the company?

Timing of any litigation will inevitably be dependent on a large number of variable factors (such as location of the defendant, defences raised, complexity of the proceedings and resistance to enforcement). Assuming the defendant is in the Cayman Islands and the matter is straightforward and uncontested, it is possible to obtain default or summary judgment within a short time period. Assuming there is no resistance to enforcement, it may be possible to complete the process in six months. If the defendant is outside the jurisdiction, the process may take substantially longer. The timing for enforcement of a judgment is also dependent on a number of variable factors. It may be possible to complete the process in two to three months, but it could take substantially longer.

7.4 With respect to enforcing collateral security, are there any significant restrictions which may impact the timing and value of enforcement, such as (a) a requirement for a public auction, or (b) regulatory consents?

Whilst there are no legislative requirements for a public auction or similar process in the Cayman Islands, liquidators owe fiduciary duties to the creditors and shareholders of a company to recover the best price possible (usually market value) for all assets of a company upon a liquidation. Recent case law has set a precedent for this in the case of enforcement over land located in the Cayman Islands. Receivers owe their primary duty to the secured party and will seek to recover sufficient funds to repay the debt due; however, they also have a duty to the obligor to recover the best price reasonably obtainable on a sale of the secured assets. Accordingly, public auction or a similar process may be appropriate in certain circumstances. Certain consents may also be required from the Monetary Authority if the obligor is a regulated entity.

7.5 Do restrictions apply to foreign lenders in the event of (a) filing suit against a company in your jurisdiction, or (b) foreclosure on collateral security?

There are no legislative restrictions on foreign lenders filing suit against a company in the Cayman Islands, assuming that they can establish that the Cayman Islands court has jurisdiction over the suit. There are no legislative restrictions applicable to foreclosure on collateral security.

7.6 Do the bankruptcy, reorganisation or similar laws in your jurisdiction provide for any kind of moratorium on enforcement of lender claims? If so, does the moratorium apply to the enforcement of collateral security?

No formal corporate rehabilitation procedure exists under either the Companies Law (2016 Revision) or the LLC Law, as is the case in England and Wales or in the United States, that would give a company or LLC the benefit of moratorium provisions in the payment of its debts, including certain secured debts. Each of a Cayman Islands company and LLC is subject to voluntary or involuntary winding up proceedings under the Companies Law (2016 Revision), although it is possible for a court to appoint a provisional liquidator after the presentation of a petition for the winding up of a company or LLC but before an order for the winding up of the company or LLC is made where, for example, there is an immediate need to take actions to safeguard assets for creditors. There is a growing practice in the Cayman Islands for provisional liquidators to be appointed with the principal objective of preparing a scheme of arrangement with the aim of avoiding a formal winding up. Although there is an automatic stay of proceedings against the vehicle when an order for winding up has been made and on the appointment of a provisional liquidator, the stay does not prevent a secured creditor from enforcing its security interest.

7.7 Will the courts in your jurisdiction recognise and enforce an arbitral award given against the company without re-examination of the merits?

The courts of the Cayman Islands will recognise and enforce arbitral awards made pursuant to an arbitration agreement in a jurisdiction which is a party to the United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards (the "**New York Convention**").

Although there is no statutory enforcement of arbitral awards made in jurisdictions not party to the New York Convention, the courts of the Cayman Islands will recognise and enforce such arbitral awards provided that (a) the parties have submitted to the arbitration by an agreement which is valid by its governing law, and (b) the arbitral award is valid and final according to the law which governs the arbitration proceedings. The arbitral award will not be regarded as final by a Cayman Islands court unless the arbitral tribunal has disposed of all the issues itself. A Cayman Islands court will not, however, recognise or enforce such arbitral awards if: (a) under the submission agreement and the law applicable thereto, the arbitrators have no jurisdiction to make the award; (b) it was obtained by fraud; (c) its recognition or, as the case may be, enforcement would be contrary to public policy; or (d) the proceedings in which it was obtained were opposed to natural justice.

8 Bankruptcy Proceedings

8.1 How does a bankruptcy proceeding in respect of a company affect the ability of a lender to enforce its rights as a secured party over the collateral security?

In accordance with the Companies Law (2016 Revision), when a winding up order is made or a provisional liquidator is appointed, no suit, action or other proceedings, including criminal proceedings, shall be proceeded with or commenced against the company or LLC except with the leave of the court and subject to such terms as the court may impose. This prohibition in our view extends to judicial proceedings and does not include security enforcement methods which do not require an order of the court in the Cayman Islands. Furthermore, subject to any debts preferred by law, each of the Companies Law (2016 Revision) and the LLC Law provide that secured creditors may enforce their security notwithstanding that a winding up order has been made in respect of the applicable company or LLC.

8.2 Are there any preference periods, clawback rights or other preferential creditors' rights (e.g., tax debts, employees' claims) with respect to the security?

The enforceability of any security document will be subject to general insolvency rules applicable to companies and LLCs in the Cayman Islands including voidable preferences and transactions effected at an undervalue.

A secured party holding a fixed charge will, notwithstanding that a winding up order has been made, be entitled to enforce his security without the leave of the Cayman Islands court and without reference to the liquidator. However, if the security created by the relevant security document is treated as a floating charge, then debts preferred under Cayman Islands law will have priority over the secured party on a liquidation of the company or LLC.

In addition, subsequent purchasers, mortgagees, chargees, lienholders and execution creditors in respect of the assets subject to the floating charge are likely to have priority over the secured party, although this will depend upon such factors as the terms of the floating charge, in particular the scope of any restrictions, whether any subsequent purchasers, mortgagees or chargees have knowledge of any restrictions and the circumstances in which any subsequent transactions arise.

8.3 Are there any entities that are excluded from bankruptcy proceedings and, if so, what is the applicable legislation?

Neither companies nor LLCs incorporated in the Cayman Islands are excluded from proceedings under the Companies Law (2016 Revision), the LLC Law or any other applicable laws or regulations.

8.4 Are there any processes other than court proceedings that are available to a creditor to seize the assets of a company in an enforcement?

The Companies Law (2016 Revision) provides that, at any time after the presentation of a winding up petition and before a winding up order has been made, the company or any creditor or contributory may (a) where any action or proceeding against the company, including a criminal proceeding, is pending in a summary court, the Cayman Islands court, the Court of Appeal or the Privy Council, apply to the court in which the action or proceeding is pending for a stay of proceedings therein, and (b) where any action or proceeding is pending against the company in a foreign court, apply to the court for an injunction to restrain further proceedings therein, and the court to which application is made may, as the case may be, stay or restrain the proceedings accordingly on such terms as it thinks fit. On a voluntary winding up, there is no automatic moratorium. The Cayman Islands court does, however, have discretion to impose a moratorium on a blanket or a case-by-case basis. In practice, the court would only exercise its discretion if there was any doubt about the company's solvency.

A creditor of a company or LLC may have a compromise or arrangement imposed upon him under the Companies Law (2016 Revision) if a majority in number representing three quarters or more in value of the creditors (or class of creditors including the affected creditor) have approved the compromise or arrangement and it has been sanctioned by the Grand Court of the Cayman Islands. Although this is not a mandatory insolvency provision, it is a circumstance in which a creditor of a company or LLC may be made subject to an arrangement or compromise affecting his rights without his consent. It would not, however, affect the enforcement of security rights.

9 Jurisdiction and Waiver of Immunity

9.1 Is a party's submission to a foreign jurisdiction legally binding and enforceable under the laws of your jurisdiction?

The submission by a company or LLC in a security document to the jurisdiction of the courts of a particular jurisdiction will be legal, valid and binding on the company or LLC assuming that the same is true under the governing law of the security document and under the laws, rules and procedures applying in the courts of that jurisdiction.

9.2 Is a party's waiver of sovereign immunity legally binding and enforceable under the laws of your jurisdiction?

Companies and LLCs can, as a matter of contract, waive immunity for any legal proceedings in the Cayman Islands. However, subject to certain exceptions, companies may receive the benefit of sovereign immunity under the State Immunity Act of the United Kingdom, which has been extended to the Cayman Islands by statutory order.

10 Licensing

10.1 What are the licensing and other eligibility requirements in your jurisdiction for lenders to a company in your jurisdiction, if any? Are these licensing and eligibility requirements different for a "foreign" lender (i.e. a lender that is not located in your jurisdiction)? In connection with any such requirements, is a distinction made under the laws of your jurisdiction between a lender that is a bank *versus* a lender that is a non-bank? If there are such requirements in your jurisdiction, what are the consequences for a lender that has not satisfied such requirements but has nonetheless made a loan to a company in your jurisdiction? What are the licensing and other eligibility requirements in your jurisdiction for an agent under a syndicated facility for lenders to a company in your jurisdiction?

There are no licensing or eligibility requirements under Cayman Islands law for lenders to a company or LLC. Assuming that the lenders are not incorporated in or registered under Cayman Islands law and all the activities of such parties have not been and will not be carried on through a place of business in the Cayman Islands, then the lenders will not be required to be licensed in the Cayman Islands solely in order to provide a loan to a company or LLC. Any lenders that are incorporated or registered in the Cayman Islands or otherwise carrying on business in the Cayman Islands will be required to register and be licensed, as applicable, in accordance with Cayman Islands law.

11 Other Matters

11.1 Are there any other material considerations which should be taken into account by lenders when participating in financings in your jurisdiction?

The questions and answers set out in this chapter cover the main legal considerations for secured financings under Cayman Islands law.

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Tina Meigh is a partner in the Cayman Islands office of Maples and Calder, where she is head of the fund finance group. She specialises in finance transactions and has extensive experience in all aspects of fund finance, banking, structured finance, derivatives and securitisations. She represents hedge funds, private equity funds and banks on lending transactions, bank products, deal structures and on all types of secured transactions. Tina advises a large number of international associations and financial institutions on derivatives and issues surrounding related collateral packages in the context of insolvency in the Cayman Islands. She also has significant experience of general corporate and commercial matters and the establishment of offshore investment funds.

MAPLES

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Chile

Carey

Diego Peralta

1 Overview

1.1 What are the main trends/significant developments in the lending markets in your jurisdiction?

According to the Chilean Superintendency of Banks and Financial Institutions ("SBIF"), during the 12 months leading up to December 2016, the growth of credit was a modest 2.54%. This is explained by slow commercial lending (with a 0.23% growth over the year), though the housing sector also grew by 7.88% and the number of loans by 16.8%, with the lowest interest rates since 2005. Consumer lending grew by 4.23% during the same period. Provisions remained stable (2.49%, compared to 2.50% during 2016, composed by 2.41% for corporates (a drop of 1 bp), 6.39% for consumer loans (rise of 20 bp) and 0.86% for housing (dropping 8 bp).

1.2 What are some significant lending transactions that have taken place in your jurisdiction in recent years?

There is no separate information pertaining to local lending transactions, but, generally speaking, the largest sector of borrowers is real estate developers, followed by commerce (retail) and construction.

Nonetheless, in the last two years, Carey has advised, among others, the following clients in significant lending transactions:

- Codelco in the refinancing of the loan granted by The Bank of Tokyo-Mitsubishi UFJ for USD250 million and in a five-year senior unsecured term loan for USD300 million by Scotiabank & Trust (Cayman); and an energy company in a Senior Unsecured Term Loan Agreement entered into under New York law, with US banks as lenders under the USD250 million tranche, and with Chilean banks as lenders under a CLP tranche equivalent to USD1,500 million.
- Export Development Canada ("EDC") in a loan agreement to Codelco for USD300 million; and Aela Energía in a long-term loan for USD435 million to finance the construction of two wind farms (Aurora and Sarco), and to refinance an existing loan with China Development Bank.

2 Guarantees

2.1 Can a company guarantee borrowings of one or more other members of its corporate group (see below for questions relating to fraudulent transfer/financial assistance)?

Following certain corporate requirements depending on the type of company involved, provided the guarantor benefits somehow from these operations, and subject to applicable insolvency, moratorium or similar laws relating to or affecting creditors' rights generally, and general principles of fairness (regardless of whether it is considered in a proceeding in equity or at law), there is no restriction for this type of guarantee.

Additionally, under Chilean general banking law, banks are not authorised to grant mortgages or pledges over their own physical assets, unless to guarantee payment of the purchase price thereof. Considering this, it has been construed that banks can provide guarantees over financial assets subject to certain restrictions regulated by the SBIF.

2.2 Are there enforceability or other concerns (such as director liability) if only a disproportionately small (or no) benefit to the guaranteeing/securing company can be shown?

Under the Chilean Corporations Law, directors of corporations are jointly and severally liable for any damages caused to shareholders for their negligent or malicious actions, making it highly unlikely that the approval of a board would be secured for such a disadvantageous operation. Should the agreements cause the company's insolvency, there are actions for revocation which apply once the reorganisation or liquidation procedures have started, according to Chilean insolvency law. Among the agreements that can be revoked are any pledge or mortgage granted by the insolvent company within a year before the insolvency proceedings (to guarantee debts previously acquired), and any act or agreement (including granting guarantees) entered into within two years before the insolvency proceedings, provided that (i) the counterparty knew of the company's poor state of business, and (ii) the agreement has caused damage to the other creditors, where damage means that terms and conditions were distant from the market's at the time of the agreement. On the other hand, article 2,468 of the Chilean Civil Code grants the creditors of an insolvent debtor the right to request the revocation of certain agreements entered into by such debtor (*acción pauliana*), provided that: (i) the transaction causes damages to the creditors (the transaction executed increased the insolvency of the debtor); (ii) the debtor was aware of its poor business condition at the time of entering into such act or contract; and (iii) in case of an onerous act or contract, the counterparty of the debtor was also aware of the poor business condition of the debtor.

2.3 Is lack of corporate power an issue?

Yes. The Chilean Civil Code establishes in articles 2,151 and 2,160 that the principal shall not be obliged toward third parties by acts or agreements entered into by its agent if (i) the latter did not mention that he was acting on behalf of the principal, and (ii) the agent acts beyond the limits of its mandate. Ratification by the principal of the non-empowered actions may be a solution for the lack of corporate power.

2.4 Are any governmental or other consents or filings, or other formalities (such as shareholder approval), required?

There are no governmental approvals required, but, depending on the company's structure, the value and the type of guarantee, there are certain corporate consents which are required. If the guarantor is a corporation, in order to guarantee third-party obligations (unless the guaranteed obligations belong to a company that is a subsidiary of the guarantor, in which case the Board's approval suffices, and also with an exception for lender banks) and also if the value of the guaranteed obligations exceed 50% of the guaranteeing corporation's assets, an extraordinary shareholders' meeting must be called in order to grant approval.

2.5 Are net worth, solvency or similar limitations imposed on the amount of a guarantee?

No. Nevertheless, any operation executed between related parties needs to be for the company's benefit, complying with the market's standards for price, terms and conditions, and also the required approval if the guaranteed value exceeds 50% of the guarantor's assets, as explained above.

2.6 Are there any exchange control or similar obstacles to enforcement of a guarantee?

There are no exchange control regulations. Payment in foreign currency is possible if the parties have agreed such form of payment. In order to enforce a guarantee (as an accessory obligation) it is required that the secured obligations comply with certain requirements, and in case of obligations governed by foreign law and subject to foreign jurisdiction, *exequatur* procedures have to be conducted. Subject to Law No. 18,010 regarding lending operations, transactions agreed in a foreign currency shall be payable according to the seller exchange rate applicable on date of payment, which must be certified by a Chilean commercial bank. Please refer to our answers to questions 7.2, 7.3 and 7.7 in regard to the enforcement of foreign judgments procedure.

3 Collateral Security

3.1 What types of collateral are available to secure lending obligations?

Securities can be classified into two big groups: (i) guarantees over assets or rights *in rem*; and (ii) personal guarantees.

i) Guarantees over assets: There are guarantees over moveable assets (pledge agreements) and guarantees over real estate, vessels and aircraft (mortgage agreements).

a) Guarantees over moveable assets:

- **Civil Pledge**: This has a wide scope, as it may apply to any moveable property, including all kinds of personal rights and credits. Any obligation may be secured by this pledge, including obligations to act, or to refrain from acting. However, it is not commonly used, as the pledgor must deliver the pledged asset, losing the ability to use and enjoy it.
- **Commercial pledge**: This aims to secure commercial obligations. Though it is very similar to the civil pledge, unlike the latter, the material possession by the pledgee is not required, as it may be delivered to a third-party bailee. It is not possible to secure future obligations – only currently existing and determined obligations – and its only requirement is that the material possession of the pledged property is not held by the pledgor. The Commerce Code requires certain formalities for granting the pledge in order for the pledgee to be able to exercise its right to be paid preferentially: (i) the execution of the pledge agreement by means of a public deed, or by private instrument entered into a Chilean Notary Public's registry; (ii) the amount of the debt secured and the pledged asset must be defined in the agreement; and (iii) for a pledge granted over a credit, the debtor of the credit must be notified not to make any payment under the pledged credit but to the creditor.
- **Banking pledge over securities**: This may be granted over bearer securities of any kind in favour of banks and other financial institutions, even those that are foreign. This pledge may secure all current or future obligations of the pledgor with the pledgee. It only requires the handing over of the instrument by the pledgor to the pledgee. Credits payable to the order (i.e., not in bearer form) must be endorsed as a guarantee to the pledgee. Finally, shares shall be pledged by means of a public deed or private instrument, which must be notified to the issuer by a Notary Public. This pledge does not allow the pledgor to remain in material possession of the pledged assets. It is worth noting that the Constitutional Court of Chile ruled in one case that this procedure was not compliant with the due process constitutional protection, thus it declared the same unconstitutional. This is not a general ruling, but it may show a tendency.
- **Pledge without conveyance** ("**PwC**"): This allows any kind of corporeal or incorporeal, present or future, moveable assets to be pledged in order to secure own or third-party obligations, present or future, irrespective of whether such obligations are determined or undetermined at the time of the pledge agreement. It must be executed either by means of a public deed or a private instrument, with the signatures of the appearing parties authorised by a Chilean Notary Public, before the instrument is entered into a Chilean Notary Public's registry. The PwC agreement must contain at least the following references: (i) the identities of the parties; (ii) the existing secured obligations or the specification that the pledge secures present and future obligations (*cláusula de garantía general*); (iii) the identification of the pledged assets; and (iv) the determined or undetermined amount to which the pledge is limited or the extent to which the pledge secures several obligations, if applicable. The PwC agreement must be registered in a special registry called the Pledge without Conveyance Registry. Upon its registration, the pledge without conveyance is enforceable upon third parties.
- **Pledge over deposited securities**: A new pledge was created at the end of 2016 to simplify the pledging of securities deposited with depository entities. The latter shall need to enter into a master agreement with all depositors to allow this type of pledge.

b) Guarantees over real estate:

- **Mortgages**: Granted by means of a public deed, a mortgage allows not only existing and determined obligations but present and future obligations of the borrower (*cláusula de garantía general*) to be secured.

Mortgages are perfected by means of registration in the corresponding Mortgage Lien Registry. Generally, the mortgage deed will also contemplate a prohibition to transfer, convey and enter into acts or contracts with respect to the mortgaged property.

- Likewise, mortgages can be granted over mining concessions and water rights, which need to be registered in the same manner in the Custodian of Mines' Registry or the Real Estate Registrar Property Registry, as appropriate.
- **Guarantees over vessels and aircraft**: Mortgages can be granted over vessels and airplanes fulfilling certain requirements, such as the vessel or airplane being duly registered in the corresponding Registry and the agreement being granted by means of a public deed.

ii) **Personal guarantees**: The most common personal guarantees in Chile are sureties (*fianzas*) and joint and several guarantees (*fianzas y codeudas solidarias*). By means of sureties, one or more third parties are bound to pay the debtor's obligation in the event such debtor does not pay the secured obligation. By virtue of joint and several guarantees, the liability for default is enforceable directly against all of the debtor(s) and guarantors as a group or against any one of them as an individual at the choice of the enforcing creditor. The main characteristic of the joint and several guarantees is that guarantors become equally liable to the creditor, just as the primary debtor. Therefore, they are not entitled to request that (i) the debt be claimed first from the borrowers and only if they do not pay, then be collected from them, and (ii) the debt be divided equally or proportionally among the various guarantors. Under Chilean law, guarantees are an accessory to the main obligations and cannot exceed the amount of such obligations. This is expressly regulated for sureties, where it is stated that they cannot exceed the main obligation being guaranteed and cannot be granted in terms more onerous than those of the main obligor, but can be granted in terms more effective (like securing its obligations as guarantor through a mortgage, for example). The Chilean Civil Code does not provide for any formalities at all to grant sureties but if the obligation intended to be secured is a commercial obligation, it must be granted in writing. Where the guarantor of a surety and a joint several co-debt is an individual married under joint ownership of the matrimonial estate (*sociedad conyugal*), the prior spouse's consent is required.

iii) **Conditional assignments of rights**: This is a widely used tool in Chile to safeguard creditors' rights in an event of default.

3.2 Is it possible to give asset security by means of a general security agreement or is an agreement required in relation to each type of asset? Briefly, what is the procedure?

It is not possible to dispose or grant a security over all of an entity's assets. The guarantee document must clearly identify which assets are being pledged (or mortgaged). Additionally, each type of security requires specific formalities for perfection (see our answer to question 3.1 above). The most advisable manner is to have an agreement for every type of asset, since each has a different registration process.

3.3 Can collateral security be taken over real property (land), plant, machinery and equipment? Briefly, what is the procedure?

Yes. Please refer to the answer to question 3.1.

3.4 Can collateral security be taken over receivables? Briefly, what is the procedure? Are debtors required to be notified of the security?

Yes. Please refer to the answer to question 3.1, since the receivables are credits.

3.5 Can collateral security be taken over cash deposited in bank accounts? Briefly, what is the procedure?

Yes, it can be taken either by means of a commercial pledge or a PwC. The procedure is briefly explained in the answer to question 3.1.

3.6 Can collateral security be taken over shares in companies incorporated in your jurisdiction? Are the shares in certificated form? Can such security validly be granted under a New York or English law governed document? Briefly, what is the procedure?

Yes. All the pledges set forth by Chilean law can be granted over shares. Please refer to our answer to question 3.1. The Chilean Corporations Law states that any liens or rights *in rem* over shares of a company must be notified by a minister of faith, who must leave a record thereof in the company's shareholders' registry. Shares can be issued either in certificated form, or dematerialised in case of corporations and companies limited by shares.

According to the Chilean Civil Code, assets located in Chile are subject to Chilean law, and hence, the pledge shall be granted in accordance with Chilean law.

3.7 Can security be taken over inventory? Briefly, what is the procedure?

Yes. Please refer to the answer to question 3.1.

3.8 Can a company grant a security interest in order to secure its obligations (i) as a borrower under a credit facility, and (ii) as a guarantor of the obligations of other borrowers and/or guarantors of obligations under a credit facility (see below for questions relating to the giving of guarantees and financial assistance)?

Yes, it can. Please refer to our answer to question 2.4 above.

3.9 What are the notarisation, registration, stamp duty and other fees (whether related to property value or otherwise) in relation to security over different types of assets?

It mainly depends on the kind of collateral the company is granting. Excepting civil and commercial pledges, all other collateral agreements must be executed by means of a public deed or by a private document which must be authorised and registered by a Notary Public. Therefore, notarisation expenses are common to all kinds of collateral over all kinds of assets.

In case of mortgages, as mentioned above, the agreement has to be registered in the relevant Mortgage Lien Registry and in the Prohibitions Registry of the Real Estate Custodian, which charges a fee as well.

In case of a PwC, it is necessary to register it in the PwC Registry, which also charges a fee. If a PwC is granted over shares which are deposited in the Central Securities Deposit, these must be registered in an electronic pledge registry, which also charges a fee for its services.

3.10 Do the filing, notification or registration requirements in relation to security over different types of assets involve a significant amount of time or expense?

No, expenses are generally not material, and in general, procedures do not take long, although it depends on the registrar and workload at the time of the registration request The PwC Registry charges a fixed fee of CLP30,000 (approx. USD50) for each such registration.

3.11 Are any regulatory or similar consents required with respect to the creation of security?

No, there are not.

3.12 If the borrowings to be secured are under a revolving credit facility, are there any special priority or other concerns?

No, there are not.

3.13 Are there particular documentary or execution requirements (notarisation, execution under power of attorney, counterparts, deeds)?

Yes; please refer to the answers above. In case of the execution of foreign agreements in Chile, documents must be apostilled and, if not in Spanish, shall need to be translated to be presented in courts.

4 Financial Assistance

4.1 Are there prohibitions or restrictions on the ability of a company to guarantee and/or give security to support borrowings incurred to finance or refinance the direct or indirect acquisition of: (a) shares of the company; (b) shares of any company which directly or indirectly owns shares in the company; or (c) shares in a sister subsidiary?

(a) Shares of the company

There are no such prohibitions or restrictions under Chilean law, except for the requirements mentioned in our answers to questions 2.4 and 2.5.

(b) Shares of any company which directly or indirectly owns shares in the company

There are no such prohibitions or restrictions under Chilean law, except for the requirements mentioned in our answers to questions 2.4 and 2.5.

(c) Shares in a sister subsidiary

There are no such prohibitions or restrictions under Chilean law, except for the requirements mentioned in our answers to questions 2.4 and 2.5.

5 Syndicated Lending/Agency/Trustee/Transfers

5.1 Will your jurisdiction recognise the role of an agent or trustee and allow the agent or trustee (rather than each lender acting separately) to enforce the loan documentation and collateral security and to apply the proceeds from the collateral to the claims of all the lenders?

Yes. Their appointment requires the existence of at least two creditors, who may grant the authorities to manage the collateral as well as enforcement and release of the same in case of an event of default, among other duties and attributions. In the case of a single lender, it can also issue a mandate for a local entity/person to act on its behalf, serving the same purpose as a collateral agent with the same powers.

5.2 If an agent or trustee is not recognised in your jurisdiction, is an alternative mechanism available to achieve the effect referred to above which would allow one party to enforce claims on behalf of all the lenders so that individual lenders do not need to enforce their security separately?

In the case of a single lender, it can also issue a mandate for a local entity/person to act on its behalf, serving the same purpose as a collateral agent with the same powers.

5.3 Assume a loan is made to a company organised under the laws of your jurisdiction and guaranteed by a guarantor organised under the laws of your jurisdiction. If such loan is transferred by Lender A to Lender B, are there any special requirements necessary to make the loan and guarantee enforceable by Lender B?

Yes. Under the Chilean Civil Code, it is necessary to duly notify the credit assignment to the debtor. Otherwise, the assignment cannot be enforced against the debtor.

Regarding the guarantees, the Chilean Civil Code provides that assignment of credits encompasses assignment of guarantees securing the same, by operation of law.

In all such cases, if there is a foreign lender lending to a Chilean, the changes must be reported to the Central Bank of Chile.

6 Withholding, Stamp and Other Taxes; Notarial and Other Costs

6.1 Are there any requirements to deduct or withhold tax from (a) interest payable on loans made to domestic or foreign lenders, or (b) the proceeds of a claim under a guarantee or the proceeds of enforcing security?

(a) As a general rule, interest paid by Chilean taxpayers to foreign lenders is subject to a 35% withholding tax. However, a reduced 4% tax rate is applicable to certain interest payments (see question 6.2). The above is notwithstanding the existence of double taxation treaties. The payment of interest by Chilean taxpayers to domestic lenders is not subject to withholding tax.

(b) Payments of interest abroad upon enforcement of a guarantee could be subject to withholding tax depending on the reimbursement rights that the guarantor has against the main obligor.

6.2 What tax incentives or other incentives are provided preferentially to foreign lenders? What taxes apply to foreign lenders with respect to their loans, mortgages or other security documents, either for the purposes of effectiveness or registration?

Interest paid to foreign banks or foreign financial institutions complying with the requirements set by Chilean tax legislation benefit from a reduced withholding tax rate of 4%. Interest payments to foreign individuals resident in a country where there is a tax treaty in place with Chile may also benefit from a reduced withholding tax rate.

Stamp tax applies to documents evidencing indebtedness for borrowed money, including loan documents, notes and bond issuances. The tax is applied over the principal amount of the loan and its current rate is 0.066% of the principal amount multiplied by the number of months-to-maturity of the loan, with a maximum of 12 months (i.e. 0.8%). In case of loans payable on-demand, the applicable rate is 0.332%.

6.3 Will any income of a foreign lender become taxable in your jurisdiction solely because of a loan to or guarantee and/or grant of security from a company in your jurisdiction?

No, it will not.

6.4 Will there be any other significant costs which would be incurred by foreign lenders in the grant of such loan/guarantee/security, such as notarial fees, etc.?

There are transactional fees and translation costs, but, as explained in our answer to question 3.9, they are not significant.

6.5 Are there any adverse consequences to a company that is a borrower (such as under thin capitalisation principles) if some or all of the lenders are organised under the laws of a jurisdiction other than your own? Please disregard withholding tax concerns for purposes of this question.

Under Chilean income tax law, thin capitalisation rules are triggered when a Chilean-resident taxpayer pays interest or other financing expenses (e.g. services, commissions, expenses reimbursements) to a related party abroad under a reduced withholding tax rate from the 35%. Per the thin capitalisation rules, any interest (or similar) payments made abroad to a related party and attributed to excessive indebtedness are subject to a 35% tax payable by the debtor. The withholding tax applicable to the payments made by the Chilean resident taxpayer can be used as a credit against such 35% tax.

A taxpayer will be deemed to have "excessive indebtedness" if its total indebtedness (related and non-related) is greater than three times its tax equity at the end of the year when payments were made to related parties.

7 Judicial Enforcement

7.1 Will the courts in your jurisdiction recognise a governing law in a contract that is the law of another jurisdiction (a "foreign governing law")? Will courts in your jurisdiction enforce a contract that has a foreign governing law?

Yes, taking into consideration the existence of a connecting factor with the parties involved. However, according to article 16 of the Chilean Civil Code and article 105 of the Private International Law Code (the "Bustamante Code"), assets are governed by the *lex situs* (the law of the jurisdiction where the assets are located), thus assets of any kind located in Chile are governed by Chilean laws. In consequence, generally speaking, a choice of law of a court in Chile will be based on the *lex situs* of the charged assets.

7.2 Will the courts in your jurisdiction recognise and enforce a judgment given against a company in New York courts or English courts (a "foreign judgment") without re-examination of the merits of the case?

Yes. Chilean courts would enforce an English/New York judgment without re-examination of the merits, provided legal requirements are met and there are no public policy considerations and to the extent the judgment complies with a proceeding called "*exequatur*" which must be followed before the Chilean Supreme Court.

7.3 Assuming a company is in payment default under a loan agreement or a guarantee agreement and has no legal defence to payment, approximately how long would it take for a foreign lender to (a) assuming the answer to question 7.1 is yes, file a suit against the company in a court in your jurisdiction, obtain a judgment, and enforce the judgment against the assets of the company, and (b) assuming the answer to question 7.2 is yes, enforce a foreign judgment in a court in your jurisdiction against the assets of the company?

(a) In general, disputes are resolved in the first instance by a lower court, which may take from two to four years. Rulings and judgments of a lower court may be reviewed in second instance by a Court of Appeals, which may take from one to two years. Beyond that, some remedies may be claimed before the Supreme Court, which may take from one to two years. Therefore, a common civil proceeding may take up to eight years. In addition, enforcement of judgments is generally executed by means of an enforcement proceeding, which may take around one year.

(b) The *exequatur* proceeding itself may usually take around six to eight months. Once the *exequatur* is obtained, the enforcement proceeding may usually take around one year, although we have obtained payment in a New York-issued ruling in a three-month period.

7.4 With respect to enforcing collateral security, are there any significant restrictions which may impact the timing and value of enforcement, such as (a) a requirement for a public auction, or (b) regulatory consents?

Yes. The enforcement of collateral security located in Chile must be made in Chile, before the competent Chilean court, in accordance with the rules for the so-called summary proceeding (*juicio ejecutivo*) contained in the Chilean Code of Civil Procedure. This procedure provides a very brief discussion stage, a stage of liquidation and subsequent public auction, which is held by auctioneers appointed by the court. This last stage can take a long time and the proceeds of the auction may be different from the expected ones.

7.5 Do restrictions apply to foreign lenders in the event of (a) filing suit against a company in your jurisdiction, or (b) foreclosure on collateral security?

No, they do not.

7.6 Do the bankruptcy, reorganisation or similar laws in your jurisdiction provide for any kind of moratorium on enforcement of lender claims? If so, does the moratorium apply to the enforcement of collateral security?

Yes. According to Chilean insolvency law, during a term of 30 days as of the legal notice of the reorganisation resolution which appoints a supervisor for the insolvency proceeding ("**Veedor**"), the debtor will be protected by the Insolvency Financial Protection (*Protección Financiera Concursal*), during which neither the declaration nor the initiation of a liquidation proceeding against the debtor or foreclosures can take place, nor individual foreclosures, any kind of executions or restitutions in lease trials may be initiated and, among others, all agreements executed by the debtor will maintain their effectiveness and payment conditions. The credits that contravene this restriction will be postponed in payment until all of the creditors have been paid off. This 30-day period may be extended under certain circumstances for two more 30-day periods. Personal guarantees issued by third parties can be foreclosed nonetheless.

7.7 Will the courts in your jurisdiction recognise and enforce an arbitral award given against the company without re-examination of the merits?

Yes. Foreign arbitral awards are recognised and enforced in Chile, subject to an *exequatur* from the Supreme Court, which will be granted provided legal requirements are met and there are no public policy considerations, without re-examination of the merits.

8 Bankruptcy Proceedings

8.1 How does a bankruptcy proceeding in respect of a company affect the ability of a lender to enforce its rights as a secured party over the collateral security?

Please see our answer to question 7.6 above.

8.2 Are there any preference periods, clawback rights or other preferential creditors' rights (e.g., tax debts, employees' claims) with respect to the security?

According to Chilean insolvency law and the Chilean Civil Code, there is a scale of preference, according to which debts are paid. The first class, which includes judicial costs, administrative and liquidation fees, labour wages, severance payments and surcharge and withholding taxes, has preference over all other credits. The second class includes the rights of the pledgee over the pledged asset. Mortgagees prefer every other credit, including first class credits, over the mortgaged asset; nevertheless, if there are not enough assets to cover the debts, the first class gives preference to the mortgagee over the mortgaged asset.

8.3 Are there any entities that are excluded from bankruptcy proceedings and, if so, what is the applicable legislation?

Banks and the Republic and its agencies and municipalities are excluded. Mutual, investment and pension funds are deemed a created patrimony that adopt an independent existence from their owner in order to serve a particular and autonomous purpose; thus they are not considered a legal entity. Their managers (corporations) might be declared insolvent.

8.4 Are there any processes other than court proceedings that are available to a creditor to seize the assets of a company in an enforcement?

No, there are not.

9 Jurisdiction and Waiver of Immunity

9.1 Is a party's submission to a foreign jurisdiction legally binding and enforceable under the laws of your jurisdiction?

Yes, it is. Nonetheless, the Republic and its agencies and the Central Bank of Chile have certain restrictions and sometimes they may not submit to foreign jurisdiction.

9.2 Is a party's waiver of sovereign immunity legally binding and enforceable under the laws of your jurisdiction?

Yes, it is. Nonetheless, the Republic and its agencies have certain restrictions and sometimes they may not waive sovereign immunity.

10 Licensing

10.1 What are the licensing and other eligibility requirements in your jurisdiction for lenders to a company in your jurisdiction, if any? Are these licensing and eligibility requirements different for a "foreign" lender (i.e. a lender that is not located in your jurisdiction)? In connection with any such requirements, is a distinction made under the laws of your jurisdiction between a lender that is a bank *versus* a lender that is a non-bank? If there are such requirements in your jurisdiction, what are the consequences for a lender that has not satisfied such requirements but has nonetheless made a loan to a company in your jurisdiction? What are the licensing and other eligibility requirements in your jurisdiction for an agent under a syndicated facility for lenders to a company in your jurisdiction?

There are no licence or permission requirements to perform lending operations in Chile.

11 Other Matters

11.1 Are there any other material considerations which should be taken into account by lenders when participating in financings in your jurisdiction?

There are regulations for the prepayment for local loans, which are not applicable to cross-border loans. Additionally, there is no interest rate limit for loans granted to Chileans by foreign or international financial institutions or banks.

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He is counsel and member of the Executive Committee of The Inter-American Bar Association, member of the Council of the Chilean Bar Association (2017–2021), member of the Advisory Committee on Capital Markets to the Financing Minister, and is a member of the New Commerce Codification Commission for Chile. Also, he was part of a working group which analysed a new General Banking Law in Chile (2015).

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1 Overview

1.1 What are the main trends/significant developments in the lending markets in your jurisdiction?

The loan markets in the People's Republic of China (the "**PRC**") continued to be active in 2017. In particular, the "One Belt, One Road Initiative" (the "**BRI**") proposed by the Chinese Government that focuses on connectivity and cooperation with neighbouring countries in South East Asia, the Middle East, Europe, and Africa, has developed rapidly. The BRI mainly relates to investment in infrastructure, construction materials, railway and highway, automobile, real estate, power grid, and iron and steel, and has contributed to rapid growth in the volume of project finance and other loans provided by financial institutions. China Development Bank, the largest outbound investment and financing cooperation bank in the PRC, set up a special lending plan equivalent to RMB 250 billion in support of projects in connection with the BRI in May 2017.

Outside of the BRI, the PRC regulators hold a conservative attitude on other types of cross-border financing; in particular, financings which are used to support the overseas direct investment conducted by PRC enterprises. In December 2017, the State Administration for Foreign Exchange ("**SAFE**") issued the *Notice on Improving Foreign Exchange Administration on Bank NeiBaoWaiDai Business* to strengthen regulatory supervision and scrutiny of guarantees provided by PRC enterprises to offshore lenders to support obligations of offshore borrowers under offshore financings for the purpose of the PRC enterprise's overseas direct investment.

2017 also witnessed significant development in microcredits for individuals or small-and-medium-sized enterprises in PRC, as part of an overall growth of fintech.

1.2 What are some significant lending transactions that have taken place in your jurisdiction in recent years?

One of the most significant transactions in 2017 was the US$4.108 billion loan for a Chinese consortium's US$16 billion privatisation of Global Logistic Properties ("**GLP**"), the largest warehouse operator in Asia. The consortium comprised Hopu Investment Management, Hillhouse Capital Group, Vanke Group and Bank of China Group Investment. This acquisition was the largest private equity acquisition in Asia to date, and was voted 2017 deal of the year and leveraged financing deal of the year by Finance Asia.

Another significant financing deal in 2017 was the HK$28 billion loan for the HK$53.1 billion privatisation of Belle International Holdings Limited, the largest shoe retailer in the PRC. The management buyout acquisition is the largest privatisation deal ever for a Hong Kong listed company. KWM advised the lenders on this transaction.

2 Guarantees

2.1 Can a company guarantee borrowings of one or more other members of its corporate group (see below for questions relating to fraudulent transfer/financial assistance)?

A company can generally guarantee borrowings of one or more other members of its corporate group. According to PRC company law, any guarantee provided by a company for a third party must be approved by its board of directors or its shareholders in accordance with the provisions of its articles of association ("**AOA**"). However, if a company guarantees the liabilities of one of its shareholders or actual controller, the guarantee must be approved by affirmative votes of more than half of the shareholders at a shareholders' meeting, excluding the shareholder whose liabilities are guaranteed.

2.2 Are there enforceability or other concerns (such as director liability) if only a disproportionately small (or no) benefit to the guaranteeing/securing company can be shown?

There are no corporate benefit rules under PRC law. Accordingly, there are no enforceability or other concerns under PRC law where benefit is difficult to demonstrate, as long as that the guarantee/ security is provided in accordance with the applicable PRC law as well as the AOA of the guarantor/security provider.

2.3 Is lack of corporate power an issue?

PRC company law does require appropriate corporate action to be taken to authorise the giving of a guarantee by a company for the benefit of a third party. Lenders should review a guarantor's AOA and verify that necessary corporate and shareholder authorisations are in place. However, there is case law which supports the view that a guarantee will not necessarily be invalid just because such authorisations were not obtained.

2.4 Are any governmental or other consents or filings, or other formalities (such as shareholder approval), required?

A guarantee/security given by an onshore company securing an obligation of an offshore borrower owing to an offshore lender may be subject to approval by or registration with SAFE. See question 2.1 above on board and shareholder approvals. No other formalities are required for a company to grant a guarantee/security.

2.5 Are net worth, solvency or similar limitations imposed on the amount of a guarantee?

A company's AOA may limit the amount that the company can guarantee. If the guarantor is a listed company, there are additional mandatory requirements which require shareholder approval for: (1) any guarantee/security given when the aggregate amount of the external guarantee given by the listed company and its controlling subsidiary companies has exceeded 50% of the listed company's latest audited net assets; (2) any guarantee/security given to secure the obligation of a debtor whose asset to liability ratio exceeds 70%; (3) any guarantee to secure an amount exceeding 10% of the latest audited net assets of the guarantor; and (4) any guarantee provided to secure obligations of any shareholder, actual controller or their affiliated parties.

2.6 Are there any exchange control or similar obstacles to enforcement of a guarantee?

There are no exchange control or similar obstacles to enforce a guarantee so long as the giving of the guarantee complies with the regulations of the SAFE. For example, a guarantee given by a PRC company to secure the obligations of an offshore debtor owing to an offshore creditor must be registered with the SAFE within 15 business days after the date of the guarantee. The use of proceeds will also need to comply with the SAFE regulations.

3 Collateral Security

3.1 What types of collateral are available to secure lending obligations?

According to PRC law, the following collateral is available to secure lending obligations:

(1) land, buildings or other fixtures;

(2) manufacturing facilities, raw materials, semi-manufactured goods and products;

(3) transportation vessels;

(4) drafts, checks, promissory notes, bonds, deposit certificates, warehouse receipts, bills of lading;

(5) transferable shares and fund units;

(6) trademark rights, patent rights, copyright or other property rights in intellectual property that can be transferred;

(7) accounts receivable;

(8) any other property that is not prohibited by the laws;

(9) construction-in-progress; and

(10) any other property that is not prohibited by PRC law to be mortgaged, or any other rights that can be pledged as stipulated by PRC law.

3.2 Is it possible to give asset security by means of a general security agreement or is an agreement required in relation to each type of asset? Briefly, what is the procedure?

It is not possible to give asset security by means of a general security agreement, as security created over different types of assets is subject to different perfection procedures.

3.3 Can collateral security be taken over real property (land), plant, machinery and equipment? Briefly, what is the procedure?

Yes. A mortgage over real property, machinery or equipment is recognised by PRC law. Mortgages over real property need to be registered with the property bureau at the place where the property is located. Mortgages over machinery and equipment need to be registered with the State Administration of Industry and Commerce ("**SAIC**") at the place where the mortgagor is located. Mortgages over real property, machinery or equipment all have to be created by a written contract.

3.4 Can collateral security be taken over receivables? Briefly, what is the procedure? Are debtors required to be notified of the security?

Yes. A pledge over receivables is recognised by PRC law. The pledge has to be registered with the Credit Information Centre of the People's Bank of China ("**PBOC**"). This registration is generally done by the pledgee. The Credit Information Centre does not conduct any review or impose any other conditions. According to the PBOC regulations, receivables over which a pledge could be created must be generated from: (i) claims arising from a sale or lease, including the sale of goods, the supply of water, power, gas and heat, the licensed use of an intellectual property right, and the lease of movable properties or immovable properties; (ii) claims arising from the provision of services in areas of medical care, education, tourism, labour or other services; (iii) the right to obtain profits from energy, transport, water conservancy, environmental protection, municipal projects and other infrastructure and public utility projects; (iv) claims arising from the provision of loans or other credit activities; and (v) other rights entitled by the right holder under the law to claim payments. PRC law does not require notice of the security to be given to the debtor. However, it is good practice for notice to be given.

3.5 Can collateral security be taken over cash deposited in bank accounts? Briefly, what is the procedure?

Yes. A pledge over a cash deposit is recognised by PRC law. To create a pledge over a cash deposit, cash in the bank account must be ascertained and identified at the time of the creation of the pledge. The general understanding is that the bank account balance must not change. However there has been a recent court case indicating that fluctuation in the bank account balance may be permitted under certain circumstances.

3.6 Can collateral security be taken over shares in companies incorporated in your jurisdiction? Are the shares in certificated form? Can such security validly be granted under a New York or English law governed document? Briefly, what is the procedure?

Yes. A pledge of shares can be created over shares in companies incorporated in China. The documents granting security over the shares must be governed by PRC law. If not, the security interest would not be enforceable in China. The procedures to create a pledge of shares differ depending on the type of company. In the case of shares of a listed company, the pledge must be registered with the China Securities Deposit and Clearing Corporation Limited. In the case of shares of a foreign invested enterprise ("**FIE**"), the pledge is subject to approval from or online filing with the Ministry of Commerce or its local branch ("**MOFCOM**"), as the case may be, depending on whether such FIE's business scope falls into the catalogue of encouraged/permitted industries for foreign investment or restricted industries for foreign investment (approval from MOFCOM may be required if the FIE falls into a restricted category). In the case of shares of a non-listed and non-FIE company, the pledge must be registered with local SAIC where the company whose shares are being pledged is registered.

3.7 Can security be taken over inventory? Briefly, what is the procedure?

Yes. PRC property law provides that a party may create a mortgage over manufacturing equipment, raw materials, semi-finished products and finished products owned by it at the present or in the future. This is a concept similar to the concept of a floating charge under the common law. The mortgage must be in writing and registered with the SAIC. Without SAIC registration, the claim of the mortgagee is vulnerable to third-party claims.

3.8 Can a company grant a security interest in order to secure its obligations (i) as a borrower under a credit facility, and (ii) as a guarantor of the obligations of other borrowers and/or guarantors of obligations under a credit facility (see below for questions relating to the giving of guarantees and financial assistance)?

Yes. The conditions outlined in questions 2.1 and 2.6 also apply here.

3.9 What are the notarisation, registration, stamp duty and other fees (whether related to property value or otherwise) in relation to security over different types of assets?

Generally, no notarisation or stamp duty is required for creating security over different types of assets. If a security document involves a non-PRC party, notarisation by a notary and legalisation by a Chinese embassy or consulate may be required. In respect of registration requirements, see questions 3.3 to 3.7. Registration fees may be charged depending on the types of assets but the fees are mostly nominal.

3.10 Do the filing, notification or registration requirements in relation to security over different types of assets involve a significant amount of time or expense?

Timing for security perfection varies depending on the type of security. For example, perfection of a pledge of shares of a FIE requires online filing with or approval from (as the case may be) MOFCOM and SAIC registration. The approval from MOFCOM normally takes a couple of months while online filing and SAIC registration may take a couple of weeks. A mortgage of equipment or property on the other hand can take a considerable period of time. When a foreign party is involved, notarisation and legalisation may be required, in which case the security perfection process is longer. Other than registration fees there are no other governmental charges in respect of the creation of security.

3.11 Are any regulatory or similar consents required with respect to the creation of security?

There are no regulatory or similar consents required with respect to the creation of security except for the limited circumstances discussed in questions 2.6 and 3.6.

3.12 If the borrowings to be secured are under a revolving credit facility, are there any special priority or other concerns?

If the borrowings to be secured are under a revolving credit facility, usually a "maximum amount security" will need to be used. Under PRC law, a maximum amount security refers to a security created to secure obligations incurred during a period of time and the aggregate secured amount is subject to a maximum cap agreed by the parties. When applying a maximum amount security under a revolving credit facility, it is necessary for the lender to calculate the maximum loan amount and the interest with a cushion.

3.13 Are there particular documentary or execution requirements (notarisation, execution under power of attorney, counterparts, deeds)?

If a PRC law-governed contract requires both signing and affixing of a company chop, due execution of the contract requires both signing by authorised signatory(ies) as well as affixing of the company chop. If a contract does not require both signing and affixing of a company chop, either signing by authorised signatory(ies) or affixing a company chop would be considered as due execution of the contract. A company is bound by execution by its legal representative. There are no special requirements on notarisation, execution under power of attorney, counterparts or deeds by a PRC party. If a signing party is a non-PRC party, notarisation and legalisation may be required in respect of the non-PRC party's execution of the relevant security documents.

4 Financial Assistance

4.1 Are there prohibitions or restrictions on the ability of a company to guarantee and/or give security to support borrowings incurred to finance or refinance the direct or indirect acquisition of: (a) shares of the company; (b) shares of any company which directly or indirectly owns shares in the company; or (c) shares in a sister subsidiary?

There is no general prohibition on financial assistance. However, the restrictions on granting of a guarantee outlined in question 2.1 also apply to the grant of security. Where a loan is extended from an offshore lender to an offshore borrower supported by a security and/or guarantee given by a PRC company to finance or refinance an offshore acquisition, SAFE regulations require that PRC outbound investment procedures are to be duly complied with.

5 Syndicated Lending/Agency/Trustee/Transfers

5.1 Will your jurisdiction recognise the role of an agent or trustee and allow the agent or trustee (rather than each lender acting separately) to enforce the loan documentation and collateral security and to apply the proceeds from the collateral to the claims of all the lenders?

The role of agent for a syndicate of banks who may change from time to time is recognised under PRC law. Trustees are not generally used in the context of syndicated lending in China. It is usual for syndicated loan lenders to appoint a facility agent or security agent to act for and on behalf of the syndicate. Subject to the provisions of the transaction documents, the agent bank may claim the whole amount of the loan from the obligors and distribute the proceeds to the syndicate banks in accordance with the provisions of the transaction documents.

5.2 If an agent or trustee is not recognised in your jurisdiction, is an alternative mechanism available to achieve the effect referred to above which would allow one party to enforce claims on behalf of all the lenders so that individual lenders do not need to enforce their security separately?

This is not applicable in the PRC.

5.3 Assume a loan is made to a company organised under the laws of your jurisdiction and guaranteed by a guarantor organised under the laws of your jurisdiction. If such loan is transferred by Lender A to Lender B, are there any special requirements necessary to make the loan and guarantee enforceable by Lender B?

According to PRC contract law, a party to a contract may transfer its rights to a third party by notifying the obligor of the transfer of the contractual rights and a party to a contract may assign its obligations after getting consent from the obligee, unless otherwise agreed in a contract. Accordingly, unless the loan agreement provides otherwise, Lender A may transfer its right to a loan already disbursed to the borrower by giving notice to the borrower. If a loan is yet to be disbursed, Lender A may only assign the obligation to disburse a loan if the borrower's consent is obtained. The notice or the consent must be in writing. No consent is required from a guarantor for the transfer or assignment of the loan from Lender A to Lender B unless the guarantee document expressly required this. It is good practice to notify the guarantor of the transfer or assignment.

6 Withholding, Stamp and Other Taxes; Notarial and Other Costs

6.1 Are there any requirements to deduct or withhold tax from (a) interest payable on loans made to domestic or foreign lenders, or (b) the proceeds of a claim under a guarantee or the proceeds of enforcing security?

Income received by a lender from loans extended by it to a PRC borrower will be subject to PRC income tax. Such income may include (a) interest received by it on the loans, and (b) the proceeds of a claim under a guarantee or of enforcing security which constitutes payment of interest. For a PRC onshore lender in general, the income tax rate is 25% of its annual net profit. Tax payable by an offshore lender will be withheld from the PRC obligor's payment – the usual rate is 10% income tax and 6% value added tax on the interest amount, but preferential rates may be applied depending on the applicable tax treaty.

6.2 What tax incentives or other incentives are provided preferentially to foreign lenders? What taxes apply to foreign lenders with respect to their loans, mortgages or other security documents, either for the purposes of effectiveness or registration?

There are no preferential tax incentives or other incentives provided specifically to foreign lenders, except that foreign lenders may enjoy a preferential income tax rate provided by the applicable tax treaty between the PRC government and the government of the offshore lender's place of business. As of the end of October 2017, the PRC government has entered into tax treaties with 103 jurisdictions, and Hong Kong and Macau Special Administrative Regions, of which 99 have come into force. In addition to income tax, stamp duty is payable at 0.05% of the loan amount by both the lender and the borrower, respectively. A lender will also be subject to a business tax. Apart from these, there is no other tax in relation to a loan transaction.

6.3 Will any income of a foreign lender become taxable in your jurisdiction solely because of a loan to or guarantee and/or grant of security from a company in your jurisdiction?

See question 6.1 above. A foreign lender may be subject to income tax and value-added tax with respect to income received by it from loans provided to a PRC obligor.

6.4 Will there be any other significant costs which would be incurred by foreign lenders in the grant of such loan/guarantee/security, such as notarial fees, etc.?

Except for stamp duty, registration fees (e.g. for mortgage registration) and notary costs (if applicable); there are no other government fees or costs.

6.5 Are there any adverse consequences to a company that is a borrower (such as under thin capitalisation principles) if some or all of the lenders are organised under the laws of a jurisdiction other than your own? Please disregard withholding tax concerns for purposes of this question.

If some or all of the lenders are foreign lenders, the loan made to PRC companies is considered as foreign debt. There are restrictions as to whether a company could borrow foreign debt and how much it can borrow. Treatment is different for a FIE in China or non-FIE. FIE and non-FIE companies may carry out cross-border financing in RMB or foreign currencies in accordance with Circular on the Matters Relating to the *Macro-prudential Management of Full-covered Cross-border Financing* ("**Circular 9**"), whilst a FIE may choose between the regulation regime under Circular 9 and its existing foreign debt management system.

7 Judicial Enforcement

7.1 Will the courts in your jurisdiction recognise a governing law in a contract that is the law of another jurisdiction (a "foreign governing law")? Will courts in your jurisdiction enforce a contract that has a foreign governing law?

The PRC courts will recognise and enforce a governing law in a contract that is the law of another jurisdiction if there is a foreign element in connection with the contract; for example, if one of the parties to the contract is a foreign party or if the subject matter is located outside of China. The choice of foreign governing law must not violate China's social public interest.

7.2 Will the courts in your jurisdiction recognise and enforce a judgment given against a company in New York courts or English courts (a "foreign judgment") without re-examination of the merits of the case?

A judgment rendered by a New York court or English court is currently not enforceable in China. This is because a PRC court will only recognise and enforce a foreign court judgment if (a) a bilateral judicial assistance treaty exists between China and the country of the foreign court, (b) both countries have joined an international convention on recognising and enforcing foreign court judgments or written orders, or (c) precedents of reciprocity exist. There is no reciprocal recognition or enforcement of judgments or written order between China and the UK or the US.

7.3 Assuming a company is in payment default under a loan agreement or a guarantee agreement and has no legal defence to payment, approximately how long would it take for a foreign lender to (a) assuming the answer to question 7.1 is yes, file a suit against the company in a court in your jurisdiction, obtain a judgment, and enforce the judgment against the assets of the company, and (b) assuming the answer to question 7.2 is yes, enforce a foreign judgment in a court in your jurisdiction against the assets of the company?

A foreign lender may immediately file a suit against the company as soon as all the required court papers are in order. It will generally take up to six months to obtain a first instance judgment which shall be final if no party makes an appeal. If either party makes an appeal to a second instance court, it will generally take up to three months to obtain a second instance judgment, which shall be the final judgment. It is difficult to predict how long it will take to enforce the judgment.

7.4 With respect to enforcing collateral security, are there any significant restrictions which may impact the timing and value of enforcement, such as (a) a requirement for a public auction, or (b) regulatory consents?

Enforcement of security could be either on a consensual basis, i.e. the creditor and the security provider agree on the realisation of the collateral by conversion to value, or the creditor and security provider arrange auction or sale without going to court. If the security provider is not cooperative, the creditor will need to bring proceedings in a competent PRC court seeking a judgment. If a favourable judgment is rendered, the creditor may commence an enforcement proceeding during which the collateral could be auctioned or sold at the oversight of the court. Consents from government bodies are generally not required unless state-owned assets or FIE shares are involved.

7.5 Do restrictions apply to foreign lenders in the event of (a) filing suit against a company in your jurisdiction, or (b) foreclosure on collateral security?

The fact that a lender is foreign does not in itself impose additional restrictions on enforcing a loan or security.

7.6 Do the bankruptcy, reorganisation or similar laws in your jurisdiction provide for any kind of moratorium on enforcement of lender claims? If so, does the moratorium apply to the enforcement of collateral security?

After a Chinese court accepts a bankruptcy application, any preservation measure in respect of the bankrupt debtor's assets shall be released and any enforcement proceeding shall be suspended. Further, pending civil proceedings or arbitrations relating to the bankrupt debtor shall also be suspended and such proceedings may resume after the administrator has taken over the assets of the bankrupt debtor.

7.7 Will the courts in your jurisdiction recognise and enforce an arbitral award given against the company without re-examination of the merits?

Chinese courts will not examine the substance of the arbitral award given by a foreign arbitration tribunal and will give effect to and enforce the award provided that it is in compliance with the New York Convention.

8 Bankruptcy Proceedings

8.1 How does a bankruptcy proceeding in respect of a company affect the ability of a lender to enforce its rights as a secured party over the collateral security?

According to PRC bankruptcy law, once a PRC court accepts an application for a bankruptcy petition in relation to a bankrupt debtor, both secured creditors and unsecured creditors will need to declare their claims to the administrator for such claims to be registered. All creditors can then participate in the distribution of the assets of the bankrupt debtor.

8.2 Are there any preference periods, clawback rights or other preferential creditors' rights (e.g., tax debts, employees' claims) with respect to the security?

In order to protect the interests of the creditors and the equity-owners of the debtor, PRC bankruptcy law allows the administrator to petition the court to invalidate certain types of transactions conducted by the debtor within one year before the court accepts the bankruptcy petition, and to claw back the relevant assets back into the debtor's assets pool for subsequent distribution to the creditors and the equity-owners: (1) transfers of assets without consideration; (2) trading at an obviously unreasonable price; (3) providing assets-based security for debts not secured by property; (4) paying off undue debts in advance; or (5) giving up its right as a creditor.

The administrator may also petition the court to claw back payment made by the bankrupt debtor to certain creditors within six months before the court accepts the bankruptcy petition, provided that, at the time of the payment, the bankrupt debtor was insolvent.

The secured creditor's rights rank behind any outstanding salaries, pensions for the disabled, basic pension insurance, basic medical insurance or other compensation incurred before 27 August 2006 (the date on which the PRC bankruptcy law was adopted and promulgated) and payable to the employees of the bankrupt debtor according to relevant laws and regulations. These employees' claims, if incurred after 27 August 2006, will rank behind the secured creditor's secured obligations. In addition, if the security is created after incurring overdue tax payment, the tax payment shall rank ahead of the security.

8.3 Are there any entities that are excluded from bankruptcy proceedings and, if so, what is the applicable legislation?

PRC bankruptcy law applies to PRC companies in general, but does not apply to PRC financial institutions. The bankruptcy proceedings of financial institutions shall be governed by rules which are yet to be promulgated by the State Council.

8.4 Are there any processes other than court proceedings that are available to a creditor to seize the assets of a company in an enforcement?

No, seizure of assets of a company in an enforcement scenario may only occur following court proceedings.

9 Jurisdiction and Waiver of Immunity

9.1 Is a party's submission to a foreign jurisdiction legally binding and enforceable under the laws of your jurisdiction?

If a contract has no foreign elements, the subject matter shall be deemed as in the exclusive jurisdiction of the Chinese courts. The submission to a foreign jurisdiction shall be valid under PRC law if the subject matter is not under the exclusive jurisdiction of the PRC courts. As for the enforcement of a judgment made in a foreign jurisdiction, it depends on the applicable bilateral treaties, or otherwise on the basis of reciprocity.

9.2 Is a party's waiver of sovereign immunity legally binding and enforceable under the laws of your jurisdiction?

China adopts the "absolute immunity" principle, which provides complete immunity to the sovereign state. Therefore, any waiver of sovereign immunity is not legally binding and not enforceable if it is made by a Chinese governmental body. Please note, however, that state-owned enterprises are considered as separate legal entities rather than Chinese government bodies and therefore sovereign immunity does not apply to state-owned enterprises.

10 Licensing

10.1 What are the licensing and other eligibility requirements in your jurisdiction for lenders to a company in your jurisdiction, if any? Are these licensing and eligibility requirements different for a "foreign" lender (i.e. a lender that is not located in your jurisdiction)? In connection with any such requirements, is a distinction made under the laws of your jurisdiction between a lender that is a bank *versus* a lender that is a non-bank? If there are such requirements in your jurisdiction, what are the consequences for a lender that has not satisfied such requirements but has nonetheless made a loan to a company in your jurisdiction? What are the licensing and other eligibility requirements in your jurisdiction for an agent under a syndicated facility for lenders to a company in your jurisdiction?

Only financial institutions or quasi-financial institutions with lending as one of their approved business activities (e.g. banks, trust companies, auto-financial companies, micro-lending companies) can engage in the lending business. A foreign lender who makes a loan to a PRC company cross-border is not required to be licensed, qualified or otherwise entitled to carry on business in the PRC. A lender which carries out a lending business without lending as its approved business scope will be deemed to be carrying on illegal financial services and be sanctioned accordingly. In China, it is usual for a facility and security agent under a syndicated facility to also be a syndicate lender. A foreign lender can be an agent without any licence in PRC.

11 Other Matters

11.1 Are there any other material considerations which should be taken into account by lenders when participating in financings in your jurisdiction?

It is worth noting that, when non-bank entities are acting as guarantor/security providers in offshore financing transactions, domestic enterprises and overseas banks must also pay close attention to the requirements imposed by SAFE and other PRC regulators in relation to cross-border guarantee/security in such cases, to ensure the compliance of such transactions.

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Areas of Practice

Jack Wang specialises in international finance, project finance, foreign direct investment, and mergers and acquisitions.

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Jack has handled many large transactions in industries such as power, petrochemicals, expressways, water plants, bridges, aluminium plants, and MTR. He has also represented various international companies in their incorporation of foreign-invested enterprises or acquisitions of domestic companies.

Work Experience

Jack joined King & Wood Mallesons in 2003. Prior to joining King & Wood Mallesons, Jack was in charge of the Department of International Finance, at the Global Law Office in Beijing. He has also practised law at the New York office of Sherman & Sterling and at the Hong Kong office of Linklaters.

He graduated from Jilin University and earned his J.D. at Emory University in the United States.

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Stanley also has strong expertise in the bank card industry, payment service institutions and payment business, pre-paid card and internet-financing.

Stanley has worked in reputable local and international law firms in their Shanghai and Hong Kong offices.

Stanley graduated from the Law School of Fudan University and qualified in the same year.

Stanley's working languages are Mandarin and English.

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- Law Firm of the Year – Banking & Finance, *Best Lawyers 2018*.
- Banking Law Firm of the Year, ALB China Law Awards 2016 and 2017.
- Law Firm of the Year – KangaNews Awards 2017 (11 consecutive years).
- Banking and Finance Firm of the Year, China Law and Practice Awards 2017.
- Best Law Firm (revenue over $200m) AFR Client Choice 2017 (for the 2nd consecutive year) and Best Professional Services Firm (over $200m) AFR Client Choice 2016.

Colombia

Santiago Gutiérrez

Lloreda Camacho & Co.

Juan Sebastián Peredo

1 Overview

1.1 What are the main trends/significant developments in the lending markets in your jurisdiction?

According to the Financial System Report of 2017 by the Superintendence of Finance, the loan portfolio grew over 2%. This growth not only favoured the general business environment, helping the credit institutions maintain an interesting lending offer, but also had a positive impact in the market in order to renegotiate lending transactions.

The growth from last year can be explained by the increase of consumer credits, household credits and microcredit transactions, for which the credit institutions provided products with more attractive interest rates and renegotiation of lending transactions, among other strategies, in addition to positive behaviour from debtors.

Given the economic scenario, we believe that the Colombian lending market will continue to implement traditional credit structures and traditional credit products, as well as new, different structures that will arise from debt restructuring.

Finally, the Colombian Central Bank recently amended the foreign exchange regime and permitted foreign lenders to hold bank accounts in Colombian pesos (COP) for purposes of lending transactions (meeting certain requirements. This new regulatory development will entail the implementation of new COP credit structures.

1.2 What are some significant lending transactions that have taken place in your jurisdiction in recent years?

Colombia continues to be a country where relevant lending transactions have been completed. Recently, the country has faced an increasing number of transactions related to infrastructure in Colombia, as well as corporate finance.

Some significant transactions in which Lloreda Camacho has participated are: (i) a pre-export finance facility granted by Société Génerale to Prodeco CI, acting as a borrower; (ii) a facility granted by Standard Chartered to Petrominerales Colombia Ltda; (iii) a facility granted by the Interamerican Development Bank to Grupo la Hipotecaria in Colombia, Salvador and Panama; (iv) a syndicated loan granted by the Toronto-Dominion Bank and a syndicate of lenders in order to finance Enerflex, a Colombian company; and (v) a syndicated loan granted by Bancolombia to Phoenix Group – Multidimensionales.

2 Guarantees

2.1 Can a company guarantee borrowings of one or more other members of its corporate group (see below for questions relating to fraudulent transfer/financial assistance)?

Companies in Colombia are permitted to guarantee borrowing of members of their corporate group, so long as their by-laws contemplate such a possibility. The guarantor must have included this activity within its corporate purpose.

2.2 Are there enforceability or other concerns (such as director liability) if only a disproportionately small (or no) benefit to the guaranteeing/securing company can be shown?

Directors of Colombian companies are subject to certain fiduciary duties. Directors, therefore, have to act in good faith, loyalty and with the diligence of a good business man (art. 23 of Law 222 of 1995). Directors' actions must be fulfilled in the interest of the company, taking into account the interests of the shareholders. Directors are jointly and unlimitedly liable for any damages that they may cause due to their own fault or wrongdoing to the company, the shareholders and third parties (art. 200 of the Colombian Commerce Code).

Therefore, directors must ensure that the transaction (guaranteeing/securing) is included in the corporate purpose of the company and that such transaction does not infringe any of the duties described above.

2.3 Is lack of corporate power an issue?

A contract may be declared annulled in the event that the legal representative of the company (i.e. the director acting on behalf of the company) exceeded his or her faculties as established in the by-laws. Such annulment must be declared by a court in Colombia.

2.4 Are any governmental or other consents or filings, or other formalities (such as shareholder approval), required?

Corporate by-laws may require that certain transactions, such as guaranteeing/securing other companies' debt, or transactions that exceed a certain threshold, must be approved by either the Board of Directors or the General Shareholders' Assembly of the company.

2.5 Are net worth, solvency or similar limitations imposed on the amount of a guarantee?

Neither net worth nor solvency are criteria that impose limits on the amount of a guarantee.

2.6 Are there any exchange control or similar obstacles to enforcement of a guarantee?

Colombia's foreign exchange regime provides for certain registration rules applicable when Colombian companies guarantee borrowings of companies abroad or when foreign companies guarantee transactions in Colombia or with Colombian residents. These registration requirements do not constitute an obstacle to the enforcement of a guarantee.

3 Collateral Security

3.1 What types of collateral are available to secure lending obligations?

Collateral can traditionally be taken over real property and movable assets. The mechanisms to secure these assets, as explained further below, are traditionally through a mortgage agreement (real property), a pledge agreement (movable assets) or trust agreement (both real property and movable assets).

3.2 Is it possible to give asset security by means of a general security agreement or is an agreement required in relation to each type of asset? Briefly, what is the procedure?

A general security agreement would be permitted for purposes of taking security, as long as each asset that is being granted in security is identified in the agreement. With regard to real property security, a different agreement would be necessary, taking into account the procedure to take such type of asset as collateral (please refer to question 3.3 below).

3.3 Can collateral security be taken over real property (land), plant, machinery and equipment? Briefly, what is the procedure?

Collateral security can be taken over a variety of assets. The procedure varies if the asset is considered real property or movable. In the case of movable assets, collateral security would be taken through a pledge agreement which would have to be registered with the Movable Assets Collateral Registry (*Registro de Garantías Mobiliarias*). In the case of real property, the collateral security would have to be taken through a mortgage agreement (through a public deed) which would have to be registered with the Public Instruments Office (*Oficina de Registro de Instrumentos Públicos*).

3.4 Can collateral security be taken over receivables? Briefly, what is the procedure? Are debtors required to be notified of the security?

Yes. Receivables can be taken as collateral security. As a general principle, the debtors of the receivables would not have to be notified. However, the grantor of the collateral must follow any particular agreements reached with the debtor regarding notification of the security.

3.5 Can collateral security be taken over cash deposited in bank accounts? Briefly, what is the procedure?

Yes. Colombia permits taking collateral security over cash deposited in bank accounts. The procedure to secure the funds in bank accounts varies if the secured party is the bank where the cash is deposited or if the secured party is not the bank. In case the secured party is the bank, the collateral security would be completed by the execution of a security agreement whereby the bank, as the secured party, would have possession of the cash. In case the secured party is not the bank, a tri-party control agreement over the bank account would have to be executed.

3.6 Can collateral security be taken over shares in companies incorporated in your jurisdiction? Are the shares in certificated form? Can such security validly be granted under a New York or English law governed document? Briefly, what is the procedure?

Yes. Collateral security can be taken over shares of Colombian companies. Law 1676 of 2013 provides for the procedure applicable for granting shares (in certificated form) as collateral security pledges. For this purpose: (i) a pledge agreement over the shares would have to be executed; (ii) the pledge would have to be registered in the stock ledger of the company, and (iii) the pledge would have to be registered with the Public Instruments Office (*Oficina de Registro de Instrumentos Públicos*). The collateral documents must be governed by Colombian law.

3.7 Can security be taken over inventory? Briefly, what is the procedure?

Yes. Inventories are considered movable assets subject to Law 1676 of 2013. Therefore, security can be taken over this type of asset, subject to complying with the registration requirements set forth in the aforementioned law.

3.8 Can a company grant a security interest in order to secure its obligations (i) as a borrower under a credit facility, and (ii) as a guarantor of the obligations of other borrowers and/or guarantors of obligations under a credit facility (see below for questions relating to the giving of guarantees and financial assistance)?

A company in Colombia can grant a security interest to either secure its obligations as a borrower or as a guarantor of other borrowers under a credit facility. With regard to granting security as a guarantor, please refer to our answers to questions 2.6 and 4.1.

3.9 What are the notarisation, registration, stamp duty and other fees (whether related to property value or otherwise) in relation to security over different types of assets?

Costs related to notarisation, registration and other fees vary from each type of security. In relation to a mortgage (real property), the following cost will arise:

(i) Notarisation fees.

(ii) Registration tax.

(iii) Registration rights.

In relation to security interests over movable assets (*garantías mobiliarias*), a registry tax must be paid to Confecámaras (the chambers of commerce association) for an amount equivalent to USD$15.

In relation to a security trust agreement, aside from the costs that may arise from transferring the asset to the trust and the costs related to the registration of such transfer and of the trust agreement as a security, the trust company (*sociedad fiduciaria*) will charge fees for the administration of the trust.

3.10 Do the filing, notification or registration requirements in relation to security over different types of assets involve a significant amount of time or expense?

With regard to collateral security taken over movable assets, filing, notification and registrations does not involve a significant amount of time and can be completed in one day (the procedure for registration is carried out through the website of the *Registro de Garantías Mobiliarias*).

With regard to real property security, the procedure would involve granting the security through a mortgage public deed and registering the security with the Public Instruments Office. This procedure can take between one and two weeks.

Finally, in relation to security granted under the trust agreement, time and expense will depend on the type of asset taken as security. The time and costs will depend on the procedure that must be followed to transfer the assets to the trust.

3.11 Are any regulatory or similar consents required with respect to the creation of security?

As a general rule, the creation of security does not depend on regulatory consents. Nevertheless, the applicable regime of certain entities may provide for particular authorisations when granting collateral security.

3.12 If the borrowings to be secured are under a revolving credit facility, are there any special priority or other concerns?

There are no special priority concerns.

3.13 Are there particular documentary or execution requirements (notarisation, execution under power of attorney, counterparts, deeds)?

Please refer to our answers to questions 3.9 and 3.10.

4 Financial Assistance

4.1 Are there prohibitions or restrictions on the ability of a company to guarantee and/or give security to support borrowings incurred to finance or refinance the direct or indirect acquisition of: (a) shares of the company; (b) shares of any company which directly or indirectly owns shares in the company; or (c) shares in a sister subsidiary?

(a) Shares of the company

There is no general prohibition for companies to use financial assistance in the acquisition of shares, except for financial services. Colombian law prohibits credit institutions, including banks and insurance companies, to lend funds to third parties in order to acquire shares or mandatorily convertible bonds of the lending bank, its affiliates or any financial institution in Colombia, unless the acquisition refers to a primary issuance of shares or a privatisation process.

Therefore, there is no general prohibition on the ability to guarantee or give security to support borrowing incurred to finance or refinance the acquisition of shares.

Banks are allowed to lend funds to third parties in order to acquire the control of companies other than financial institutions.

(b) Shares of any company which directly or indirectly owns shares in the company

There is no general prohibition for the acquisition of shares under this scenario (please refer to the limitations for credit institutions). Regarding the acquisition of shares of a parent company, article 232 of the Colombian Commerce Code establishes that a subordinated company shall not hold shares of the parent company that controls it, and that any agreement contrary to such provision shall be considered null and void.

(c) Shares in a sister subsidiary

There is no general prohibition for the acquisition of shares under this scenario (please refer to the limitations for credit institutions).

5 Syndicated Lending/Agency/Trustee/Transfers

5.1 Will your jurisdiction recognise the role of an agent or trustee and allow the agent or trustee (rather than each lender acting separately) to enforce the loan documentation and collateral security and to apply the proceeds from the collateral to the claims of all the lenders?

Yes. In Colombia, the role of an agent or a trustee is recognised. This recognition permits the agent to enforce the loan documentation and collateral security (being the "secured party") and apply the proceeds to the claims of all the lenders. This is true from the perspective of foreign indebtedness (where the loan is subject to foreign law) or local indebtedness (using similar legal structures that resemble an agent or trustee).

5.2 If an agent or trustee is not recognised in your jurisdiction, is an alternative mechanism available to achieve the effect referred to above which would allow one party to enforce claims on behalf of all the lenders so that individual lenders do not need to enforce their security separately?

The role of an agent or trustee is recognised in Colombia.

5.3 Assume a loan is made to a company organised under the laws of your jurisdiction and guaranteed by a guarantor organised under the laws of your jurisdiction. If such loan is transferred by Lender A to Lender B, are there any special requirements necessary to make the loan and guarantee enforceable by Lender B?

There are no special requirements for debt transfer in Colombia, except as otherwise provided in the relevant debt documents.

The particular lending and security instruments would have to be assigned or novated. The collateral security registrations would have to be updated in order to reflect the new lender in the registry. If the transaction is a foreign loan, the foreign indebtedness registration with the Colombian Central Bank must be updated.

6 Withholding, Stamp and Other Taxes; Notarial and Other Costs

6.1 Are there any requirements to deduct or withhold tax from (a) interest payable on loans made to domestic or foreign lenders, or (b) the proceeds of a claim under a guarantee or the proceeds of enforcing security?

(a) As a general rule, interest is a deductible expense for income tax purposes. Article 107 of the Colombian Tax Code allows such deduction as long as the following conditions are fulfilled: (i) interest must be related to the income-producing activity; (ii) it must be necessary; and (iii) it must be reasonable to carry out income-producing activity.

- (i) Interest deductibility for income tax purposes is subject to further limitations:
- (ii) Deduction on interest expenses shall not exceed the highest interest rate authorised by the Superintendence of Finance.
- (iii) The inflationary component of interest is not treated as a deductible expense.
- (iv) In accordance with the Thin Capitalization Rule (article 118-1 of the Colombian Tax Code), interest accrued on debts or liabilities, the amount of which exceeds the taxpayer's equity by three times, is not deductible.
- (v) Deduction of payments made abroad (interest included) is limited to an amount equal to 15% of the annual taxable income, unless a withholding tax is triggered by the Colombian debtor.
- (vi) Interest payments to non-residents are subject to an income withholding tax at a tax rate of 15%.
- (vii) Interest expenses to related parties are not deductible, except: (i) short-term debt (less than 12 months) for the acquisition of raw materials or merchandise; or (ii) related parties that have complied with transfer pricing regulations. Presumptive interest shall be accrued if the lender is a shareholder of the borrower.

(b) The proceeds of a claim under a guarantee or the proceeds of enforcing security are not subject to income tax consequences, as long as payments under such procedures are treated as principal. For payments treated as interest, the abovementioned provisions apply.

6.2 What tax incentives or other incentives are provided preferentially to foreign lenders? What taxes apply to foreign lenders with respect to their loans, mortgages or other security documents, either for the purposes of effectiveness or registration?

Colombian tax legislation does not provide any special incentive to foreign lenders, unless a tax treaty applies. Interest income accrued or paid abroad is subject to a 15% income withholding tax. If such withholding is triggered and paid, foreign lenders are not obliged to file an income tax return in Colombia. A general income withholding tax rate (*33% for fiscal year 2018*) applies on interest payments if the lender is located in a jurisdiction listed as a tax haven by the Colombian Government (Decree 1625 of 2016).

6.3 Will any income of a foreign lender become taxable in your jurisdiction solely because of a loan to or guarantee and/or grant of security from a company in your jurisdiction?

Yes. In cross-border loan relationships, interest payments from a Colombian borrower are treated as Colombian-source income and hence subject to taxation in Colombia.

6.4 Will there be any other significant costs which would be incurred by foreign lenders in the grant of such loan/guarantee/security, such as notarial fees, etc.?

There are no other significant costs. Please refer to our answer to question 3.9.

6.5 Are there any adverse consequences to a company that is a borrower (such as under thin capitalisation principles) if some or all of the lenders are organised under the laws of a jurisdiction other than your own? Please disregard withholding tax concerns for purposes of this question.

No. We do not identify adverse consequences. Nevertheless, please refer to our taxation comments in our answer to question 6.1 above (with regard to thin capitalisation, please refer to question 6.1 (a) (iii)).

7 Judicial Enforcement

7.1 Will the courts in your jurisdiction recognise a governing law in a contract that is the law of another jurisdiction (a "foreign governing law")? Will courts in your jurisdiction enforce a contract that has a foreign governing law?

Pursuant to Colombian law, it is possible to agree on foreign governing law and jurisdiction, whenever it is considered that the contract is performed abroad (or substantially performed abroad). This is the case with foreign loans. However, agreeing on foreign law and submitting the contract to local jurisdiction may entail significant difficulties in terms of applying and proving the foreign law before local courts.

7.2 Will the courts in your jurisdiction recognise and enforce a judgment given against a company in New York courts or English courts (a "foreign judgment") without re-examination of the merits of the case?

Yes, courts in Colombia would recognise and enforce a foreign judgment. In order for foreign judgments to have the same enforceability as a local judgment, they should be first recognised by the Supreme Court of Justice, prior to being submitted for collection proceedings. This process is known as *exequatur*.

Exequatur shall be commenced before the Supreme Court of Justice in order to validate the foreign judgment if it complies with the following requirements established in article 606 of the Colombian General Process Code: (i) the judgment does not relate to "*in rem*" rights vested in assets that were located in Colombia at the time the proceeding was commenced; (ii) it does not contravene any laws deemed to be "public policy laws"; (iii) it is executed accordingly with the law of the country of origin, and it is presented as a duly legalised copy; (iv) it is a final award not subject to further challenges; (v) it does not refer to any matter upon which Colombian courts have exclusive jurisdiction; and (vi) it does not refer to a matter under pending litigation in Colombia or already ruled upon in Colombia. *Exequatur* also depends on diplomatic reciprocity. Once *exequatur* is granted, the interested party shall commence collection proceedings.

7.3 Assuming a company is in payment default under a loan agreement or a guarantee agreement and has no legal defence to payment, approximately how long would it take for a foreign lender to (a) assuming the answer to question 7.1 is yes, file a suit against the company in a court in your jurisdiction, obtain a judgment, and enforce the judgment against the assets of the company, and (b) assuming the answer to question 7.2 is yes, enforce a foreign judgment in a court in your jurisdiction against the assets of the company?

Filing a suit against a company in a court under Colombian jurisdiction may take approximately one to three weeks. Then, obtaining a first instance judgment may take approximately a year-and-a-half to two years, and a second instance ruling, if applicable, may take approximately six months to one year. Please bear in mind that agreeing on foreign law and submitting the contract to local jurisdiction may entail significant difficulties in terms of applying and proving the foreign law before local courts.

For the enforcement of a foreign judgment in a court in Colombia against the assets of a company, as mentioned in our answer to question 7.2, the Supreme Court has to recognise the judgment as a valid and enforceable decision under the *exequatur* proceeding. This proceeding may take from six months to one year. Once the foreign judgment is recognised, it would be considered an executive title. In order to enforce such title, a collection proceeding should be initiated. The duration of this proceeding may last around six months.

7.4 With respect to enforcing collateral security, are there any significant restrictions which may impact the timing and value of enforcement, such as (a) a requirement for a public auction, or (b) regulatory consents?

Mortgages require completing a court-mandated auction. The proceeds from such court-mandated auction would be delivered to the secured party. In case the auction is unsuccessful, the collateral would be delivered to the secured party.

In relation to pledges over movable assets, governed by Law 1676 of 2013, creditors may be entitled to directly claim or acquire property over pledged collateral through a direct payment mechanism, by a special execution of the collateral or by a judicial proceeding. This makes collateral over movable assets more efficient in terms of timing and value of enforcement.

7.5 Do restrictions apply to foreign lenders in the event of (a) filing suit against a company in your jurisdiction, or (b) foreclosure on collateral security?

No, there are no restrictions that exclusively apply to foreign lenders in the event of filing a suit against a company in Colombia, nor in the event of foreclosure on collateral security.

7.6 Do the bankruptcy, reorganisation or similar laws in your jurisdiction provide for any kind of moratorium on enforcement of lender claims? If so, does the moratorium apply to the enforcement of collateral security?

Under the commencement of a reorganisation proceeding, secured lenders are granted priority over any other unsecured creditors for the enforcement of collateral. This makes it possible for the secured lenders to enforce their security interest during the reorganisation proceedings, only if the collateral is not required for the operation of the debtor's business.

In case the enforcement of collateral security is over movable assets or real property affecting the operation of the debtor's business, any lawsuit for execution or any other collection proceeding for these assets against the debtor will not continue from the date of commencement of the reorganisation proceeding.

Pursuant to the initiation of a judicial liquidation proceeding, the debtor's encumbered property would be excluded from the liquidation mass for the benefit of the secured lenders. Therefore, if there is no reorganisation agreement and the company enters into liquidation, the creditors will be paid in their respective order of priority, regarding the preference of the specific collateral over which the secured parties had a security interest, provided that there are still available funds and assets after paying creditors with a higher priority.

7.7 Will the courts in your jurisdiction recognise and enforce an arbitral award given against the company without re-examination of the merits?

Courts in Colombia may recognise and enforce arbitral awards after a recognition proceeding is completed in accordance with the 1958 New York Convention requirements. If the arbitral tribunal has taken place in Colombia, this recognition is not required and the arbitral award may be enforced without any re-examination.

8 Bankruptcy Proceedings

8.1 How does a bankruptcy proceeding in respect of a company affect the ability of a lender to enforce its rights as a secured party over the collateral security?

Duly granted collateral security provides priority to the secured lenders upon the initiation of bankruptcy proceedings, in relation to the asset taken as collateral. Creditors who hold collateral security (after 2013, based on Law 1676 of 2013) over the debtor's movable assets can enforce this security (subject to the registration conditions) for the payment of the debt (during a reorganisation proceeding). Such prerogative (i.e. direct enforcement of the guarantees during the reorganisation proceeding) can only be used if the movable assets are not necessary for the development of the economic activity of the debtor. In case the security was not granted over movable assets subject to Law 1676 of 2013, such guarantees would have the traditional prerogatives for the protection of the creditor and the ranking: (1) first class: employment and tax obligations; (2) second class: creditors with a pledge granted in their favour; (3) third class: creditors with a mortgage granted in their favour; (4) fourth class: other tax-related obligations; and (5) fifth class: creditors that do not hold a security to secure the debtor's obligations.

8.2 Are there any preference periods, clawback rights or other preferential creditors' rights (e.g., tax debts, employees' claims) with respect to the security?

Law 1116 of 2006 establishes the clawback actions that are aimed at revoking or recharacterising the acts or transactions carried out by the debtor before an insolvency proceeding. Such acts or transactions must have adversely affected other creditors or the priority payment order. The suspect periods applicable for these type of actions is: (i) 18 months: payment of obligations and any act or transaction resulting in the transfer, granting or cancellation of liens or property rights of the debtor that diminish its patrimony, or leases that hinder the reorganisation proceedings. In this scenario, there must not be any evidence that the transferee or lessee acted in good faith; (ii) 24 months: gratuitous acts; and (iii) six months: amendments to the by-laws when such amendments diminish the debtor's patrimony in prejudice of the creditors or modify the liability of the shareholders of the debtor.

8.3 Are there any entities that are excluded from bankruptcy proceedings and, if so, what is the applicable legislation?

The following entities have special bankruptcy proceedings: entities supervised by the Superintendence of Finance (*Superintendencia Financiera*); entities supervised by the Superintendence of Solidarity Economy (*Superintendencia de Economía Solidaria*) that perform financial activities; State-owned entities; public utilities entities; and entities that provide health services (*Entidades Promoras de Salud* and *Instituciones Prestadoras de Servicios de Salud*).

8.4 Are there any processes other than court proceedings that are available to a creditor to seize the assets of a company in an enforcement?

Pursuant to Law 1676 of 2013, it is possible to have a special execution of the guarantee of a movable asset in opposition to a judicial execution, upon the agreement of the parties to such special execution or if the pledge meets certain requirements provided under Law 1676 of 2013. This procedure is different from a court proceeding. This type of enforcement can be carried out before a Chamber of Commerce or a Notary Public, depending on the agreement of the parties.

9 Jurisdiction and Waiver of Immunity

9.1 Is a party's submission to a foreign jurisdiction legally binding and enforceable under the laws of your jurisdiction?

Colombian parties are permitted to submit to a foreign jurisdiction. Please refer to our answer to question 7.1 above.

9.2 Is a party's waiver of sovereign immunity legally binding and enforceable under the laws of your jurisdiction?

Yes. A party's waiver of sovereign immunity is legally binding and enforceable.

10 Licensing

10.1 What are the licensing and other eligibility requirements in your jurisdiction for lenders to a company in your jurisdiction, if any? Are these licensing and eligibility requirements different for a "foreign" lender (i.e. a lender that is not located in your jurisdiction)? In connection with any such requirements, is a distinction made under the laws of your jurisdiction between a lender that is a bank *versus* a lender that is a non-bank? If there are such requirements in your jurisdiction, what are the consequences for a lender that has not satisfied such requirements but has nonetheless made a loan to a company in your jurisdiction? What are the licensing and other eligibility requirements in your jurisdiction for an agent under a syndicated facility for lenders to a company in your jurisdiction?

There are no licensing requirements for foreign lenders in Colombia. Nevertheless, under Colombian foreign exchange regulations, foreign indebtedness and foreign lenders must be registered with the Colombian Central Bank prior to the disbursements of funds under a lending transaction with a Colombian borrower. This registration only requires the filing of a form with the local bank that acts as intermediary for the Colombian borrower and takes between one and two days.

11 Other Matters

11.1 Are there any other material considerations which should be taken into account by lenders when participating in financings in your jurisdiction?

Colombian residents may obtain loans in foreign currency from non-residents to fund any activity or purpose. Prior to the disbursement, the foreign indebtedness must be reported by the Colombian resident to the Colombian Central Bank through a foreign exchange intermediary. Additionally, a copy of the relevant loan agreement has to be submitted to the foreign exchange intermediary, along with any other documents that the intermediary may request. Disbursement and payments completed under the loan must be timely reported to the Colombian Central Bank.

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Lloreda Camacho & Co., with more than 75 years' experience, is widely recognised as a leading Colombian law firm that provides integral legal services, especially to foreign companies doing business in Colombia.

Our Financial Service Practice is recognised for its active involvement with the banking and finance industry in Colombia. Partners and associates of the firm have been involved in some of Colombia's most relevant lending and secured finance transactions. Likewise, partners and associates participate, or have participated in the past, as members of the board of directors of listed companies, institutions of the capital markets and entities under the surveillance of the Superintendence of Finance of Colombia.

Our members are well regarded for their in-depth knowledge of Colombian and cross-border financial and securities regulation that impacts lending and secured finance transactions.

Costa Rica

Hernán Cordero Maduro

Cordero & Cordero Abogados

Ricardo Cordero B.

1 Overview

1.1 What are the main trends/significant developments in the lending markets in your jurisdiction?

Costa Rica's major trends are mainly related to the challenge that banks and financial entities are facing on issues such as fintech developments, online access to information and banking services, alternative lending platforms and a sound legal system. The market is urged to develop strategies to compete with PTP lending and crowdlending that are starting to generate a larger presence in the local market. In addition, new technologies are required to provide a higher standard, and effective and secure services to their customers. The traditional way of lending will definitely continue to dominate; however, it will have to start adapting to the efficiency of the digital era as well as other high-tech services. Regulatory entities are also going to be challenged to include these new fintech initiatives into the regulatory framework.

1.2 What are some significant lending transactions that have taken place in your jurisdiction in recent years?

The most significant lending transactions that have taken place in recent years have been focused on government financial aid programmes, as well as infrastructure and development loan agreements. Some of the major transactions are as follows: Inter-American Development Bank: a US$150 million-dollar loan to create a programme to prevent violence and social exclusion; a US$ 500 million-dollar loan to finance investment projects under a comprehensive programme that covers: mitigation of the impacts of climate change, sustainable economic growth and the promotion of regional integration through the "Regional Electricity Market" for generation, transmission and distribution of electricity, along with the already owed $1.483 million dollars; with BCIE, a US$340 million-dollar loan aimed at infrastructure modernisation; a US$50 million-dollar loan for the purchase, construction, improvement or expansion of housing, and the development of housing projects and sustainable housing for the middle class in Costa Rica; and a US$48 million-dollar loan to finance the Wholesale Regional Market Project in the Chorotega region.

2 Guarantees

2.1 Can a company guarantee borrowings of one or more other members of its corporate group (see below for questions relating to fraudulent transfer/financial assistance)?

Yes, it can. There should be no limitation on undertaking such act or contract in the company's corporate statute or by-laws. The Costa Rican Congress recently approved the *Minority Investor Protection Law*, which amends certain articles of the Code of Commerce, including article 32*ter* which refers to the requirement of corporate governance policies related to borrowing amongst members of its corporate group and giving specific protection to minority shareholders and investors, specifically when it comes to authorising borrowings of those related parties (a member of its corporate group or an independent third-party company). Along with this modification, and assuming that the corporate statute or by-laws establishes no limits, banks and financial entities should also request borrowers to comply with articles 1262 and 1263 of the Costa Rican Civil Code. In this regard, the borrower and/or the guaranteeing company must hold an extraordinary shareholders' meeting in which it analyses the terms and conditions of the transaction and authorises its legal representative (or any other person) to act on behalf of the company in order to authorise the guarantee for the borrowings of that related third party (a member of its corporate group or an independent third-party company).

2.2 Are there enforceability or other concerns (such as director liability) if only a disproportionately small (or no) benefit to the guaranteeing/securing company can be shown?

Pursuant to Costa Rican law, if a company intends to guarantee or secure related third-party borrowings, it is required to show or justify a benefit or expressly indicate that it must receive some kind of economic retribution. As indicated in question 2.1 above, in order to comply with corporate mandate rules, the company should analyse such retribution (whether small or significant) and expressly authorise its legal representative, by means of an Extraordinary Shareholders' Meeting, to represent the company in such act or contract.

2.3 Is lack of corporate power an issue?

Yes. All corporate undertakings must be executed by a legal representative of the company with sufficient power or else duly authorised – by the company's shareholders in a duly held shareholders' assembly – to execute the corresponding act or contract. If there is a lack of corporate power by the legal representative, then the act or contract may be rendered null and void. In addition, if a guarantee is subject to registration and the legal representative's power or authorisation is not duly recognised, then the guarantee will not be properly recorded and as a result the guaranteed party may be negatively affected. The corporate powers for legal representatives are governed pursuant to Title VIII of the Costa Rican Civil Code.

2.4 Are any governmental or other consents or filings, or other formalities (such as shareholder approval), required?

Under Costa Rican law, government filings or consents for granting guarantees are not required. With regards to shareholder approval, this will be subject to the limitations (if any) that the company and/or its legal representatives may have in its corporate statutes or by-laws. If there are no registered limitations to the corporate statutes or by-laws, shareholder approval is not required for guaranteeing its own borrowings, as long as the legal representative has the sufficient corporate power to execute the corresponding act or contract, but a Board of Directors Meeting must take place in compliance with article 32*ter* of the Commerce Code as indicated in question 2.1. Shareholder approval is required for guaranteeing the borrowings of its own shareholders and/or officers of the company and it is also required for borrowings of third parties. If there are registered limitations or restrictions on the corporate statutes or by-laws and/or limitations or restrictions on the appointment of legal representatives, then, as established in question 2.3 above, shareholders' approval is also required.

2.5 Are net worth, solvency or similar limitations imposed on the amount of a guarantee?

Under Costa Rican laws and regulations, this is not requirement. Nevertheless, upon granting a guarantee to a lender, the debtor should not be under a critical financial position that may be considered a technical insolvency affecting other lenders. Any acts or contracts executed under a technical insolvency may render those acts and contracts null and void. Upon the confirmation of a company's insolvency, acts or contracts executed up to six months prior to that confirmation (of insolvency) may be presumed null and void. Despite the above, local banks and/or financing entities that are subject to supervision by the Financial Entities Superintendence ("SUGEF") are obligated to comply with the SUGEF 1-05 Regulations whose purpose intends banks and financing entities to quantify its clients' credit capacity and related risks and forces them to establish the corresponding solvency safeguards.

2.6 Are there any exchange control or similar obstacles to enforcement of a guarantee?

No. There are no obstacles of this sort in order to enforce a guarantee. As a matter of fact, the Organic Law of the Costa Rican Central Bank ("*Ley Orgánica del Banco Central de Costa Rica*") specifically authorises private and public entities and/or individuals to enter into and execute private and public agreements using a foreign currency.

3 Collateral Security

3.1 What types of collateral are available to secure lending obligations?

Based on the definition of collateral as "property that is pledged as security against a debt or property subject to a security interest", the following are some types of collateral available to secure lending obligations in Costa Rica: mortgages or common mortgages ("*hipoteca*"); pledges ("*prenda*"); mortgage certificates ("*cédula hipotecaria*"); trust agreements ("*fideicomiso de garantía*"); and moveable guarantees ("*garantía mobiliaria*"). These types of collateral are explained in detail below.

3.2 Is it possible to give asset security by means of a general security agreement or is an agreement required in relation to each type of asset? Briefly, what is the procedure?

Yes, it is possible. In Costa Rica, trust agreements (also referred to as guarantee trust agreements) are usually used as a general security agreement in which real property (fee simple), concession rights, moveable assets, machinery, equipment and assignable rights can be transferred or assigned by the debtor or a third party (also referred to as the "Trustor") to a designated third party identified as a Trustee. The Trustee must hold the title of the assets or rights placed in trust as a collateral guarantee towards the lender (also referred to as the "Beneficiary") and must execute the trust agreement according to the instructions expressly indicated in such document. It is required that the instructions established in the trust agreement follow certain minimum due process rules of procedure.

The transfer of assets or rights to the Trustee can be executed by means of a private agreement, with the exception of registrable assets such as real property and certain vehicles and machinery which have to be transferred through a public deed ("*escritura pública*") executed exclusively by a Notary Public.

Upon the occurrence of an event of default by the debtor or Trustor under the trust agreement or the other loan documents, and failure to cure or at least take specific actions to cure the default, the Beneficiary must give written notice of the default to the Trustee and to the debtor or Trustor. If the debtor or Trustor fail to timely cure the event of default within the term granted in the trust agreement for this purpose, the Trustee must proceed to execute the auction of the trust estate.

3.3 Can collateral security be taken over real property (land), plant, machinery and equipment? Briefly, what is the procedure?

Yes. Collateral security can be taken over real property (fee simple) and moveable assets such as any type of plant, machinery, equipment, inventory, fungible goods as well as assignable rights.

The most common type of collateral security over real property is through a mortgage in which the debtor provides a property as a security to guarantee a specific loan. The lender and debtor agree on all terms and conditions, such as, but not limited to, mortgage grade, lender's name, debtor's name, loan amount, term, advance payment penalty, interest, loan currency, place of payment and the usual contractual clauses that will govern the loan and the mortgage. The mortgage lien – granted through a public deed before a Notary Public – is imposed over the registered real property and has to be recorded before the National Registry. The mortgage entry will be recorded on the property's ownership entry and will be publicly available.

Another type of security over real property is by means of a mortgage certificate. This security has the same legal force as a common mortgage. The National Registry issues the mortgage certificate that identifies the amount for which the certificate is issued and, unlike the common mortgage where there is an established lender, these certificates may be transferred by endorsement. In such cases, the mortgage certificate is also recorded as a lien on the property's ownership entry.

With regards to moveable assets, the most common type of collateral security is the pledge. All moveable assets that are legally subject to an auction and judicial persecution may be pledged to secure or guarantee a loan. Like mortgages, the pledge agreement must include certain terms and conditions such as: the lender's name; the debtor's name; the loan amount; the term; the advance payment penalty; the interest; the loan currency; the place of payment; and the characteristic contractual clauses that will govern the financing. The pledge lien imposed over registered or registrable moveable assets must be granted through a public deed before a Notary Public and recorded at the National Registry. Moveable assets which are non-registrable can also be granted as collateral pursuant to the Moveable Guarantee Law. This type of collateral is executed by means of a private document and recorded at the Moveable Guarantee Registry. This moveable guarantee provides more flexibility to the parties in order to be able to receive other types of moveable assets such as collateral and register that collateral in a verifiable registry. In addition to the above-indicated collateral security (mortgage and pledge), as indicated in question 3.2 above, another type of security is the trust agreement.

3.4 Can collateral security be taken over receivables? Briefly, what is the procedure? Are debtors required to be notified of the security?

Pursuant to Costa Rican law, a pledge collateral security can be taken over receivables as well as any other debt or credit. In order for the pledge to have legal value, it is required for the debtor to deliver or assign the receivable to the lender by way of a formal assignment, who is automatically appointed legal depositary (free of charge) of the receivable.

The lender is not allowed to dispose or take control of the collateral without the express consent of the debtor. Any agreement that violates the above will be considered null and void. It is customary to execute this pledge before a Notary Public in a public deed and/or a private document and register the security before the Moveable Guarantee Registry.

In addition, collateral security can be taken over these types of documents through a trust agreement. As established above, the receivable will be transferred to the Trustee who will execute the trust agreement according to the instructions expressly indicated in such document. This trust agreement is also recorded before the Moveable Guarantee Registry.

3.5 Can collateral security be taken over cash deposited in bank accounts? Briefly, what is the procedure?

Although a pledge collateral security can be taken over cash deposited in bank accounts in the same way as a receivable (see question 3.4 above), this is not common practice unless the lender is the same bank that grants the loan, manages the bank account and receives such security. The procedure is the same as that established above.

3.6 Can collateral security be taken over shares in companies incorporated in your jurisdiction? Are the shares in certificated form? Can such security validly be granted under a New York or English law governed document? Briefly, what is the procedure?

Yes, collateral security can be taken over shares in companies (whether a corporation ("*Sociedad Anónima*") or a limited liability company ("*Sociedad de Responsabilidad Limitada*")). The most common way to take security over shares is through a pledge, which has to be executed according to Costa Rican Law. In the case of corporations (which have shares in the form of certificates), in order for the pledge to have legal value, it is required for the debtor to deliver the share certificates to the lender, who is automatically appointed legal depositary (free of charge) of the share certificates. In the case of limited liability companies (the shares of which, called "quotas", are not in a certificated form), in order for the pledge to have legal value, it should be registered in the company's Quota Holders' Registry Book and the quota holders, through a quota holders' general assembly, should approve it.

The lender is not allowed to dispose or take control of the shares unless the established execution process is followed. In order for this execution to be valid, it should follow the established due process. Any agreement that violates the above due process is considered null and void. Nevertheless, in case there is a non-fulfilment on behalf of the debtor, the lender can enforce the security either through a court of law or through a private executor ("*corredor jurado*") and recover regular and delayed payment interest.

In addition, collateral security can be taken over shares through a trust agreement. As established above, the shares are transferred to the Trustee who will execute the trust agreement according to the instructions expressly indicated in such document.

3.7 Can security be taken over inventory? Briefly, what is the procedure?

Yes, collateral security can be taken over inventory. Inventory in Costa Rica is described as the moveable assets that a person or entity holds for its sale or lease in the due course of its normal business activity, such as raw materials and/or goods required for transformation into sellable assets. As indicated in question 3.3 above, any moveable asset that is legally subject to an auction and judicial persecution may be pledged to secure or guarantee. These types of assets may also be subject to the registration as a moveable guarantee under the special registry for these types of assets. Taking into consideration that inventory is a moveable asset, it is subject to a pledge collateral security as indicated above. In addition, inventory can be transferred to a trust agreement as established in question 3.2 above.

3.8 Can a company grant a security interest in order to secure its obligations (i) as a borrower under a credit facility, and (ii) as a guarantor of the obligations of other borrowers and/or guarantors of obligations under a credit facility (see below for questions relating to the giving of guarantees and financial assistance)?

Yes, a company can grant a security interest in order to secure both its obligations as a borrower under a credit facility and as a guarantor of the obligations of another borrower under a credit facility.

However, as established in question 2.1 above, in order to comply with corporate mandate rules established in articles 1262 and 1263 of the Costa Rican Civil Code, if the company grants a security interest as a guarantor of obligations of other borrowers, it is the guaranteeing company who must hold a Board of Directors Meeting to approve the transaction, and an Extraordinary Shareholders' Meeting in which it analyses the terms and conditions of the transaction and authorises its legal representative (or any other person) to guarantee the borrowings of a third party (a member of its corporate group or an independent third-party company) on its behalf.

3.9 What are the notarisation, registration, stamp duty and other fees (whether related to property value or otherwise) in relation to security over different types of assets?

In Costa Rica, the notarisation, registration, stamp duty and other fees are established pursuant to the following legislation: (i) National Registry Tariff Law No. 4564; (ii) Notarial Code No. 7764; and (iii) General Tariff for Fees for Law and Notary Public Professionals No. 36562-JP. In this regard, depending on the act or contract that is being executed, there is a standardised cost for the notarisation and registration of security. In all instances, if the act or contract has an estimated amount, such fees and stamps are proportional to the estimated amount. If for some reason the amount cannot be estimated, then the fees and stamps are going to be subject to the type of act or contract and type of security taken.

3.10 Do the filing, notification or registration requirements in relation to security over different types of assets involve a significant amount of time or expense?

The time required to execute a specific security will ultimately depend on the type of security. For example, registration of a mortgage, mortgage certificate or pledge over registered or registrable assets before the National Registry will take approximately eight (8) working days, taking into consideration that no formal or draft errors are identified by the National Registry.

With regards to expenses, it also varies on the type of security. In general, a security that is subject to registration (see question 3.11 below) will usually have filing and registration expenses that range between 0.60% and 2% of the estimated amount. Security that is not subject to registration will usually have filing and notification expenses that range between 0.15% and 1% of the estimated amount.

3.11 Are any regulatory or similar consents required with respect to the creation of security?

No specific regulatory consents are required with respect to the creation of security. However, some securities such as a mortgage or a pledge over registered/registrable assets require registration before the National Registry and, as a result, certain legal and regulatory requirements need to be met in order to register such collateral security. If these securities are not registered, then they are not going to be applicable to/enforceable on third parties. Nevertheless, consent is not required.

In addition, certain specific concessions (i.e. maritime zone concessions located under certain legal framework such as the *Polo Turísitico de Papagayo*) may require administrative consent with respect to the creation of security.

3.12 If the borrowings to be secured are under a revolving credit facility, are there any special priority or other concerns?

When dealing with revolving credit facilities, it is customary to guarantee the total amount of the facility with a type of secured collateral such as a mortgage, mortgage certificate, pledge or trust agreement. As established in question 8.1, creditors with these types of collateral have preference over non-secured creditors.

3.13 Are there particular documentary or execution requirements (notarisation, execution under power of attorney, counterparts, deeds)?

Pursuant to Costa Rican laws and general practice, most securities are executed through a public deed before a Notary Public. Notarised documents such as public deeds ("*escritura pública*") are subject to very detailed formalities established in Notarial Code No. 7764, and the Notary Public in charge of such execution must comply with documentary formalities and strictly follow corporate mandate rules (see questions 2.1 and 2.3 above). Notwithstanding the above, in recent years the trend has been to liberalise loans from these general formalities in order to grant more access to credit and financing possibilities.

4 Financial Assistance

4.1 Are there prohibitions or restrictions on the ability of a company to guarantee and/or give security to support borrowings incurred to finance or refinance the direct or indirect acquisition of: (a) shares of the company; (b) shares of any company which directly or indirectly owns shares in the company; or (c) shares in a sister subsidiary?

a) Shares of the company

The Costa Rican Code of Commerce establishes that a company cannot purchase shares of its own capital stock, unless the purchase is made with funds obtained from the company's gross profits from its legally approved balance. Thus, a company cannot finance or borrow money to purchase its own shares. As a result, a company is restricted from guaranteeing or supporting borrowings for the purchase of shares of the same company. In any case, a company is legally limited to 50% ownership of its own capital stock.

(b) Shares of any company which directly or indirectly owns shares in the company

Beside the restrictions explained in question 2.1, there is no specific prohibition or restriction for a company to guarantee and/or give security to support borrowings incurred to finance or refinance the direct or indirect acquisition of shares of any company which directly or indirectly owns shares in the company.

(c) Shares in a sister subsidiary

Beside the restrictions explained in question 2.1, there is no specific prohibition or restriction for a company to guarantee and/or give security to support borrowings incurred to finance or refinance the direct or indirect acquisition shares in a sister subsidiary.

5 Syndicated Lending/Agency/Trustee/Transfers

5.1 Will your jurisdiction recognise the role of an agent or trustee and allow the agent or trustee (rather than each lender acting separately) to enforce the loan documentation and collateral security and to apply the proceeds from the collateral to the claims of all the lenders?

When dealing with syndicated loans, Costa Rica will recognise the role of an agent who will hold the security in its name and on behalf of the remaining lenders. In this regard, it is important to clearly establish in the financing documents the role of the agent within the syndication and the rules that it must follow for the repayment of the loan, execution of the collateral, communication with the borrower, etc.

5.2 If an agent or trustee is not recognised in your jurisdiction, is an alternative mechanism available to achieve the effect referred to above which would allow one party to enforce claims on behalf of all the lenders so that individual lenders do not need to enforce their security separately?

A trust agreement is an alternative mechanism to that of the syndicated loan in which an agent is not recognised. In the trust agreement, the Beneficiaries are all the lenders, the Trustor is the borrower and/or that who provides the collateral, and the Trustee is a third party which receives the assets in trust and holds them (see question 3.2). Under Costa Rican law, there can be several Beneficiaries or lenders, as well as several Trustors or borrowers. Upon enforcement, the trust agreement must clearly stipulate who is responsible for executing the instructions under the trust agreement, which should always be a representative from the Trustee.

5.3 Assume a loan is made to a company organised under the laws of your jurisdiction and guaranteed by a guarantor organised under the laws of your jurisdiction. If such loan is transferred by Lender A to Lender B, are there any special requirements necessary to make the loan and guarantee enforceable by Lender B?

Assuming there is no limit to assign or transfer the loan from Lender A to Lender B, in order for the assignment or transfer to be valid and enforceable against the borrower, the borrower must be duly notified of the assignment of the loan. In addition, it is important to certify the date of the assignment through a public deed granted before a Notary Public ("*fecha cierta de la cesión*"). The assignment will be valid to third parties from the moment it is certified pursuant to the above and its recording before the Moveable Guarantee Registry.

6 Withholding, Stamp and Other Taxes; Notarial and Other Costs

6.1 Are there any requirements to deduct or withhold tax from (a) interest payable on loans made to domestic or foreign lenders, or (b) the proceeds of a claim under a guarantee or the proceeds of enforcing security?

According to the Costa Rican Income Tax Law, interest payments made by Costa Rican corporations or entities to foreign lenders or financial institutions, as a result of the repayment of any loan, are subject to a 15% withholding tax in Costa Rica. If such interest payment is made to a foreign lender that is part of a bank group that is supervised locally, there is a withholding tax that ranges from 5.5% to 15%. In addition, if such interest payments are made by Costa Rican corporations to multilateral banks, development banks and other non-profit financial entities, the above-indicated withholding tax does not apply.

6.2 What tax incentives or other incentives are provided preferentially to foreign lenders? What taxes apply to foreign lenders with respect to their loans, mortgages or other security documents, either for the purposes of effectiveness or registration?

Please see question 6.1.

6.3 Will any income of a foreign lender become taxable in your jurisdiction solely because of a loan to or guarantee and/or grant of security from a company in your jurisdiction?

Costa Rica has a territorial tax system; thus, if a foreign lender grants a loan from abroad to a company established in Costa Rica, income generated through that loan or guarantee or grant of security is not taxable in Costa Rica. Nevertheless, as established in question 6.1 above, remittance of interest may be subject to a withholding tax depending on the type of entity.

6.4 Will there be any other significant costs which would be incurred by foreign lenders in the grant of such loan/guarantee/security, such as notarial fees, etc.?

Generally, other than the established withholding tax indicated above, lenders do not assume any other cost in order to grant a loan and secure such loan in Costa Rica. As established in this document, most collateral is executed through a Notary Public in a public deed that is usually registered before the corresponding Section of the National Registry. These costs, which are more specifically referred to in question 3.10 above, are always assumed by the borrower.

6.5 Are there any adverse consequences to a company that is a borrower (such as under thin capitalisation principles) if some or all of the lenders are organised under the laws of a jurisdiction other than your own? Please disregard withholding tax concerns for purposes of this question.

No. There are no adverse consequences.

7 Judicial Enforcement

7.1 Will the courts in your jurisdiction recognise a governing law in a contract that is the law of another jurisdiction (a "foreign governing law")? Will courts in your jurisdiction enforce a contract that has a foreign governing law?

The courts in Costa Rica will always recognise a governing law in a contract and enforce that contract, unless the specific subject matter goes against a public policy law ("*ley de orden público*") that strictly prohibits such subjection to foreign law.

7.2 Will the courts in your jurisdiction recognise and enforce a judgment given against a company in New York courts or English courts (a "foreign judgment") without re-examination of the merits of the case?

Yes. However, the following requirements have to be met: (a) the foreign judgment has been legalised by means of the Apostille Treaty or through the Costa Rican Consulate and translated into Spanish; (b) the foreign courts followed the established due process; (c) the subject matter of the foreign judgment was not tried in a Costa Rican court; (d) there is no former adjudication or *res judicata* on the same case by a Costa Rican court; (e) the rights declared in the foreign judgment are subject to execution in the forum where the judgment was rendered; and (f) the rights declared in the foreign judgment do not go against Costa Rican public policy laws.

7.3 Assuming a company is in payment default under a loan agreement or a guarantee agreement and has no legal defence to payment, approximately how long would it take for a foreign lender to (a) assuming the answer to question 7.1 is yes, file a suit against the company in a court in your jurisdiction, obtain a judgment, and enforce the judgment against the assets of the company, and (b) assuming the answer to question 7.2 is yes, enforce a foreign judgment in a court in your jurisdiction against the assets of the company?

In general terms, if the default under a loan agreement has been well established, the lawsuit may be prepared and filed immediately. In order to obtain a judgment, assuming that the debtor raises procedural issues, an approximate timeframe would be six to ten months, minimum. In addition, enforcement of the judgment against the assets of the company can take an additional four months.

If we assume that all the legal requirements of the foreign judgment are in place, enforcement of such judgment in Costa Rica can take approximately between six and ten months.

7.4 With respect to enforcing collateral security, are there any significant restrictions which may impact the timing and value of enforcement, such as (a) a requirement for a public auction, or (b) regulatory consents?

Under Costa Rican law, some of the most important restrictions which impact the timing and value of enforcements is when it is required to serve notice of the commencement of the legal proceeding. This first step in an enforcement case can be cumbersome and delay the proceeding. Once this is executed in accordance with due process and the established notification laws, there are no consents that might delay the process. Notwithstanding the above, the most recent notification laws have significantly reduced the notification process, making the entire enforcement process less problematic.

7.5 Do restrictions apply to foreign lenders in the event of (a) filing suit against a company in your jurisdiction, or (b) foreclosure on collateral security?

No, there are no restrictions that apply to foreign lenders.

7.6 Do the bankruptcy, reorganisation or similar laws in your jurisdiction provide for any kind of moratorium on enforcement of lender claims? If so, does the moratorium apply to the enforcement of collateral security?

Upon declaration of bankruptcy, a moratorium on interest payments is declared to all borrowings not secured by means of a mortgage, mortgage certificate, pledge or similar. Although this moratorium does not apply to secured lenders, they cannot demand payment of the interest until the assets have been auctioned and proceedings paid.

7.7 Will the courts in your jurisdiction recognise and enforce an arbitral award given against the company without re-examination of the merits?

Yes. Please see question 7.2.

8 Bankruptcy Proceedings

8.1 How does a bankruptcy proceeding in respect of a company affect the ability of a lender to enforce its rights as a secured party over the collateral security?

Under Costa Rican law, lenders who have collateral security such as a perfected mortgage, pledge, mortgage certificate or trust agreement has a privileged right to enforce their security over unsecured creditors. The previous statement applies as long as the perfection of the security is not declared judicially fraudulent. In any event, any collection procedure that the lender executes will be brought before the same civil court where the bankruptcy proceeding is taking place.

Our law establishes a specific remedy ("*Acción Pauliana*") in order to request the nullity of any act or contract that has been executed up to two years prior to the declaration of bankruptcy which might affect unsecure creditors. In such case, the administrator of the bankruptcy has the power to begin such remedy action and the unsecured creditors may assist in such action.

8.2 Are there any preference periods, clawback rights or other preferential creditors' rights (e.g., tax debts, employees' claims) with respect to the security?

There are certain limited debts and obligations that have preference with respect to security. These have to be declared by a judge and the resulting liens are also known as legal mortgages which are established such as unpaid taxes, duly executed homeowners' association fees and some administrative charges. In this regard, these types of obligations have a priority with respect to the security.

8.3 Are there any entities that are excluded from bankruptcy proceedings and, if so, what is the applicable legislation?

There are only certain legal entities not subject to bankruptcy. These include the Government of Costa Rica, all public and autonomous institutions, local municipalities and State-owned banks.

8.4 Are there any processes other than court proceedings that are available to a creditor to seize the assets of a company in an enforcement?

Yes, there are several processes other than court proceedings available to seize the assets of a company during enforcement. Under most trust agreements in which assets are transferred to the Trustee to hold them in trust to secure an obligation, upon the occurrence of an event of default by the debtor or Trustor (according to the terms and conditions of the trust agreement or the other loan documents) and failure to cure or at least take specific actions to cure the default, the creditor – also referred to as the Beneficiary – must give written notice of the default to the Trustee and to the Trustor. If the Trustor fails to timely cure the event of default within the term granted in the trust agreement for this purpose, the Trustee must proceed to execute the auction of the Trust Estate. The trust agreement must establish the rules to hold a private auction of the entrusted assets and, if there are no offers to the auction, the Trustee has the power to transfer the entrusted assets to the creditor or Beneficiary.

For a pledge agreement in which certain moveable assets are taken as collateral security (see question 3.6 above), upon an event of default, the lender can enforce the security through a private executor ("*corredor jurado*") and recover regular and delayed payment interest.

In addition, if a security contains an arbitration or conciliation clause, this process may be followed in order to seize – with the consent of the borrower – assets of a company.

In any case, under Costa Rican law it is strictly prohibited for creditors to immediately seize the assets of a company upon non-fulfilment of the terms and conditions or an event of default, such as lack of payment. This immediate seizure is also known as "*pacto comisorio*". All documents and processes must refer to an execution process (whether private or public, judicial or non-judicial) where due process is followed. Any agreement that violates the above will be considered null and void.

9 Jurisdiction and Waiver of Immunity

9.1 Is a party's submission to a foreign jurisdiction legally binding and enforceable under the laws of your jurisdiction?

A party's submission to a foreign jurisdiction is legally binding and enforceable under the laws of Costa Rica, unless there is a public policy law ("*ley de orden público*") that strictly prohibits such avoidance of domestic laws.

9.2 Is a party's waiver of sovereign immunity legally binding and enforceable under the laws of your jurisdiction?

Generally, yes.

10 Licensing

10.1 What are the licensing and other eligibility requirements in your jurisdiction for lenders to a company in your jurisdiction, if any? Are these licensing and eligibility requirements different for a "foreign" lender (i.e. a lender that is not located in your jurisdiction)? In connection with any such requirements, is a distinction made under the laws of your jurisdiction between a lender that is a bank *versus* a lender that is a non-bank? If there are such requirements in your jurisdiction, what are the consequences for a lender that has not satisfied such requirements but has nonetheless made a loan to a company in your jurisdiction? What are the licensing and other eligibility requirements in your jurisdiction for an agent under a syndicated facility for lenders to a company in your jurisdiction?

Lenders – whether local or foreign – do not need to be licensed or authorised in Costa Rica or in their jurisdiction of incorporation in order to be able to grant loans in Costa Rica. In addition, there are no eligibility requirements for lenders to local entities or individuals. Nonetheless, as indicated in question 2.5 above, local banks and/or financing entities that are registered in Costa Rica and as a result are subject to supervision by SUGEF, are obligated to comply with certain provisions such as SUGEF 1-05, among other local supervision regulations.

11 Other Matters

11.1 Are there any other material considerations which should be taken into account by lenders when participating in financings in your jurisdiction?

Although foreign lenders do not require authorisation to grant loans in Costa Rica, they must have a corporate identification number ("*cédula jurídica*") in order to be identified as the lender in the financing documents to be registered at the corresponding Section of the National Registry. This corporate identification number is granted by the National Registry and it does not generate any legal or tax consequences.

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1 Overview

1.1 What are the main trends/significant developments in the lending markets in your jurisdiction?

The lending market in Croatia has experienced growth in corporate lending in 2017 due to increased liquidity and facilitated conditions. In the context of significant lending transactions, the Croatian lending market is small due to the inconsiderable number of larger companies and groups, some of them still government-owned.

Refinancing of the motorways loans in the amount of €2.5 billion is apparently being considered by a syndicate of local banks.

Major infrastructure projects (e.g. Peljesac Bridge – €357 million from the Cohesion Policy funds, LNG Terminal Krk – €101,40 million from the EU Connecting Europe Facility fund) are not financed by private loans but through EU funds, EIB, EBRD and the Croatian Bank for Reconstruction and Development programmes.

The sale of NPL's in Croatia hit a peak a few years ago. In the first quarter of 2017, 1 billion HRK (around €130 million) was sold at the purchase price of 26.9 per cent.

1.2 What are some significant lending transactions that have taken place in your jurisdiction in recent years?

Currently, all attention is focused on Agrokor, one of the largest retail joint stock companies in South East Europe. In the last few years, Agrokor acquired several large companies (e.g. acquisition of the biggest Slovenian retail chain Mercator valued at €500 million). However, subsequently, as a result of failed negotiations for debt restructuring through a syndicate loan from BNP Paribas, Credit Suisse AG, London Branch, Goldman Sachs International and J.P. Morgan Limited due to unfavourable terms, Agrokor's expansionary moves and cross-collateralisation within the group resulted with the possibility of bankruptcy. As a consequence, the parliament, on the basis of the Parmalat experience, adopted a law aimed at protecting the sustainability of business operations of systemically important companies ("Lex Agrokor"), allowing the government to appoint a trustee with the goal of reaching a settlement with creditors and eventually restructuring the company. In the restructuring procedure existing creditors were given the option of a roll-up structure allowing old credit to take priority on the basis of new credit. A total of €960 million of fresh capital was attracted with this structure. The faith of the company is still uncertain.

2 Guarantees

2.1 Can a company guarantee borrowings of one or more other members of its corporate group (see below for questions relating to fraudulent transfer/financial assistance)?

A company can guarantee borrowings of its members (downstream guarantees) only in accordance with the capital maintenance principle (see question 2.2), otherwise it is considered a prohibited distribution.

With regards to joint stock companies ("d.d."), any benefit of the company to the member can be granted only in the form of a dividend or reimbursement for non-monetary capital contributions on arm's length terms.

There are two exemptions from the prohibited distribution rule that refer to distributions on the grounds of company management agreement and transfer of profit and loss agreement ("venture contracts"), which are not considered prohibited distributions.

Downstream guarantees are allowed and can also be given as "additional obligation of the member" provided under the incorporation deed (not applicable for joint stock companies).

2.2 Are there enforceability or other concerns (such as director liability) if only a disproportionately small (or no) benefit to the guaranteeing/securing company can be shown?

An important principle of the corporate lending framework is the capital maintenance principle. It applies to limited liability companies ("d.o.o."), as well as to joint stock companies ("d.d."). Any distribution for the benefit of the member made contrary to arm's-length terms would be contrary to such principle and therefore prohibited. This means that any distribution (including all benefits and payments under the guarantee) is allowed if made in exchange for full value or with the obligation to return what is received. Establishment of an upstream guarantee would not be prohibited *per se* but only if this resulted with impairment of the company's assets according to the company's balance sheet (by payment, enforcement, etc.).

The consequence of such prohibited distribution is the obligation of the member to return the received benefit or its personal liability for damage to the company and its creditors ("lifting of the corporate veil"). If the company cannot recover the loss from the member which received the benefit or from the directors, other members may be liable for payment if prohibited distribution disables the company to settle obligations towards the creditors.

Maintenance of the company's capital is the obligation of the management and prohibited guaranteeing/securing may incur personal liability of the directors if a company's assets are impaired due to lack of due care of a prudent businessman.

2.3 Is lack of corporate power an issue?

Any limitations of management (specific conditions, consents, restrictions regarding the type of agreements) to represent the company do not affect the validity of agreements with third parties regardless whether such limitation is visible from the Company Register.

2.4 Are any governmental or other consents or filings, or other formalities (such as shareholder approval), required?

In general, no governmental or other consents are required for granting guarantees. However, the consent of the Ministry of Finance is required if the Republic of Croatia is the guarantor i.e., security provider. Possible limitation or special authorisation could be required under the provisions of incorporation deed or internal decisions of the company.

2.5 Are net worth, solvency or similar limitations imposed on the amount of a guarantee?

See question 2.2 regarding the capital maintenance principle.

2.6 Are there any exchange control or similar obstacles to enforcement of a guarantee?

There are no exchange controls or similar obstacles to enforcement of a guarantee.

3 Collateral Security

3.1 What types of collateral are available to secure lending obligations?

For the purpose of securing lending obligations, available types of collateral, according to Croatian law, are as follows:

- Security over receivables:
  - a pledge; and/or
  - a security assignment ("fiduciary transfer").
- Security over movables:
  - a pledge;
  - a mortgage ("registered security"); and/or
  - a fiduciary transfer of ownership.
- Security over immovables:
  - a mortgage; and/or
  - a fiduciary transfer of ownership.
- Security over shares:
  - a share pledge; and/or
  - a security assignment.

3.2 Is it possible to give asset security by means of a general security agreement or is an agreement required in relation to each type of asset? Briefly, what is the procedure?

Since the requirements and the procedure for creation, registration and enforcement of security are different for different types of assets, separate agreements for each type are usually required. Croatian law allows the creation of "a floating security" over generic movables. Such security must be sufficiently identifiable since a floating security over all assets of the debtor is not possible.

3.3 Can collateral security be taken over real property (land), plant, machinery and equipment? Briefly, what is the procedure?

There are two types of securities over immovables: (i) mortgage and (ii) fiduciary transfer of ownership. Both securities are established by security agreement in the form of notarial deed and registration in the Land Registry. Mortgages ("*hipoteka*") are a more common form of security and are an accessory to the underlying receivable, which means they cannot be transferred independently of the receivable they secure. The difference between the mortgage and the fiduciary transfer is that the title of the property does not transfer to the mortgagee, unlike the fiduciary ownership where the ownership is limited and conditional upon the settlement of the secured receivable.

A mortgage over land plot may exceptionally be extended to movables located on the land plot, such as plant, livestock, machinery and equipment that serve the economic purpose of the building on the land plot.

For security over machinery and equipment please see question 3.7.

3.4 Can collateral security be taken over receivables? Briefly, what is the procedure? Are debtors required to be notified of the security?

Security in the form of a pledge or security assignment (fiduciary transfer of rights) may be established over receivables. Uniform rules apply to security over all rights, including receivables.

A pledge over receivables is established by two constitutive elements: (i) transfer of the right and (ii) notification to the debtor. The registration of the security in the Register of Judicial and Notarial Securities Over Movables and Rights does not exclude the obligation of notifying the debtor.

The security assignment is based on the rules governing assignment ("*cessio*") of rights in general. The security becomes perfect when the agreement is concluded. In such case, the notification to the debtor is required, but the assignment remains valid even if the debtor is not notified since the notification is not a constitutive element. However, if the debtor was not notified and the security over receivable is not registered or evident from the Register, the debtor is entitled to discharge his obligation by making the payment to the assignor.

Security over rights may be created either independently between the parties or with the involvement of the court or the notary public in the security proceeding. In the case of notarial or judicial security, the security is registered in the Register of Judicial and Notarial Securities Over Movables and Rights.

3.5 Can collateral security be taken over cash deposited in bank accounts? Briefly, what is the procedure?

Cash deposited in bank accounts is considered a receivable against the bank account. However, specific rules apply to financial securities over receivables against bank accounts (cash deposits, credit receivables and financial instruments). The security agreement must be in written form.

There are two types of securities: (i) pledge and (ii) financial security transfer. The pledge entitles the beneficiary to use and dispose of the deposited cash of the security provider with the obligation to return or replace the security at the latest on the due date for the performance of the obligation covered by the security. The beneficiary of the security transfer has an unlimited right to use and dispose of the deposited cash. The security may be enforced directly by the beneficiary by sale, compensation or seizure.

3.6 Can collateral security be taken over shares in companies incorporated in your jurisdiction? Are the shares in certificated form? Can such security validly be granted under a New York or English law governed document? Briefly, what is the procedure?

Collateral security can be created over shares of joint stock companies ("d.d.") and limited liability companies ("d.o.o.").

(i) Joint stock companies ("d.d.") have shares that can be in dematerialised or in certificated form (in theory only but not used over the last several years). Security over certificated shares in bearer form is from the legal perspective considered as security over movables and is created by the security agreement and the transfer of possession.

In the case of dematerialised shares, the creation of security requires registration of the security in the Central Depository & Clearing Company (CDCC). If dematerialised shares are not registered in the CDCC, security is created by assignment ("*cessio"*).

(ii) Security over shares of a limited liability company is created solely by an agreement that does not require notarial form. Registration in the book of shares is required but only has the function of publicity.

The beneficiary of the security does not acquire the membership in the company and is only entitled to obtain profit without the right to vote.

Pursuant to Croatian conflict of laws rules, security over shares can be granted based on foreign documents; however, Croatian law applies to the enforcement of such security.

3.7 Can security be taken over inventory? Briefly, what is the procedure?

Security over movables may be established as: (i) a pledge with the transfer of possession; (ii) a mortgage; or (iii) fiduciary transfer of ownership. For the purpose of this question, movables such as vessels and aircrafts are not considered inventory.

Security over movables can also be created in the security proceeding before courts or notary public (see question 3.4).

Securities over movables are not very common in Croatia.

3.8 Can a company grant a security interest in order to secure its obligations (i) as a borrower under a credit facility, and (ii) as a guarantor of the obligations of other borrowers and/or guarantors of obligations under a credit facility (see below for questions relating to the giving of guarantees and financial assistance)?

A company can grant a security interest in order to secure (i) its own obligations as a borrower and (ii) as a guarantor of the obligations of other borrowers/guarantors under a credit facility. The latter being only if not contrary to limitations provided by Croatian company law (question 2.1 and 2.2).

3.9 What are the notarisation, registration, stamp duty and other fees (whether related to property value or otherwise) in relation to security over different types of assets?

With regard to creating security, there are three possible fees depending on the type of assets (i) fees of the notary public (when the security agreement is in the form of notarial act), (ii) registration fees (land registry, notarial and judicial registry, vessel's registry) and (iii) security proceeding fees if the security is created with the involvement of the court or the notary. The notary fees are subject to the value of the security object and prescribed by the notary's tariff. Notary fees can be significant, while the registration fees are usually minor.

3.10 Do the filing, notification or registration requirements in relation to security over different types of assets involve a significant amount of time or expense?

Filing, notification or registration requirements do not generally involve a significant amount of time (for expenses, see question number 3.9). Registration in the land registry may take longer, depending on the court handling the registration.

3.11 Are any regulatory or similar consents required with respect to the creation of security?

In general, there is no consent required with respect to the creation of security. The consent may be required for creation of security over shares if provided so by the company's deed of incorporation.

3.12 If the borrowings to be secured are under a revolving credit facility, are there any special priority or other concerns?

There is no special priority or specific conditions in case the borrowings are secured under a revolving credit facility.

3.13 Are there particular documentary or execution requirements (notarisation, execution under power of attorney, counterparts, deeds)?

The security agreement should be in the form of a notarial deed or a notarised private document in order to be an enforceable document. It is important that the security agreement contains an *exequendi* clause – consent of the security provider to direct enforcement. Upon the request of the security beneficiary, the notary public issues an enforceability confirmation on the security agreement confirming that the requirements for enforcement are fulfilled.

Regarding the authorisation for any action with regards to creation or the enforcement of the security (except in the court proceeding), a special power of attorney is required and in some cases the power of attorney should be certified by the notary public or accompanied by an apostille.

4 Financial Assistance

4.1 Are there prohibitions or restrictions on the ability of a company to guarantee and/or give security to support borrowings incurred to finance or refinance the direct or indirect acquisition of: (a) shares of the company; (b) shares of any company which directly or indirectly owns shares in the company; or (c) shares in a sister subsidiary?

(a) Shares of the company

With regard to joint stock companies, Croatian law explicitly provides that an agreement under which the company grants financial assistance to third parties in form of advance payment, security or loan for acquisition of its own shares is invalid. This does not apply to (i) operation of credit and financial institutions and (ii) financial assistance for acquisition of shares by the employees of the company.

There is no explicit provision on financial assistance for acquisition of shares of the limited liability company; however, the general rule of capital maintenance would apply.

(b) Shares of any company which directly or indirectly owns shares in the company

Provision on the invalidity of the agreement explicitly applies to financial assistance for acquisition of shares of the company that owns shares of the company providing financial assistance.

(c) Shares in a sister subsidiary

Provision on the invalidity of the agreement explicitly applies to financial assistance for acquisition of shares of the sister company.

5 Syndicated Lending/Agency/Trustee/Transfers

5.1 Will your jurisdiction recognise the role of an agent or trustee and allow the agent or trustee (rather than each lender acting separately) to enforce the loan documentation and collateral security and to apply the proceeds from the collateral to the claims of all the lenders?

Croatian banks, together with local or foreign banks, have been providing syndicated loans. So in principle yes agents are recognised by practice, although not closely regulated, from the bylaws regulating the credit institutions and official opinions from the Tax Authority, the role of an agent (one of the lenders) is to coordinate all transaction between the lenders and the borrowers, as well as running administrative operations and balance sheets for all lenders. Furthermore, it arises that the agent acts in the name and for the account of other lenders and that he is authorised to collect payments on behalf of all lenders from the borrower. In the case where creditors are joint and sever, each of the creditors could enforce the whole claim. The agent being the debtor itself could initiate the proceeding, however, success of possible objections from the borrower is uncertain since there is no court practice. Finally, Croatian law does not recognise the concept of trust.

5.2 If an agent or trustee is not recognised in your jurisdiction, is an alternative mechanism available to achieve the effect referred to above which would allow one party to enforce claims on behalf of all the lenders so that individual lenders do not need to enforce their security separately?

According to the Croatian Obligations Act, when there is more than one creditor of one claim, if such creditors are joint and sever, each of them is entitled to enforce the whole claim and redistribute the collected amount among the creditors. With respect to the secured claim, when security is registered in public registries, only the registered creditor could enforce the security.

5.3 Assume a loan is made to a company organised under the laws of your jurisdiction and guaranteed by a guarantor organised under the laws of your jurisdiction. If such loan is transferred by Lender A to Lender B, are there any special requirements necessary to make the loan and guarantee enforceable by Lender B?

For the loan and guarantee to be enforceable, the loan should be assigned either by (a) assignment of claim when one claim is transferred from one creditor to another, or by (b) transfer of the contract when all rights and obligations from the contract are transferred from one party to the new party. With respect to the guarantee, when the claim is (a) assigned – all rights including the rights from the guarantee are transferred to the new creditor and enforceable by the new creditor. With respect to transfer of the contract (b), the guarantees would also be transferred and enforceable unless the guarantor objects to guarantee the creditor.

6 Withholding, Stamp and Other Taxes; Notarial and Other Costs

6.1 Are there any requirements to deduct or withhold tax from (a) interest payable on loans made to domestic or foreign lenders, or (b) the proceeds of a claim under a guarantee or the proceeds of enforcing security?

Interest paid to foreign lenders (not natural persons) in Croatia are subject to withholding tax. The obligator of withholding tax is the payee – the borrower. Exceptionally, interest paid on loans given by foreign banks or other financial institutions are not subject to withholding tax. Payment of withholding tax by foreign entities is regulated under bilateral treaties or the domestic Income Tax Act. If a bilateral treaty regarding the avoidances of double taxation exists, such treaties would regulate the taxation of interest payable on loans. Depending on each treaty, withholding tax can be reduced or not paid at all. In each case, the certificate issued and notarised by a competent foreign body should be obtained and filed with the tax authority in order that such tax obligation is deduced. If there is an absence of treaties regulating avoidance of double taxation, interest payable on loans are subject to 15 per cent withholding tax. Regarding domestic lenders, there are no special provisions. The profit from the interest, together with the total annual income, is taxed according to annual income tax.

There are no special requirements to deduct or withhold tax from (b) proceeds of a claim under a guarantee or the proceeds of enforcing security.

6.2 What tax incentives or other incentives are provided preferentially to foreign lenders? What taxes apply to foreign lenders with respect to their loans, mortgages or other security documents, either for the purposes of effectiveness or registration?

There are no special taxes or other incentives provided preferentially to foreign lenders. No taxes apply to foreign lenders with respect to loans, mortgages or other security documents for the purposes of effectiveness or registration. With regards to fees for registration, please see question 3.9.

6.3 Will any income of a foreign lender become taxable in your jurisdiction solely because of a loan to or guarantee and/or grant of security from a company in your jurisdiction?

A foreign lender would not be taxable in Croatia solely because of a loan or guarantee or grant of security from a company in Croatia.

6.4 Will there be any other significant costs which would be incurred by foreign lenders in the grant of such loan/guarantee/security, such as notarial fees, etc.?

Please see question 3.9.

6.5 Are there any adverse consequences to a company that is a borrower (such as under thin capitalisation principles) if some or all of the lenders are organised under the laws of a jurisdiction other than your own? Please disregard withholding tax concerns for purposes of this question.

In general, there should be no adverse consequences to borrowers in the case where all or some lenders are foreigners.

7 Judicial Enforcement

7.1 Will the courts in your jurisdiction recognise a governing law in a contract that is the law of another jurisdiction (a "foreign governing law")? Will courts in your jurisdiction enforce a contract that has a foreign governing law?

Croatian courts would recognise a foreign governing law in a contract. The parties are free to incorporate a law of any jurisdiction since freedom of choice is one of the cornerstones of conflict of law rules legislation. According to the Conflict of Rules Act, the contract is governed by a law chosen by the parties where such choice is not limited to EU law or any conventions. However, if such law is contrary to the Constitution, it would not be recognised. Regulation (EC) No 593/2008 of the European Parliament and of the Council of 17 June 2008 on the law applicable to contractual obligations (Rome I) is also applied.

Croatian courts, if found to be competent, would enforce a contract that has a foreign governing law provided that provisions of law are not contrary to the Constitution and *ordre public*.

7.2 Will the courts in your jurisdiction recognise and enforce a judgment given against a company in New York courts or English courts (a "foreign judgment") without re-examination of the merits of the case?

Different rules apply for recognition of foreign judgments, depending on whether a judgment was given by a court of the EU or a non-EU Member State:

Recognition of a judgment given by court of EU Member State (e.g. English court) is regulated by Regulation (EU) no 1215/2012 of the European Parliament and of the Council of 12 December 2012 on jurisdiction and the recognition and enforcement of judgments in civil and commercial matters (Brussel I) which regulates that a judgment given in an EU Member State shall be recognised in other EU Member States without any special procedure being required, i.e. without re-examination of the merits of the case.

Recognition of a judgment given by court of non-EU Member State (e.g. New York court) is regulated by the Conflict of Rules Act and such judgments are recognised without re-examination of the merits. In the procedure of recognition before the court, the court will only check whether formal requirements are fulfilled, i.e:

- if such judgment was final in the state of origin;
- whether there is exclusive jurisdiction of Croatian courts;
- whether there is already an existing judgment (*res judicata*);
- whether the judgment is contrary to the Constitution; and
- whether there is reciprocity between the origin state and Croatia with respect to recognition of foreign judgments.

7.3 Assuming a company is in payment default under a loan agreement or a guarantee agreement and has no legal defence to payment, approximately how long would it take for a foreign lender to (a) assuming the answer to question 7.1 is yes, file a suit against the company in a court in your jurisdiction, obtain a judgment, and enforce the judgment against the assets of the company, and (b) assuming the answer to question 7.2 is yes, enforce a foreign judgment in a court in your jurisdiction against the assets of the company?

The timeframe for obtainment and enforcement of a judgment depends on certain factors such as the complexity of the case and the promptness of the court, which again depends on the workload of the court, and finally the type of assets – whether bank accounts, moveable or immovable property are enforced. For obtainment and enforcement of the judgment, (a) judgment could be obtained, on average, within three years and then enforced within months (when enforcing bank accounts with sufficient funds) to three years (when enforcing immovables). This would mainly depend on whether an appeal was logged against the first instance judgment which can prolong the process for approximately one year. For (recognition) and enforcement of a foreign judgment, (b) it could also take form a few months to a few years, again, depending on the type of assets, financial situation of the debtor and workload of the court.

7.4 With respect to enforcing collateral security, are there any significant restrictions which may impact the timing and value of enforcement, such as (a) a requirement for a public auction, or (b) regulatory consents?

Significant restrictions that may impact the timing and value of enforcement are (a) public auctions – which are mandatory in enforcement proceedings (one to two public auctions for immovables and one auction for moveable property). Croatian law does not propose any (b) regulatory consents with respect to enforcement of collateral security.

7.5 Do restrictions apply to foreign lenders in the event of (a) filing suit against a company in your jurisdiction, or (b) foreclosure on collateral security?

No special restrictions apply to foreign lenders in the event of (a) or (b). However, where there is no reciprocity, i.e. treaties between the country of a seat of a foreign lender and Croatia regarding proceeding costs, it could be requested that the Plaintiff-foreign lender gives security for payment of proceeding costs. Also, if such Plaintiff-foreign lender does not have seat or representation (e.g. attorney) in Croatia, they will have to appoint a delivery agent to be served with court documents during the proceeding.

7.6 Do the bankruptcy, reorganisation or similar laws in your jurisdiction provide for any kind of moratorium on enforcement of lender claims? If so, does the moratorium apply to the enforcement of collateral security?

The Bankruptcy Act provides that once pre-bankruptcy proceedings or bankruptcy proceedings are opened, no enforcement proceedings are allowed against the debtor, up to the closure of such proceeding. The proceedings are deemed to be opened once the decree that the proceeding is opened is published on an electronic bulletin board of the court. Moratorium does not apply to enforcement of collateral security if such debtor has the right of separate security (e.g. mortgage on real-estate registered in Land Registry).

Also, in 2017, a new Act on the extraordinary management procedure in companies of systemic importance for the Republic of Croatia (*Lex Agrokor*), i.e. companies that employ more than 5000 workers and have over 1 billion Eur of debt entered into force. The same rules apply as in the (pre) bankruptcy proceeding with regards to moratorium and secured claims.

7.7 Will the courts in your jurisdiction recognise and enforce an arbitral award given against the company without re-examination of the merits?

Recognition of foreign arbitral awards is regulated by the Arbitration Act. Croatian courts would recognise and enforce arbitral awards given against the company without re-examination of the merits, subject to the arbitration award not being contrary to the public order and that there is no exclusive jurisdiction of Croatian courts. Croatia is also a party to the Convention on Recognition and Enforcement of Foreign Arbitral Awards (The New York Convention 1958).

8 Bankruptcy Proceedings

8.1 How does a bankruptcy proceeding in respect of a company affect the ability of a lender to enforce its rights as a secured party over the collateral security?

In (pre-) bankruptcy proceedings, creditors with secured claims have preferential status, i.e. they can use their right of "separate settlement". Such creditors have the right for their claim to be reimbursed from the proceeds of sale of their collateral, whereas other creditors with non-secured claims can only be reimbursed from the proceeds of sale from the remainder of other unencumbered assets.

8.2 Are there any preference periods, clawback rights or other preferential creditors' rights (e.g., tax debts, employees' claims) with respect to the security?

Bankruptcy trustees, as well as the creditors, may challenge legal actions taken prior to the opening of the bankruptcy proceedings if such actions are deemed to disrupt the balanced settlement of the creditors, or legal actions that benefit certain creditors (clawback), as follows:

i. actions taken three months prior to filing a motion for opening a bankruptcy proceeding or after, by which action a creditor was able to settle/secure his claim, can be challenged if such action was taken in a time when the debtor was insolvent and if the creditor was aware of his insolvency or was aware that the bankruptcy proceeding was opened;
ii. actions which allows one creditor to settle/secure a claim that he is not entitled to/claim that is not due, if such action was taken in the last month before filing a motion for opening a bankruptcy proceeding or was taken two or three months before filing such motion if the debtor was insolvent or when the creditor was aware that such action would damage other creditors;
iii. actions which directly damage the creditors if such actions were taken three months prior to filing motion for opening a bankruptcy proceeding and if the debtor was insolvent and the other party was aware of such insolvency or if it was taken after – if the other party was aware of the debtor`s insolvency or that the motion was filed;
iv. actions taken by the debtor in the last 10 years prior to filing a motion for opening the bankruptcy proceeding or after, with the purpose of damaging the creditors if the other party was aware of such intentions of the debtor;
v. debtor's actions without compensation taken within four years prior to filing a motion that the bankruptcy proceeding is opened; and
vi. actions by which the shareholder's claim for loan replacing the share capital or other similar claim is secured, when such action is taken five years prior to filing a motion that the bankruptcy proceeding is opened or after or giving a guarantee for the claim if such action is taken one year before filing the motion that bankruptcy proceedings is opened.

Employee's claims are considered to be "first class I claims" and have priority over all other claims.

8.3 Are there any entities that are excluded from bankruptcy proceedings and, if so, what is the applicable legislation?

Bankruptcy and pre-bankruptcy proceeding cannot be initiated against the Republic of Croatia, funds financed by Republic of Croatia, Croatian Health Insurance Fund, Croatian Pension Insurance Institute and local and regional self-governing units.

8.4 Are there any processes other than court proceedings that are available to a creditor to seize the assets of a company in an enforcement?

Assets are normally seized in court proceedings.

9 Jurisdiction and Waiver of Immunity

9.1 Is a party's submission to a foreign jurisdiction legally binding and enforceable under the laws of your jurisdiction?

A party's submission to a foreign jurisdiction is legally binding unless there is exclusive jurisdiction of Croatian courts for such submission according to the Croatian legislature. According to the Croatian Conflict of Rules Act, the parties can choose the forum if at least one of the parties is a foreigner or a foreign company and there is no exclusive jurisdiction of the Croatian court. Also, according to Article 25 of Brussels I Regulation, the parties can choose, in a written agreement, that a certain court of a EU Member State has jurisdiction and such court would be competent unless the agreement is null and void as to its substantive validity under the law of that Member State.

9.2 Is a party's waiver of sovereign immunity legally binding and enforceable under the laws of your jurisdiction?

A party's waiver of sovereign immunity is legally binding and enforceable. Such waiver should always be given explicitly.

10 Licensing

10.1 What are the licensing and other eligibility requirements in your jurisdiction for lenders to a company in your jurisdiction, if any? Are these licensing and eligibility requirements different for a "foreign" lender (i.e. a lender that is not located in your jurisdiction)? In connection with any such requirements, is a distinction made under the laws of your jurisdiction between a lender that is a bank *versus* a lender that is a non-bank? If there are such requirements in your jurisdiction, what are the consequences for a lender that has not satisfied such requirements but has nonetheless made a loan to a company in your jurisdiction? What are the licensing and other eligibility requirements in your jurisdiction for an agent under a syndicated facility for lenders to a company in your jurisdiction?

Loans can be given by a financial institution ("*kredit*") or by any other natural or legal person ("*zajam*"), whereas the differences between the two, other than the aforementioned entity authorised to give such a loan, are: a *kredit* agreement should always be in writing, the object of the loan is always money and interest always apply, while a *zajam* agreement is a non-formal contract, the object of the contract can be money or other fungible object, with or without interest. Therefore, under Croatian laws, distinction is made between a lender that is a financial institution and a lender that is a non-financial institution. Pursuant to Croatian banking and financing laws, a bank should obtain a special licence for operating as a bank from the Croatian National Bank. There are no special licensing requirements for other (foreign) legal and natural persons to give loans.

With respect to foreign lenders, i.e. foreign financial institution, they can give loans in Croatia if such financial institutions are incorporated within the EU and have a subsidiary in Croatia or are authorised to directly operate as financial institutions in Croatia or financial institutions from other countries that have a subsidiary in Croatia.

A kredit loan given by a lender without the proper licence would be considered null and void, while the lender or their management could be punished with fines for an offence, depending of each case.

Croatian law does not specifically regulate an agent under a syndicated facility. Consequently, no licensing and eligibility requirements apply.

11 Other Matters

11.1 Are there any other material considerations which should be taken into account by lenders when participating in financings in your jurisdiction?

Most of the relevant and general issues have been covered in the chapter. Possible material consideration that should be taken into account depends on a broad variety of circumstances in each case. Some general considerations while participating in financing in Croatia is that the lending is regulated by the Croatian Obligation Act and by an Act on financial operations and pre-bankruptcy settlement. Both acts also regulated the interest rates. Interest rates depend on the reference rate set out by the Croatian National Bank.

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Macesic & Partners is one of the oldest Croatian law firms operating through two offices in Zagreb and Rijeka, covering the entire territory of Croatia. It has developed from the partnership of Miroljub Macesic and Anamari Laskarin. The practice of Miroljub Macesic was combined (when he took over) in 1993 with the practice of Georgije Ivkovic who acted as an attorney-at-law from 1970.

The Offices employ six lawyers, all of whom speak English, three speak Italian and one French. The services specialise in main business activities: corporate; banking and financing; transport; insurance; energy; real estate; intellectual property; and litigations and arbitrations. The attorneys are experienced in running complex, multi-disciplinary and multimillion matters with international elements. The offices provide specific knowledge on conflict of law rules, recognition and enforcement of foreign judgments and arbitration awards, security of claim measures, ascertainment and preservation of facts and evidences and similar expertise serving the clients by meeting their high requests and providing always a high-quality service. The firm is a member of several professional and experts' organisations and associations and it is listed by all major professional listings. It regularly assists as a local correspondent to numerous international law firms.

Cyprus

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1 Overview

1.1 What are the main trends/significant developments in the lending markets in your jurisdiction?

Cyprus has come a long way since the collapse and virtual financial meltdown of its banking sector in March of 2013. The MoU between Cyprus and the Troika paved the way for the recovery of the Cypriot banking and financial system by focusing on certain key objectives, including the implementation of structural reforms aimed at enhancing competitiveness and sustainable and balanced growth.

Five years on, the measures continue to make a positive impact: deposits have stabilised and official data released by the Cyprus Statistical Service confirms that the growth rate for Cyprus in the fourth quarter of 2017 stood at 4.0%, marking the highest growth in the economy since the second quarter of 2008. Although record-high levels of non-performing loans (NPLs) (which still comprise 43% of total loans) are experiencing a slow, albeit marked, downturn, they continue to pose a problem for the Cyprus banking system. On her most recent visit to Cyprus, the ECB's chief supervisor, Daniele Nouy, stated that "the efforts made by the Cypriot banks over the last few years to tackle the challenges they face are commendable and measurable progress has indeed been made, but additional and persistent efforts are still required to ensure further progress in the reduction of NPLs".

The high level of NPL's in Cyprus is attributed, in the main, to structural and/or legal impediments (such as restrictions on the sale of certain types of collateral). That said, the outlook is positive with proposed reforms in the pipeline to address and alleviate the situation both on a European and domestic level. The European Commission is currently taking a series of structural measures in order to reduce NPLs on a pan-European level in an aim to bring further uniformity across banks in the EU; on a domestic level, the proposed enactment of securitisation laws are expected to further assist in de-leveraging and alleviating the high level of NPLs on banks' balance sheets. In addition, it is expected that the current plans by the newly elected government to create a national asset management company will further facilitate the reduction of NPLs in the Cypriot banking system.

1.2 What are some significant lending transactions that have taken place in your jurisdiction in recent years?

Increased availability of debt leverage deals has had a significant impact on transaction volumes. Generally, however, new lending remains at a low level.

2 Guarantees

2.1 Can a company guarantee borrowings of one or more other members of its corporate group (see below for questions relating to fraudulent transfer/financial assistance)?

Generally speaking, a Cypriot company can provide guarantees for the borrowings of one or more members of its group, if (i) there is commercial benefit in it doing so (whether direct or indirect), and (ii) it is permitted to do so under its constitutional documents.

By way of example, it may be argued that a parent company granting a downstream guarantee to its subsidiary to secure the latter's borrowing obligations towards a third party has commercial benefits not only for the wider group but also for the parent company itself; especially where, as a result of the giving of the guarantee, the subsidiary can sustain upward profitability, and in turn, the distribution of increased dividend payments to its parent.

2.2 Are there enforceability or other concerns (such as director liability) if only a disproportionately small (or no) benefit to the guaranteeing/securing company can be shown?

Directors (acting always as a board) owe certain duties to the company which derive from both statute and common law. Under common law, these fiduciary duties include the duty of the directors to exercise their powers in good faith for the purposes for which they were conferred, and to act in the best interests of the company as a whole; i.e. all the shareholders of the company as a general body and not in the interests of a named shareholder and/or shareholders.

In the absence of judicial guidance on the matter, it is not clear whether the absence (or insufficiency) of corporate benefit would render a guarantee void, and consequently a creditor's rights thereunder, unenforceable. Given this grey area, the directors of a company should be able to demonstrate that they have fully considered corporate benefit issues and relevant considerations will invariably include the likelihood of the guarantee being called (as against the benefit to be derived by the company entering into the guarantee) and, if so called, whether the company is able to meet its financial obligations thereunder and still remain solvent.

Notwithstanding the above, relief from directors' duties may be sought from the shareholders in a general meeting, provided there is no fraud on the minority. It is considered good practice to have a shareholders' resolution in place to ratify, confirm and approve any decision of the directors to approve the company in acting as guarantor. Relief may also be sought under the Companies Laws of Cyprus, Cap. 113, as amended. The relevant statutory provision provides that in proceedings brought against a director for breach of duty, the relevant director may be absolved from liability, provided that he or she can prove that he or she acted honestly and reasonably, with regard to all the circumstances.

2.3 Is lack of corporate power an issue?

The memorandum and articles of association of a company should be carefully vetted in order to determine whether the granting of guarantees is within the company's objects. Even if no express power is granted, and provided they are not expressly prohibited, the objects may be so broadly drafted, so as to include the granting of guarantees as being ancillary to and in furtherance of the objects of the company. An act which is not authorised by the objects clause of the memorandum is *ultra vires*, i.e. beyond the company's powers as set out in its memorandum and void *ab initio*, and may not be remedied by any subsequent act of the shareholders.

Section 33A of the Companies Law, Cap. 113 ("Companies Law") attempted to do away with the *ultra vires* doctrine by providing that a company will be bound *vis-à-vis* third parties by acts or transactions of its officers, even if they do not fall within the objects of the company, provided that (i) the third party acted in 'good faith', and (ii) the acts in question do not exceed the powers prescribed by law, or which the law permits to be prescribed, to the officers concerned. Publication of the memorandum and articles does not in itself constitute sufficient proof of knowledge *vis-à-vis* the third party.

2.4 Are any governmental or other consents or filings, or other formalities (such as shareholder approval), required?

See question 3.9 below on stamp duty.

No governmental consents, filings or registration requirements are needed in order to grant a guarantee.

Whether a shareholder resolution is required is a matter for the articles of association of a company. In certain circumstances, shareholder approval may be required to whitewash any transactions which constitute prohibited financial assistance (see section 4 below) and/or to eliminate the risk of a transaction being rendered void for lack of corporate benefit (see question 2.2 above). More often than not, however, and irrespective of whether the articles of association require it, a shareholders' resolution will be put in place as a matter of good corporate practice.

Guarantees, being contracts, must comply with certain essential elements to ensure their validity and enforceability including an offer, an acceptance, the intention to create legal relations and consideration. Typically, the beneficiary of the guarantee must also provide consideration for the guarantor's promise (which may often prove difficult to demonstrate) and so to avoid a guarantee falling foul of contract law requirements for want of consideration, it is often executed as a deed.

2.5 Are net worth, solvency or similar limitations imposed on the amount of a guarantee?

See question 3.9 below on stamp duty.

No governmental consents, filings or registration requirements are needed in order to grant a guarantee.

Whether a shareholder resolution is required is a matter for the articles of association of a company. In certain circumstances, shareholder approval may be required to whitewash any transactions which constitute prohibited financial assistance (see section 4 below) and/or to eliminate the risk of a transaction being rendered void for lack of corporate benefit (see question 2.2 above). More often than not, however, and irrespective of whether the articles of association require it, a shareholders' resolution will be put in place as a matter of good corporate practice.

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2.6 Are there any exchange control or similar obstacles to enforcement of a guarantee?

There are no exchange control restrictions to enforcement of a guarantee.

A guarantee may be subject to stamp duty in Cyprus. An unstamped guarantee may not be adduced as evidence in Cyprus court enforcement proceedings unless stamp duty fees (including any penalties for late payment) have been settled.

3 Collateral Security

3.1 What types of collateral are available to secure lending obligations?

Generally speaking, any type of asset may be encumbered or charged to secure lending obligations in Cyprus.

The most common forms of collateral are:

- immovable property (such as land and/or any building, structure or thing affixed to it);
- tangible movable property (chattels);
- financial instruments such as shares and debt securities (claims and receivables);
- cash; and
- intangible movable property, such as intellectual property.

3.2 Is it possible to give asset security by means of a general security agreement or is an agreement required in relation to each type of asset? Briefly, what is the procedure?

It is possible to give asset security by means of a general security agreement in the form of a single fixed and floating charge debenture over various asset classes owned by a chargor.

The debenture will standardly include a fixed charge over particular assets, thereby giving a chargee control over any dealings or disposals of a particular asset by the chargor. It will also include a floating charge in relation to that part of the chargor's asset pool which is less ascertainable from time to time and which confers on the chargee the right to deal with the assets subject to the floating charge in the ordinary course of business. A debenture will also generally extend to include any assignment of receivables and contracts as well as any mortgages on immovable property and shares.

Practically speaking, it is more common to have in place specific security agreements in relation to certain assets such as land and shares (see questions 3.3 and 3.6 below, respectively), with any other assets being caught by an all-encompassing debenture creating security over all asset classes owned by a charger; in this way, any additional statutory perfection requirements and formalities affecting the validity and enforceability of a particular security arrangement are more easily satisfied.

3.3 Can collateral security be taken over real property (land), plant, machinery and equipment? Briefly, what is the procedure?

Collateral security may be taken over plant, machinery and equipment by way of a fixed charge debenture.

In terms of real or immovable property, security is taken by way of a mortgage of the property in favour of the mortgagee, pursuant to the provisions of the Immovable Property (Transfer & Mortgage) Law, Law 9/1965, as amended; which requires, as a priority point, for the mortgage instrument to be deposited with the District Lands Office in the district where the relevant property is located. Upon registration, no subsequent transfer or further mortgaging of the mortgaged property is possible except with the mortgagees' prior consent.

3.4 Can collateral security be taken over receivables? Briefly, what is the procedure? Are debtors required to be notified of the security?

Collateral security over receivables is possible as either: (i) an assignment by way of security (subject the assignability of the receivables in question); (ii) a fixed charge; or (iii) a floating charge (see question 3.2 above).

Cypriot law does not recognise the concept of a legal assignment and the assignment of a receivable, as a chose in action, will invariably take the form of an equitable assignment. Provided that the intention to assign has been notified, being both a perfection and priority requirement as against subsequent creditors, equity will recognise it. The assignment is effective only once notified to the assignee.

3.5 Can collateral security be taken over cash deposited in bank accounts? Briefly, what is the procedure?

It is possible to take collateral security over cash deposited in a Cyprus bank account by way of a fixed or floating charge.

It is common to take a fixed charge over a blocked deposit account with any withdrawals from that account by the chargor made possible only with creditor consent. On the contrary, a floating charge will be given over a trading account to circumvent the impracticability of lender consent each time outbound payments need to be made from the account. In this way, the chargor is given the flexibility to continue to use the account for ordinary business purposes until the occurrence of a trigger event (such as a default), at which time the floating charge will crystallise, and attach to all the relevant assets secured by it, including, in the case of bank account charges, any cash held in the chargor's account subject to the charge.

3.6 Can collateral security be taken over shares in companies incorporated in your jurisdiction? Are the shares in certificated form? Can such security validly be granted under a New York or English law governed document? Briefly, what is the procedure?

The creation of security over shares in a Cyprus company takes the form of a pledge of shares or fixed charge. The most commonly used mechanism is the share pledge which involves the physical delivery to the pledgee of the share certificates representing the pledged shares.

A pledge, as a possessory form of security, creates upon the execution of the relevant security instrument an equitable charge over the shares, and on delivery to the pledgee of the share certificate or certificates representing those shares, a legal charge over the share certificates themselves.

On the borrowers' default, the pledgee is afforded a common law right to sell the pledged assets without recourse to court, provided of course that the security instrument includes a mechanism enabling the pledgee to transfer the pledged shares (using certain aids to enforcement of the pledge which are usually annexed to the charge instrument itself) without additional consent from the pledgor or other formalities or approvals. The aids to enforcement will often include: the original share certificates representing the pledged shares; undated blank instruments of transfer of shares duly executed by the Pledgor; a resolution of the board of directors of the company approving the pledging of the shares and the transfer of such shares on default; and waivers of pre-emption rights (if any).

Unless the terms of the security instrument provide otherwise, the pledgor remains the owner of the pledged shares throughout the life of the pledge and continues to enjoy the rights attaching to the shares in a manner which does not prejudice the rights of the pledgee, until and unless a default event occurs.

Section 138 of the Contract Laws of Cyprus, Cap. 149 as amended, prescribes the formalities required to create a valid and enforceable pledge over the shares of a Cyprus company, namely, it must be signed by the pledgor and made in the presence of two witnesses. Over and above these requirements, section 138(2) sets certain additional requirements for a pledge of shares to be valid and enforceable, which include: (a) the giving of notice of pledge by the pledgee to the company in which the shares are pledged; (b) the company making a memorandum of such pledge in the register of shareholders against the shares in respect of which the notice is given; and (c) the subsequent delivery by the company of a certificate confirming (b) above.

Finally, security may also be taken over shares of public companies listed on the Cyprus Stock Exchange. As these shares are in dematerialised form, there will be no "pledge" of the share certificates as such but instead a charge created over the special account of a particular investors' share account which will be registered in the Central Securities Depository and Central Registry of the Cyprus Stock Exchange. A charge over dematerialised securities is valid from the moment of its registration. The requirements of section 138 of the Contract Law do not apply in the case of pledge of dematerialised securities.

Although the security could theoretically be governed by New York or English law, given that the subject matter of the pledge are shares of a Cyprus company, any transfer of those shares to the pledgee or some other third party on enforcement is subject to mandatory provisions of Cypriot law, and will be determined in light of the Companies Laws of Cyprus, as well as the memorandum and articles of association of the Cyprus company concerned.

3.7 Can security be taken over inventory? Briefly, what is the procedure?

Security over inventory usually takes the form of a fixed and floating charge debenture, although a floating charge is the most commonly used form of security due to the constantly fluctuating nature of the asset and the inability of the chargee to exercise control (as in the case of a fixed charge).

3.8 Can a company grant a security interest in order to secure its obligations (i) as a borrower under a credit facility, and (ii) as a guarantor of the obligations of other borrowers and/or guarantors of obligations under a credit facility (see below for questions relating to the giving of guarantees and financial assistance)?

A company may grant a security interest in order to secure its own obligations as borrower or to guarantee the borrowings of a third party. The provision of third-party security by a company will, however, be subject to corporate benefit, capacity, solvency and financial assistance issues – see questions 2.2, 2.5, 4.1 and 8.2.

3.9 What are the notarisation, registration, stamp duty and other fees (whether related to property value or otherwise) in relation to security over different types of assets?

Notarisation fees are not applicable in Cyprus.

The registration fees that will apply in Cyprus are as follows:

(i) Under the Companies Law

Section 90 of the Companies Law provides that every charge (as well as every amendment, assignment or change to it) created by a Cyprus company and conferring security on the company's property or undertaking shall be void against the liquidator and any creditor of the company, unless the prescribed particulars of the charge and a certified copy of the instrument creating it, are delivered to the Registrar of Companies in Cyprus for registration within 21 days after the date of its creation. The prescribed period is extended to 42 days in the case of a charge created by a Cyprus company outside Cyprus, comprising property situated outside Cyprus. Section 90(2) provides an exhaustive list of categories of charge which are capable of registration.

Registration under section 90 of the Companies Law is not a priority point, but a perfection requirement. Registration has the effect of giving public notice of the security to third parties dealing with the company that the particular assets or part of the undertaking has been charged in in the chargee's favour. Failure to register will not affect the validity of the charge as between the parties to it *inter se*; however as mentioned earlier, registration will be necessary to render the security enforceable against any third party creditor or liquidator.

Registration of a charge will incur the payment of filing fees in the region of approx. €680 per charge registered.

Pledges of shares in a Cyprus company are specifically exempted from the ambit of section 90.

Similarly, agreements for the provision of financial collateral which fall within the within the ambit of the Financial Collateral Arrangements Law (Law 43(I) of 2004) are exempted from registration.

Other statutorily prescribed registration fees over specific assets:

Certain additional registration requirements apply in relation to charges over specific classes of assets. A legal mortgage over immovable property requires registration with the District Lands Office Land (see question 3.3). Registration fees of one thousandth of the amount secured are payable. A mortgage over a vessel or any share in a vessel is registered with the Department of Merchant Shipping, with registration fees dependent on the gross tonnage of the vessel (€0.034172 per gross tonne for the first 10,000 tonnes and half that rate above 10,000 tonnes).

(ii) Stamp Duty

Cyprus stamp duty is charged on 'documents' (i.e. agreements or contracts made in writing) relating to assets located in Cyprus and/or matters or things taking place in Cyprus. In general, agreements which do not involve assets situated in Cyprus are generally exempt from stamp duty; however, the final adjudicator on whether or not stamp duty is payable on any document, will be the Commissioner of Stamp duties.

Stamp duty is calculated on the value of the agreement and is capped to a maximum amount of €20,000 on the principal document. Any documents relating to the same transaction and which are considered ancillary to the principal document will incur a nominal rate of stamp duty.

Stamp Duty rates:

- €0–€5,000: nil.
- €5,001–€170,000: 0, 15%.
- Over €170,000: 0, 20%.

Stamp duty must be paid within 30 days from the date of the 'signing' of the relevant document. If for whatever reason the agreement is considered stampable and was not stamped, then a penalty will be payable. Failure to stamp a document which is subject to stamp duty does not invalidate the document of the acts contemplated thereby, but it cannot be adduced as evidence in enforcement proceedings brought before a Cyprus court unless the stamp duty and any penalties for late payment have been paid.

3.10 Do the filing, notification or registration requirements in relation to security over different types of assets involve a significant amount of time or expense?

Filing or registration fees are not significant (see question 3.9 above). In terms of timing, registration occurs upon filing which, in most cases, is a same-day procedure. A certificate of registration of charge (in the case of shares) may be issued by the Registrar of Companies within a matter of days after filing.

3.11 Are any regulatory or similar consents required with respect to the creation of security?

No regulatory or similar consents are needed, although if regulated entities are involved, they may be subject to additional requirements.

3.12 If the borrowings to be secured are under a revolving credit facility, are there any special priority or other concerns?

There are no special priority or other concerns if the borrowings to be secured are under a revolving credit facility.

3.13 Are there particular documentary or execution requirements (notarisation, execution under power of attorney, counterparts, deeds)?

There are specific statutory requirements and formalities that will need to be met in relation to the creation a pledge over shares in a Cyprus company pursuant to the Contract laws of Cyprus, Cap. 149, as amended. See further question 3.6 above.

In the case of deeds, it is no longer a requirement for these to be executed under seal; however if a company chooses to affix its common seal, this must be done in accordance with the articles of association of the company.

4 Financial Assistance

4.1 Are there prohibitions or restrictions on the ability of a company to guarantee and/or give security to support borrowings incurred to finance or refinance the direct or indirect acquisition of: (a) shares of the company; (b) shares of any company which directly or indirectly owns shares in the company; or (c) shares in a sister subsidiary?

(a) Shares of the company

Section 53(1) of the Companies Law imposes a prohibition on Cypriot companies to give, whether directly or indirectly, and whether by means of a loan, guarantee, the provision of security or otherwise, any financial assistance for the purpose of or in connection with a purchase or subscription of shares made, or to be made, by any person in the company or in its holding company.

The general prohibition is subject to certain permitted exceptions such as where the lending of money is part of the ordinary business of the company. Similarly, where an otherwise prohibited transaction has been whitewashed under 53(3), a private company may proceed in giving financial assistance without falling foul of the general prohibition imposed by section 53(1).

The whitewash mechanism requires that (i) the private company concerned is not a subsidiary of a public company registered in Cyprus, and (ii) the transaction has been approved (at any time) by a resolution passed by holders of 90% of all issued voting capital in the company acting in general meeting.

Apart from any action brought against a director for misappropriation of company funds, or breach of duty, any contravention of section 53 (1) will subject the company and every officer to a default fine.

(b) Shares of any company which directly or indirectly owns shares in the company

Yes, see (a) above.

(c) Shares in a sister subsidiary

No prohibition would apply in this scenario.

5 Syndicated Lending/Agency/Trustee/Transfers

5.1 Will your jurisdiction recognise the role of an agent or trustee and allow the agent or trustee (rather than each lender acting separately) to enforce the loan documentation and collateral security and to apply the proceeds from the collateral to the claims of all the lenders?

As a common law jurisdiction, Cyprus law will recognise the role of a security agent or trustee who will hold the security over assets of the borrower on trust for the benefit of a pool of creditors. The duties and responsibilities of the security agent or trustee will be governed by the agency provisions in the loan instrument and the proceeds from enforcement of the loan or collateral security will be administered in accordance with the terms of the intercreditor agreement.

5.2 If an agent or trustee is not recognised in your jurisdiction, is an alternative mechanism available to achieve the effect referred to above which would allow one party to enforce claims on behalf of all the lenders so that individual lenders do not need to enforce their security separately?

Not applicable – see question 5.1.

5.3 Assume a loan is made to a company organised under the laws of your jurisdiction and guaranteed by a guarantor organised under the laws of your jurisdiction. If such loan is transferred by Lender A to Lender B, are there any special requirements necessary to make the loan and guarantee enforceable by Lender B?

There are no special requirements under the laws of Cyprus to make the loan and guarantee enforceable by Lender B, subject to any requirements specified in the loan agreement having been met.

6 Withholding, Stamp and Other Taxes; Notarial and Other Costs

6.1 Are there any requirements to deduct or withhold tax from (a) interest payable on loans made to domestic or foreign lenders, or (b) the proceeds of a claim under a guarantee or the proceeds of enforcing security?

Generally, Cyprus tax legislation does not provide for a withholding tax on interest payable on loans made to domestic or foreign lenders, or the proceeds of a claim under a guarantee or the proceeds of enforcing security.

6.2 What tax incentives or other incentives are provided preferentially to foreign lenders? What taxes apply to foreign lenders with respect to their loans, mortgages or other security documents, either for the purposes of effectiveness or registration?

No specific tax incentives exist for foreign lenders. Generally, foreign lenders are not subject to Cyprus tax or subject to Cyprus withholding tax on any interest payments.

Cyprus stamp duty may be applicable on the loan documentation (see the response to question 3.9).

6.3 Will any income of a foreign lender become taxable in your jurisdiction solely because of a loan to or guarantee and/or grant of security from a company in your jurisdiction?

A foreign lender is not subject to Cyprus tax solely because of a loan to or a guarantee or security given by a local company.

6.4 Will there be any other significant costs which would be incurred by foreign lenders in the grant of such loan/guarantee/security, such as notarial fees, etc.?

There are no significant costs other than those described in question 3.9 above.

6.5 Are there any adverse consequences to a company that is a borrower (such as under thin capitalisation principles) if some or all of the lenders are organised under the laws of a jurisdiction other than your own? Please disregard withholding tax concerns for purposes of this question.

Cyprus tax legislation does not specifically provide for thin capitalisation or similar rules.

7 Judicial Enforcement

7.1 Will the courts in your jurisdiction recognise a governing law in a contract that is the law of another jurisdiction (a "foreign governing law")? Will courts in your jurisdiction enforce a contract that has a foreign governing law?

The courts of Cyprus will recognise and give effect to a contractual foreign choice of governing law in any action brought before a Cyprus court pursuant to the Rome I Regulation (Reg. (EC) No. 593/2008) regardless of the domicile of the parties (Regulation (EU) No. 1215/2012 (recast)). The cornerstone of the Regulation is to enshrine the principle of party autonomy and flexibility in respect of choice of law. Where parties choose a foreign governing law which is not the law most closely connected with the contract (assuming this would otherwise be Cypriot law) the courts in Cyprus will tend to give effect to it subject to (i) such choice of foreign law being pleaded and proved, (ii) mandatory provisions of Cypriot law which cannot be derogated from by agreement (penal, revenue and court procedural rules), and (iii) laws which are manifestly inconsistent with public policy.

7.2 Will the courts in your jurisdiction recognise and enforce a judgment given against a company in New York courts or English courts (a "foreign judgment") without re-examination of the merits of the case?

Recognition and enforcement of judgments given by New York courts:

There is no bilateral treaty between Cyprus and the USA on the enforcement of foreign judgments. Although a judgment of a New York court will be recognised under the Recognition, Enforcement and Execution of Foreign Judgments Law, Law 121(I)/2000, enforcement is not immediate. Section 5 of that law sets the procedural requirements to be followed, which commences by way of an application by summons accompanied by an affidavit. The hearing is set four weeks after the date of filing of the application and the respondent is given the right to file an objection (relating to jurisdictional matters and issues of substance).

Recognition and enforcement of judgments given by English courts:

The courts in Cyprus will recognise and enforce judgments issued by English courts in accordance with the Brussels I Regulation (Reg. (EC) No. 44/2001) and Regulation (EU) No. 1215/2012 (recast) without any special procedure being required as to its recognition, this being an automatic process. Under the Regulation, a judgment given by the courts of an EU country may not be reviewed as to its substance although a court may refuse to recognise a judgment issued in another Member State under certain limited circumstances (e.g. where it is contrary to public policy). As soon as the judgment is recognised, the competent Cyprus court issues an order for its enforcement and the judgment will be executed as though issued by a Cyprus court.

7.3 Assuming a company is in payment default under a loan agreement or a guarantee agreement and has no legal defence to payment, approximately how long would it take for a foreign lender to (a) assuming the answer to question 7.1 is yes, file a suit against the company in a court in your jurisdiction, obtain a judgment, and enforce the judgment against the assets of the company, and (b) assuming the answer to question 7.2 is yes, enforce a foreign judgment in a court in your jurisdiction against the assets of the company?

The answer is specific to the facts and circumstances of each case and depends on the caseload of the court examining the matter.

7.4 With respect to enforcing collateral security, are there any significant restrictions which may impact the timing and value of enforcement, such as (a) a requirement for a public auction, or (b) regulatory consents?

No. Certain types of borrowers or assets may be subject to their own regulatory requirements and may need prior approval from their respective supervisory authorities.

In exercising the enforcement rights afforded to them under the relevant security documents, a secured creditor is obliged under common law to obtain a fair price when realising assets subject to security and to pay regard to the principle of unjust enrichment.

7.5 Do restrictions apply to foreign lenders in the event of (a) filing suit against a company in your jurisdiction, or (b) foreclosure on collateral security?

Foreign lenders can file a suit against a company in Cyprus and foreclose on collateral security without restriction.

7.6 Do the bankruptcy, reorganisation or similar laws in your jurisdiction provide for any kind of moratorium on enforcement of lender claims? If so, does the moratorium apply to the enforcement of collateral security?

Recent amendments to the Companies Law (Law 62(I) of 2015) have introduced a process of "examinership". The amendments make provision for the appointment of a licensed insolvency practitioner as the "examiner" whose role is to examine the state of the company's affairs and agree restructuring proposals with shareholders during a four-month moratorium, in which the company is considered to be under the protection of the court, and immune from creditor action. Such examiner is appointed pursuant to a petition filed at court and once the court deems that, *inter alia*, a company is unable to pay its debts (i.e. the net asset value of the company is negative, taking into account potential and future liabilities).

Additionally, a court can make an order authorising the examiner to dispose of assets subject to security pursuant to section 202H(1)(d) of the Companies Law if it is satisfied that it would be advantageous to do so. The relevant section provides that where any claim against the company is secured by a mortgage, charge, lien or other encumbrance or a pledge of, on or affecting the whole or any part of the property, no action may be taken to realise the whole or any part of that security, except with the consent of the examiner. Specifically in relation to floating charges an examiner may, by order of the Court, realise the charged property (as if it was not subject to the charge) if in doing so would be to facilitate the survival of the company concerned as a going concern. Any net proceeds from the sale of secured assets pursuant to this section are used first to repay the secured debt with any surplus being distributed among unsecured creditors.

Bankruptcy under the Bankruptcy Law, Cap. 5 (as amended by Law 61(I)/2015):

Cypriot courts have the power (in accordance with Cap. 5) to order a 95-day moratorium on any enforcement action by creditors for the purpose of enabling a debtor to agree an arrangement (referred to as a "personal repayment plan") with them. If the plan is approved by a 75% majority of creditors in value and is sanctioned by the court, the arrangement will be binding on the debtor and all creditors. Dissenting creditors are given a right to be heard in court.

7.7 Will the courts in your jurisdiction recognise and enforce an arbitral award given against the company without re-examination of the merits?

As a contracting state to the New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards of 10 June 1958, a Cyprus court will enforce an arbitral award without re-examining the merits, provided that certain requirements as set out in the Convention have been met.

8 Bankruptcy Proceedings

8.1 How does a bankruptcy proceeding in respect of a company affect the ability of a lender to enforce its rights as a secured party over the collateral security?

The main provisions relating to corporate insolvency in Cyprus are contained in the Companies Law (sections 202–305 inclusive) as amended by Law 62(I)/2015. The lender's ability to enforce its rights as a secured party over the collateral security will invariably be affected by its inability to enforce the security during the protected period without the consent of the examiner – see question 7.7.

8.2 Are there any preference periods, clawback rights or other preferential creditors' rights (e.g., tax debts, employees' claims) with respect to the security?

Under section 301 of the Companies Law, any conveyance, mortgage, delivery of goods, payment, execution or other act relating to property made or done by or against a company within six months before the commencement of its winding-up, shall, within the context of a winding up, be considered a fraudulent preference against its creditors and invalid. In determining whether there is a fraudulent preference, the court looks at the dominant intention of giving the creditor a preference over other creditors coupled with a voluntary act made by the company. In establishing whether the intention to defraud existed, the burden of proof will rest with those intending to avoid the transaction.

Section 303 of the Companies Law provides (in the context of a winding up) that a floating charge on the undertaking or property of the company created within 12 months of the commencement of winding-up shall, unless it is proved that immediately after the creation of the charge the company was solvent, be invalid. The onus of proof rests with the chargee.

Certain claims are treated preferentially in a winding up and will therefore rank ahead of debts secured by a floating charge; namely, the costs of the winding up and preferential claims, which consist of all government and local taxes and duties due at the date of liquidation (due and payable within 12 months prior to that date) and where there are assessed taxes, taxes not exceeding one whole year's assessment; and all sums due to employees including wages, accrued holiday pay, deductions from wages and compensation for injury.

8.3 Are there any entities that are excluded from bankruptcy proceedings and, if so, what is the applicable legislation?

No, all companies registered in accordance with the Companies Law will be subject to the insolvency provisions contained therein. Additional requirements will apply to certain regulated entities and companies which carry on business in one or more Member States who will be subject to the provisions of the EU Insolvency Regulation.

8.4 Are there any processes other than court proceedings that are available to a creditor to seize the assets of a company in an enforcement?

Out-of-court proceedings available to a creditor to seize the assets of a company in an enforcement include powers of sale, taking possession, appointment of a manager or receiver and appropriation of financial collateral. The most common practice is for a receiver to be appointed.

9 Jurisdiction and Waiver of Immunity

9.1 Is a party's submission to a foreign jurisdiction legally binding and enforceable under the laws of your jurisdiction?

A party's submission to a foreign jurisdiction is legally binding and enforceable under the laws of Cyprus. See the response to question 7.2 above.

9.2 Is a party's waiver of sovereign immunity legally binding and enforceable under the laws of your jurisdiction?

A party's waiver of sovereign immunity will be legally binding and enforceable under the laws of Cyprus.

10 Licensing

10.1 What are the licensing and other eligibility requirements in your jurisdiction for lenders to a company in your jurisdiction, if any? Are these licensing and eligibility requirements different for a "foreign" lender (i.e. a lender that is not located in your jurisdiction)? In connection with any such requirements, is a distinction made under the laws of your jurisdiction between a lender that is a bank *versus* a lender that is a non-bank? If there are such requirements in your jurisdiction, what are the consequences for a lender that has not satisfied such requirements but has nonetheless made a loan to a company in your jurisdiction? What are the licensing and other eligibility requirements in your jurisdiction for an agent under a syndicated facility for lenders to a company in your jurisdiction?

There are no eligibility requirements in Cyprus in respect of lenders to a Cyprus company.

A lender licensed in their home jurisdiction does not need to be additionally licensed in Cyprus in order to lend funds to a local company.

11 Other Matters

11.1 Are there any other material considerations which should be taken into account by lenders when participating in financings in your jurisdiction?

There are no special considerations that need to be borne in mind by lenders when participating in financings in Cyprus.

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Marinella has over 10 years of post-qualification experience in her chosen practice areas. Marinella started her career in the corporate and commercial department of one of the largest law firms in Cyprus. During her career Marinella has had the opportunity to advise extensively on a number of high-profile blue-chip transactions for a vast range of multinationals and Magic Circle law firms.

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George focuses on tax, intellectual property, immigration and corporate and commercial law. He graduated from the University of Westminster and after completing his Bachelor's degree, he joined the audit and tax practice of a Cyprus major accountancy firm. He was later admitted to the Cyprus Bar Association and is currently a partner with E & G Economides LLC. He is a member of the Cyprus Bar Association and the Individual Tax and Private Client Committee of the International Bar Association. In addition to the above, George is also extensively involved in the firm's business development and marketing activities.

Economides
ADVOCATES & LEGAL CONSULTANTS

E & G Economides LLC, based in Limassol, specialises in Corporate & Commercial, Mergers & Acquisitions, Banking and Finance and Capital Markets work. Litigation, Financial Services and Private Client matters are also offered. With a team currently comprising over 20 advocates, the firm has continued to grow and expand its areas of practice with the support of an active network of global associates with long-standing ties to the corporate and financial communities.

The firm maintains a diverse client base and is regularly instructed by high-net-worth individuals, entrepreneurs, multinational corporations and tax firms, as well as global banking and credit institutions and both domestic and international transactions.

Our clients' interests often have a global focus and we are therefore frequently mandated to co-operate with international law firms on multijurisdictional projects and other cross-border engagements. Such assignments have been pivotal in yielding a globally minded perspective and have brought the firm into close co-operation with international law firms.

Denmark

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1 Overview

1.1 What are the main trends/significant developments in the lending markets in your jurisdiction?

Interest levels remain historically low and the general market conditions for doing business in Denmark continue to improve as the financial crisis is left behind. Pension funds are in their pursuit of a reasonable yield on investments showing an increased interest in funding large infrastructure projects and corporations including other alternative investments. One of the most recent examples is a new infrastructure fund with a focus on Africa launched by A.P. Møller Holding A/S together with a number of pension funds such as PKA, PensionDanmark, Lægernes Pension and PFA having received commitments in the total of USD 650 million and expecting the total equity commitment to reach USD 1 billion within a year.

Lending-based crowdfunding is also rapidly increasing as an alternative source of financing.

1.2 What are some significant lending transactions that have taken place in your jurisdiction in recent years?

See question 1.1.

2 Guarantees

2.1 Can a company guarantee borrowings of one or more other members of its corporate group (see below for questions relating to fraudulent transfer/financial assistance)?

As a general rule, Danish private and public limited companies may guarantee borrowings of one or more other members of its corporate group provided, in particular, that the corporate benefit requirement is adequately observed (see question 2.2), and that Danish legislation on financial assistance is complied with (see question 4.1).

2.2 Are there enforceability or other concerns (such as director liability) if only a disproportionately small (or no) benefit to the guaranteeing/securing company can be shown?

Under Danish law, it is the directors' duty to ensure that corporate transactions and positions are in the best interest of the company; which often, but not always, mirrors the interest of the shareholders. Put differently, each action of the company must be financially, commercially, or strategically justified. The corporate benefit must accrue to the individual Danish company rather than the corporate group as a whole. In addition to the duty to continuously ensure that the available capital resources are adequate, the corporate benefit requirement entails, for example, that the directors must establish a reasonable balance between the corporate benefit and the risk assumed pursuant to the guarantee.

Under certain circumstances, e.g., in the event of bad faith of the beneficiary, and if the corporate benefit requirement is not duly observed, the guarantee granted by the company may be invalid and unenforceable and the directors may be subject to personal liability for damages and criminal sanctions. Especially in case of a Danish company's granting of upstream or cross-stream guarantees in favour of direct or indirect parent or sister companies, the directors may find it desirable to include limitation language in the guarantee addressing the fulfilment of the corporate benefit requirement.

2.3 Is lack of corporate power an issue?

Lack of corporate power is generally not an issue. In addition to satisfaction of the company's signing powers, lenders usually require a board resolution of the guarantor to minimise potential doubt about lack of corporate power and corporate benefit concerns. Lenders' diligent examinations also include a review of the guarantor's articles of association and publicly available corporate information to ensure among other things that the guarantor's corporate objectives are wide enough to cover the issue of a guarantee.

2.4 Are any governmental or other consents or filings, or other formalities (such as shareholder approval), required?

No; generally, under Danish law, guarantees are not subject to specific formalities.

Broadly speaking, while granting a guarantee is not in the nature of an extraordinary matter to be transacted at the general meeting, in special circumstances the board of directors may find it desirable – even merely as a gesture – to refer such a matter to the general meeting, thereby alleviating disagreement between the shareholders and minimising subsequent shareholder criticism.

2.5 Are net worth, solvency or similar limitations imposed on the amount of a guarantee?

No; however, the directors must at all times ensure that the financial resources of the company are adequate, i.e. that the company has sufficient liquidity to meet its current and future liabilities as they fall due. The duty implies that the directors must assess the company's financial position and ensure that the available capital resources justify the granting of the guarantee. To accommodate directors' liability concerns, limitation language concerning the scope of guarantee is often included.

2.6 Are there any exchange control or similar obstacles to enforcement of a guarantee?

No.

Naturally, it is good practice to examine whether *non-Danish* exchange control or similar obstacles apply.

Denmark enforces 'freezing of funds' and similar financial restrictive measures adopted by the UN and the EU.

3 Collateral Security

3.1 What types of collateral are available to secure lending obligations?

Lending obligations may be secured by a number of different types of security under Danish law, including by way of a pledge, security assignment, mortgage, general floating charge covering specific groups of assets and retention of title. In general, any type of asset may be validly pledged. Furthermore, it is possible not only to agree a negative pledge over certain assets *inter partes* but also to register the negative pledge in the Personal Register whereby it will also have legal effect towards third parties.

3.2 Is it possible to give asset security by means of a general security agreement or is an agreement required in relation to each type of asset? Briefly, what is the procedure?

Danish law does not recognise the concept of a general security agreement covering all assets of the security provider. Each type of asset must be regulated in an individual security agreement or in a combined security agreement incorporating the necessary regulation of each type of security and clearly identifying each individual asset granted as security.

However, a Danish company may provide security by way of a general floating charge over a number of specifically allowed classes of its assets, including trade receivables, inventory, vehicles not previously registered in Denmark, operating equipment and machinery, IPR and goodwill, which is perfected by registration in the Personal Register.

Further, a company operating from a leased property may mortgage its operating equipment, including machines and technical installations.

3.3 Can collateral security be taken over real property (land), plant, machinery and equipment? Briefly, what is the procedure?

Security may be taken over real property by way of real estate mortgages, which are perfected by registration in the Land Register. On properties permanently fitted for a specific business, such mortgage will also cover technical installations, machinery and operating equipment, unless otherwise agreed.

Provided that assets are not covered by a real estate mortgage, security can be taken separately over machinery and operating equipment in the form of a chattel mortgage, which is perfected by registration in the Personal Register or by physical removal of the assets from the pledgor. Similarly, operating equipment and machinery may be mortgaged under a general floating charge. See question 3.2 with respect to granting security over operating equipment and machines of a company operating from a leased property.

3.4 Can collateral security be taken over receivables? Briefly, what is the procedure? Are debtors required to be notified of the security?

Security over receivables can be created by way of a floating charge covering all of the security provider's trade receivables; or by a separate assignment of specific, identified receivables. A floating charge is perfected via registration in the Personal Register and does not require individual notice to the debtors. An assignment on the other hand must be notified to the relevant third party debtor(s); such notice must include an instruction to pay directly to the security holder in order for the assignment to be duly perfected.

3.5 Can collateral security be taken over cash deposited in bank accounts? Briefly, what is the procedure?

Security may be taken over cash deposited in a bank account by establishment of a pledge over the bank account. Due perfection requires notification of the pledge to the bank and that the account holder is deprived of all disposal rights to the bank account. Consequently, pledges over bank accounts are impractical with respect to accounts used in a company's day-to-day operations.

3.6 Can collateral security be taken over shares in companies incorporated in your jurisdiction? Are the shares in certificated form? Can such security validly be granted under a New York or English law governed document? Briefly, what is the procedure?

Shares in unlisted companies can be pledged unless otherwise set out in the company's articles of association. Shares need not be in certificated form in order to be pledged. Provided that the company has not issued negotiable share certificates, the pledge of shares (regardless of whether the shares are certificated or not) is perfected by written notice to the company stating that the share(s) are pledged. Such notice must be provided no later than the time of disbursement of the loan proceeds to avoid risk of claw-back in case of bankruptcy.

If negotiable share certificates have been issued, duly perfection requires that the pledgor is deprived of its physical share certificates. However, physical share certificates are usually not issued by Danish companies.

If the company's shares are issued in dematerialised form through a central securities depositary ("**CSD**"), the pledge is perfected by registration in a Danish CSD (currently only one CSD in Denmark: VP Securities A/S).

A share pledge agreement may be governed by the laws of a foreign jurisdiction, including New York or English laws. However, Danish law would still apply in respect of perfection requirements. Furthermore, Danish law contains certain mandatory duty of care provisions aimed at protecting a pledgor in connection with the enforcement of the security, *cf*. question 7.4. It is therefore advisable and in accordance with market practice in Denmark to have the share pledge agreement governed by Danish law.

3.7 Can security be taken over inventory? Briefly, what is the procedure?

Security over inventory can be created by way of a general floating charge or a separate pledge. A general floating charge is perfected by registration in the Personal Register. A pledge over inventory or stock is perfected by the pledgor being physically prevented from freely disposing of the pledged assets (in Danish: *nøglepant*).

3.8 Can a company grant a security interest in order to secure its obligations (i) as a borrower under a credit facility, and (ii) as a guarantor of the obligations of other borrowers and/or guarantors of obligations under a credit facility (see below for questions relating to the giving of guarantees and financial assistance)?

Yes, subject to the limitations described under questions 2.1, 2.2 and 4.1.

3.9 What are the notarisation, registration, stamp duty and other fees (whether related to property value or otherwise) in relation to security over different types of assets?

There are no notarisation requirements.

Registrations of charges and mortgages with the Land Register, the Motor Vehicle Register and the Personal Register are subject to stamp duty calculated as 1.5 per cent of the nominal value of the mortgage plus a filing fee of DKK 1,660. Registration of a mortgage over commercial vessels is subject to stamp duty of 0.1 per cent of the secured amount.

3.10 Do the filing, notification or registration requirements in relation to security over different types of assets involve a significant amount of time or expense?

No, it involves only limited amount of time and expense, save for security involving registration with the Land Register, the Personal Register or the Motor Vehicle Register, which is subject to stamp duty; see question 3.9.

Registrations with the Land Register, the Personal Register and the Motor Vehicle Register are carried out online, and most often it is possible to obtain a final registration the very same day as the filing is made.

3.11 Are any regulatory or similar consents required with respect to the creation of security?

In general, no regulatory consents are required. Third party consents pursuant to underlying contracts may need to be considered.

3.12 If the borrowings to be secured are under a revolving credit facility, are there any special priority or other concerns?

No, there are not.

3.13 Are there particular documentary or execution requirements (notarisation, execution under power of attorney, counterparts, deeds)?

If a mortgage requires registration with, for example, the Land Register or the Personal Register, and the digital filing is signed by a person pursuant to a power of attorney, such power of attorney must be prepared in the mandatory format of the Danish Registers and the signature(s) of the principal(s) must be witnessed by two persons.

No other documentary or execution requirements apply.

4 Financial Assistance

4.1 Are there prohibitions or restrictions on the ability of a company to guarantee and/or give security to support borrowings incurred to finance or refinance the direct or indirect acquisition of: (a) shares of the company; (b) shares of any company which directly or indirectly owns shares in the company; or (c) shares in a sister subsidiary?

(a) Shares of the company

According to the general rule set forth in the Companies Act, a private or public limited company may not, directly or indirectly, advance funds, grant loans, or provide security (including guarantees) for a third party's acquisition of (or subscription for) shares of that company or of its parent company (i.e. a prohibition against financing of purchase of own shares).

This general prohibition does, however, not apply if certain requirements concerning the following matters are met: (i) shareholder approval; (ii) the proposed transaction is advisable considering the company's financial position or, if it is a parent company, its consolidated financial position; (iii) a report by the central management body to be publicly registered with the Danish Business Authority; and (iv) the proposed transaction is entered into on market terms including preparation of a credit rating of the purchaser and, if relevant, the financier.

Furthermore, the general prohibition does not apply to banks or mortgage loans granted by mortgage credit institutions or to transactions for the acquisition of shares to or from the employees of the company or any subsidiary.

Certain post-financing situations regarding acquisition of companies have been held to be unlawful by the Danish Business Authority, although such matters in themselves could be seen as justified corporate actions.

(b) Shares of any company which directly or indirectly owns shares in the company

The general prohibition including exceptions referred to under question 4.1 (a) also apply to a company's, direct or indirect, purchase of (or subscription for) shares in a parent company and presumably also in an indirect parent company.

(c) Shares in a sister subsidiary

Danish law does not stipulate any prohibition on financial assistance provided for the purchase of (or subscription for) shares in a sister subsidiary.

5 Syndicated Lending/Agency/Trustee/ Transfers

5.1 Will your jurisdiction recognise the role of an agent or trustee and allow the agent or trustee (rather than each lender acting separately) to enforce the loan documentation and collateral security and to apply the proceeds from the collateral to the claims of all the lenders?

Yes. Lenders may appoint agents, including security agents under the loan documentation, and such agents may enforce the rights of the lenders and apply the proceeds from the security to the claims of all the lenders; *cf.* chapter 4 of the Danish Capital Markets Act, which entered into force on 3 January 2018.

5.2 If an agent or trustee is not recognised in your jurisdiction, is an alternative mechanism available to achieve the effect referred to above which would allow one party to enforce claims on behalf of all the lenders so that individual lenders do not need to enforce their security separately?

See question 5.1.

5.3 Assume a loan is made to a company organised under the laws of your jurisdiction and guaranteed by a guarantor organised under the laws of your jurisdiction. If such loan is transferred by Lender A to Lender B, are there any special requirements necessary to make the loan and guarantee enforceable by Lender B?

The guarantee will often be granted in favour of the lenders from time to time and state that the guarantor's obligations are not reduced or discharged as a consequence of any transfer by a lender of its rights, in which case the loan and guarantee are enforceable by Lender B without further notice to the guarantor or other actions.

In the absence of such provisions in the guarantee, Lender B's enforcement of any rights under the loan requires that the borrower is notified of the transfer. In general, a guarantee in respect of a loan obligation will continue to apply and may be called upon by any new lender that has validly acquired the loan that is being guaranteed. However, the guarantor must be notified of the transfer in order to avoid the risk of the guarantor fulfilling its guarantee obligation by payment to the initial lenders or third parties.

6 Withholding, Stamp and Other Taxes; Notarial and Other Costs

6.1 Are there any requirements to deduct or withhold tax from (a) interest payable on loans made to domestic or foreign lenders, or (b) the proceeds of a claim under a guarantee or the proceeds of enforcing security?

Apart from the obligation of a Danish borrower to withhold tax at source from interest payments to a foreign lender, *cf.* question 6.3, there are no requirements to deduct or withhold tax under Danish law.

6.2 What tax incentives or other incentives are provided preferentially to foreign lenders? What taxes apply to foreign lenders with respect to their loans, mortgages or other security documents, either for the purposes of effectiveness or registration?

No tax incentives or other incentives are provided preferentially to foreign lenders.

Provided that no permanent establishment in Denmark exists with which the income from the loan, guarantee or security interest is effectively connected, no taxes apply to foreign lenders in such cases; *cf.* question 3.9 with respect to applicable stamp duties.

6.3 Will any income of a foreign lender become taxable in your jurisdiction solely because of a loan to or guarantee and/or grant of security from a company in your jurisdiction?

No. Tax liability requires, as a general rule, that the foreign lender has a permanent establishment in Denmark. Similarly, loan interest income secured on real property does not in itself lead to tax liability.

A Danish borrower may, however, be subject to withholding tax at source from interest payments, i.e. tax on unearned income, regarding certain intra-group loans (22 per cent of the total interest amount) if not otherwise provided by, for example, applicable double taxation agreements, or EU Directive 2003/49 on a common system of taxation applicable to interest and royalty payments made between associated companies of different EU Member States.

6.4 Will there be any other significant costs which would be incurred by foreign lenders in the grant of such loan/guarantee/security, such as notarial fees, etc.?

See question 3.9.

6.5 Are there any adverse consequences to a company that is a borrower (such as under thin capitalisation principles) if some or all of the lenders are organised under the laws of a jurisdiction other than your own? Please disregard withholding tax concerns for purposes of this question.

Danish tax law includes a number of deductibility limitation rules to be applied in the order given below: (1) the 'thin capitalisation' rule; (2) the 'interest-rate ceiling' rule; and (3) the 'EBIT' rule.

<u>The 'thin capitalisation' rule</u>

The thin capitalisation rule entails that thin capitalised companies' access to deduct interest and capital loss on controlled loans is limited. The thin capitalisation rule only kicks in if the controlled debt exceeds DKK 10 million and the lender(s) is/are not a natural person. It includes back-to-back structures involving third party lenders, e.g. banks. The thin capitalisation rule presupposes (i) a debt-to-equity ratio of four to one at the end of the income year, i.e. that the debt of the company exceeds the equity of the company by more than four times, and (ii) that the company does not prove that a similar financing can be obtained between independent parties. Any interest on debt to related parties in excess of this ratio will be subject to deductibility reduction.

<u>The 'interest-rate ceiling' rule</u>

The 'interest-rate ceiling' rule entails that a company's access to deduct net financing expenses is reduced. Unlike the thin capitalisation rule, this rule also has an impact on debt to independent lenders. The deductibility reduction caused by the 'interest-rate ceiling' entails that the net financing expenses are only deductible to the extent that they do not exceed the tax value of the company's assets multiplied by a standard rate of return. This deductibility reduction rule only applies to the net financing expenses exceeding DKK 21.3 million.

The 'EBIT' rule

The taxable income before net financing expenses (EBIT income, i.e. earnings before interest and taxes) may as a maximum be reduced by 80 per cent as a result of the net financing expenses following a deductibility reduction, if any, under the 'interest-rate ceiling' rule. Like the 'interest-rate ceiling' rule, the EBIT deductibility reduction rule only applies to the net financing expenses exceeding DKK 21.3 million. Net financing expenses restricted under the EBIT rule may be carried forward for tax deduction in the following years.

7 Judicial Enforcement

7.1 Will the courts in your jurisdiction recognise a governing law in a contract that is the law of another jurisdiction (a "foreign governing law")? Will courts in your jurisdiction enforce a contract that has a foreign governing law?

Danish courts will generally recognise the law of a foreign jurisdiction as the governing law in a contract and enforce the provisions of such contract with the exception of any provisions contrary to Danish public policy.

7.2 Will the courts in your jurisdiction recognise and enforce a judgment given against a company in New York courts or English courts (a "foreign judgment") without re-examination of the merits of the case?

A foreign judgment rendered in the courts of a country which is not a contracting state under: (i) the Council Regulation (EC) No 1215/2012, as amended, and implemented in Danish law; (ii) the Brussels Convention of 27 September 1968; (iii) the revised Lugano Convention of 30 October 2007; or (iv) the Hague Convention of 30 June 2005 on Choice of Court Agreements, would not be recognised or enforceable in Denmark without a retrial on the merits. Accordingly, a judgment rendered by a New York court would not be enforceable in Denmark.

A foreign judgment rendered by a court in any EU Member State, e.g. England, or any country that is a party to the revised Lugano Convention, will be recognised and enforceable by the Danish courts in accordance with the provisions of the Council Regulation, the revised Lugano Convention and the Hague Convention, respectively.

7.3 Assuming a company is in payment default under a loan agreement or a guarantee agreement and has no legal defence to payment, approximately how long would it take for a foreign lender to (a) assuming the answer to question 7.1 is yes, file a suit against the company in a court in your jurisdiction, obtain a judgment, and enforce the judgment against the assets of the company, and (b) assuming the answer to question 7.2 is yes, enforce a foreign judgment in a court in your jurisdiction against the assets of the company?

The duration of the legal proceedings will depend on which Danish court determines the case. If the Copenhagen City Court is the court of first instance, we estimate that it will take approximately 9–12 months to obtain an enforceable judgment. If the loan agreement satisfies the requirements for a debt instrument (in Danish: *gældsbrev*) and includes a clause of immediate enforceability, claims under the loan agreement may be enforced directly by the lender by application to the Bailiff's Court (in Danish*: fogedretten*) without having to obtain a judgment beforehand; *cf.* question 8.4.

Unless otherwise stated in the judgment and subject to the debtor's appeal of the judgment which may suspend the lenders' right to enforce the judgment, a judgment will become enforceable 14 days after the date of the ruling. Enforcement is carried out through the Bailiff's Court under the relevant district court by written application to the Bailiff's Court with the objective to seize the assets of the debtor and sell these via a forced sale. This procedure will likely take two to three months.

A similar duration of the enforcement process should be expected with respect to enforcement of foreign judgments if the Council Regulation applies, i.e. with respect to judgments rendered by a competent court of another EU Member State (see question 7.2).

7.4 With respect to enforcing collateral security, are there any significant restrictions which may impact the timing and value of enforcement, such as (a) a requirement for a public auction, or (b) regulatory consents?

In general, a creditor is free to enforce a pledge in accordance with the enforcement provisions of the pledge agreement without having to obtain a judgment provided that the pledgor is given one week's prior written notice to satisfy the claim and the loan agreement satisfies the requirements for immediate enforceability.

Notwithstanding the above, enforcement of certain types of security, for example, real estate mortgages, floating charges and dematerialised shares issued through a CSD, must be carried out in accordance with specific, statutory procedures set out in the Administration of Justice Act and the Capital Markets Act, including certain provisions regarding public auctions that may impact the timing of the enforcement. Further, a secured creditor is subject to a general duty of care obligation and obliged to look after the interests of the pledgor when enforcing security interests. No regulatory consents are otherwise required; see, however, section 8 regarding bankruptcy proceedings.

7.5 Do restrictions apply to foreign lenders in the event of (a) filing suit against a company in your jurisdiction, or (b) foreclosure on collateral security?

If required by an EU or EFTA defendant (i.e. including a Danish defendant), a foreign plaintiff not domiciled in an EU or EFTA country must furnish security for the legal costs that he might be obliged to pay as a result of the proceedings, unless such plaintiff resides in a country having entered into a bilateral treaty with Denmark permitting a plaintiff residing in Denmark to bring a legal claim against a person in that country without having to furnish security.

In general, no restrictions apply to foreign lenders in the event of foreclosure on security.

7.6 Do the bankruptcy, reorganisation or similar laws in your jurisdiction provide for any kind of moratorium on enforcement of lender claims? If so, does the moratorium apply to the enforcement of collateral security?

The Bankruptcy Act contains certain limitations on secured creditors' access to enforce security during the period when an insolvent company is taken under reconstruction proceedings. Reconstruction proceedings may be initiated by the insolvent company or any of its creditors. However, if more than 50 per cent of the creditors (based on the amounts owed to these) present at the first creditors' meeting do not support the proposed reconstruction plan and the opposing creditors constitute no less than 25 per cent of the company's total known debt, the reconstruction proceedings will immediately be terminated. See also question 8.1.

7.7 Will the courts in your jurisdiction recognise and enforce an arbitral award given against the company without re-examination of the merits?

Yes. Foreign awards based on an arbitration agreement are recognised and enforced in Denmark in accordance with the New York Convention as ratified by Denmark in 1972.

8 Bankruptcy Proceedings

8.1 How does a bankruptcy proceeding in respect of a company affect the ability of a lender to enforce its rights as a secured party over the collateral security?

Secured claims are covered prior to the statutory ranking of creditors. To the extent the value of the asset granted as security does not cover the secured claim, any uncovered part of the claim will be subject to the statutory ranking of creditors.

If the lender's claim is secured by way of a pledge (in Danish: *håndpant*) or other corresponding security interest, including a floating charge on claims (in Danish: *virksomhedspant*) or receivables charge (in Danish: *fordringspant*), the secured lender is entitled to enforce its claim independently of the bankruptcy estate.

As for other claims secured by real estate mortgage or chattel mortgage, such ordinary claims are enforced in cooperation with the bankruptcy estate. Where the estate has not made a petition for a forced sale within six month from the date of the bankruptcy order, any mortgagee with an overdue claim may demand that the estate conducts a forced sale without undue delay.

Effective as of the time of the decree of the bankruptcy proceedings, unsecured creditors cannot levy execution on the property of the insolvent debtor.

8.2 Are there any preference periods, clawback rights or other preferential creditors' rights (e.g., tax debts, employees' claims) with respect to the security?

The Bankruptcy Act includes clawback provisions which effectively set aside certain transactions executed during the period leading up to the bankruptcy proceedings provided, among other things, that:

- The transaction was made to the detriment of the creditors or result in fraudulent preference of some creditors over other creditors (e.g. in the form of presents, renunciation of inheritance, wages and other remuneration for work, early repayment of debt, provision of security without new credit being granted, etc.).
- The transaction took place after or within a specified period before the commencement of bankruptcy; i.e. within three months, six months, or – in case of related parties and provided that the burden of proof of solvency at the time of the transaction is not met or, pursuant to a recent amendment to the Bankruptcy Act taking effect on 1 January 2018, if the recipient of a gift cannot prove that the debtor undoubtedly kept sufficient assets to cover its liabilities – up to one year or two years.
- The relevant point in time to be considered when assessing if a security interest may be avoided is the time of perfection of the security interest.

In addition, the clawback provisions include an avoidance rule not limited in time applicable in the event that the debtor was or became insolvent as a consequence of the transaction and the preferred party knew or should have known of the debtor's insolvency and the circumstances causing the transaction to be fraudulent.

The said recent amendment to the Bankruptcy Act, which applies to presents granted as of 1 January 2018, expands the possibility of declaring void certain presents. By way of example, presents which are grossly disproportionate to the debtor's financial situation can be set aside even if the present was granted prior to the specified periods described above.

8.3 Are there any entities that are excluded from bankruptcy proceedings and, if so, what is the applicable legislation?

No. All natural persons and legal entities may be subject to bankruptcy proceedings.

Public authorities such as municipal authorities are excluded from bankruptcy proceedings.

As for enterprises of which the members are personally liable for the debts of the business, e.g. a partnership (in Danish: *interessentskab*) or a limited partnership (in Danish: *kommanditselskab*), a bankruptcy procedure may only be initiated if *all* such members have been declared bankrupt.

8.4 Are there any processes other than court proceedings that are available to a creditor to seize the assets of a company in an enforcement?

If a creditor is in possession of a basis of enforcement (in Danish: *eksekutionsgrundlag*) e.g. a judgment, settlement, or certain mortgages, the creditor may take the claim directly to the Bailiff's Court, without the need to obtain prior judgment, in order to enforce the security through the Bailiff's Court.

9 Jurisdiction and Waiver of Immunity

9.1 Is a party's submission to a foreign jurisdiction legally binding and enforceable under the laws of your jurisdiction?

In general, a party's submission to a foreign jurisdiction will be legally binding and enforceable under Danish law, subject to certain exceptions regarding consumers and employees.

9.2 Is a party's waiver of sovereign immunity legally binding and enforceable under the laws of your jurisdiction?

Yes, save for matters specifically protected by international law, e.g. diplomatic immunity and assets protected by diplomatic immunity or other provisions under international law.

10 Licensing

10.1 What are the licensing and other eligibility requirements in your jurisdiction for lenders to a company in your jurisdiction, if any? Are these licensing and eligibility requirements different for a "foreign" lender (i.e. a lender that is not located in your jurisdiction)? In connection with any such requirements, is a distinction made under the laws of your jurisdiction between a lender that is a bank *versus* a lender that is a non-bank? If there are such requirements in your jurisdiction, what are the consequences for a lender that has not satisfied such requirements but has nonetheless made a loan to a company in your jurisdiction? What are the licensing and other eligibility requirements in your jurisdiction for an agent under a syndicated facility for lenders to a company in your jurisdiction?

There are no licensing or other eligibility requirements in Denmark for Danish or non-Danish lenders. Granting loans without receiving deposits from the public does not in itself require authorisation. This also applies to Danish and non-Danish (security) agents under a syndicated facility. If other categories of financial activities are to be conducted, this may be subject to authorisation/licence and supervision by the Danish FSA. A financial institution, e.g. a bank or a mortgage credit institution, which is subject to the Financial Business Act, may by way of example not carry out activities until it has obtained a designated authorisation/licence from the Danish FSA.

11 Other Matters

11.1 Are there any other material considerations which should be taken into account by lenders when participating in financings in your jurisdiction?

No, there are no other material considerations which should be taken into account.

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Located in the centre of Copenhagen, Nielsen Nørager Law Firm LLP advises international and Danish clients on complex commercial transactions within finance and banking, corporate and commercial, debt and equity capital markets, private and public M&A, IPOs, securities regulation, venture and private equity, tax, and a number of other practice areas.

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Chapter 44

England

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1 Overview

1.1 What are the main trends/significant developments in the lending markets in your jurisdiction?

The United Kingdom issued formal notice of its intention to leave the European Union in March 2017, commencing the two-year period officially allocated by the EU regulations to finalise Brexit. Despite the uncertainty surrounding the final outcome of the Brexit negotiations (and the length of the transition period, if any), as well as the Catalan independence referendum in October 2017, the UK and European loan markets have proven resilient and market activity has, perhaps surprisingly, remained largely unaffected. English law continues to be the choice for almost all cross-border European deals (whether or not there is any connection with England): the UK's departure from the EU has no significant effect on English contract law, which does not derive from European law.

The trends of robust liquidity, low interest rates and fierce competition for lending mandates have continued. This, coupled with a buoyant leveraged/private equity market and a steady flow of M&A activity, has led to further improvement in the pricing and documentation terms for borrowers and sponsors. Strong investment grade borrowers also continue to dictate favourable terms, and continuing competition for lending in the mid-market and cross over space also means terms drifting in borrowers' favour. In the leveraged market, covenant-lite structures have become more popular and the pipeline for leveraged transactions remains strong. The corporate lending market is nearing a refinancing cycle as borrowers need to refinance debt which was borrowed when pricing dropped in 2014–15, and treasurers also have their eye on the potential that rising demand and reduction of excess liquidity, combined with the implementation of further bank regulation which will increase the cost of bank lending, will cause an upwards shift in pricing in the short- to medium-term.

1.2 What are some significant lending transactions that have taken place in your jurisdiction in recent years?

British American Tobacco plc completed the acquisition of the remaining 57.8% stake not already owned by it in Reynolds American Inc. in January 2017. The cash component of the acquisition was financed by a US$25bn loan facility, one of the largest syndicated financings in the European loan markets in recent years. Wood Group's US2.2bn acquisition of Amec Foster Wheeler Plc in October 2017 was supported by a US$2.75bn syndicated loan facility.

In the leveraged market, the US$5.3bn-equivalent acquisition by Hellman 7 Friedman LLC of Nets A/S, the largest European leveraged buyout in nearly five years, is being partly financed by a €2.95bn first lien loan facility.

The above facilities, in each case documented under English law, highlight the depth of the syndicated loan markets in the UK and Europe and the continuing relevance of English law in cross-border M&A transactions and the European loan markets more generally.

2 Guarantees

2.1 Can a company guarantee borrowings of one or more other members of its corporate group (see below for questions relating to fraudulent transfer/financial assistance)?

Generally yes, provided there is adequate corporate benefit (which need not be direct financial benefit but can include less tangible factors such as management support) and the company has the capacity to give the guarantee.

2.2 Are there enforceability or other concerns (such as director liability) if only a disproportionately small (or no) benefit to the guaranteeing/securing company can be shown?

In general, directors are required to act in good faith and have a duty to promote the success of the company for the benefit of its members as a whole. In normal circumstances, where directors form a view that giving the guarantee promotes the success of the company because of the benefits to the borrower, guarantees for no direct benefit are valid. Downstream guarantees are generally no problem; for upstream or cross-stream guarantees it is necessary for the director to apply more thought to these matters. On the other hand, if the company is of doubtful solvency and a long-term view is unrealistic, this duty is displaced with a duty to have regard to the interests of the creditors of the company (taking precedence over the interests of members). If there is no reasonable prospect that the company can avoid insolvent liquidation or administration, directors should also be mindful of wrongful trading liability. In certain circumstances, a guarantee may be set aside as a preference or due to the insolvency of the company (see question 8.2).

Recent commentary by the Institute of Chartered Accountants of England and Wales has questioned whether a company ought to be able to ascribe no liability, in the Company's accounts, to a guarantee given in respect of a parent company even if the directors assess that there is a low likelihood of the parent company failing to pay and the guarantee being called. For the time being, this issue remains under consideration and market practice has not changed, but if the ICAEW view were to prevail then directors may find it less easy to give upstream guarantees.

2.3 Is lack of corporate power an issue?

Lack of corporate power would not necessarily make a guarantee void; however, the capacity of a company to enter into a guarantee should be checked by looking at its memorandum (if any) and articles of association. The company's objects will often include an express power to grant guarantees, but even if this is not expressly stated then the objects may be wide enough to cover granting guarantees if that is ancillary to the business.

2.4 Are any governmental or other consents or filings, or other formalities (such as shareholder approval), required?

Generally no; however, there may be particular requirements in the case of regulated entities. A shareholder resolution is also often provided to mitigate corporate benefit concerns.

A guarantee is required to be in writing, signed by the guarantor.

Guarantees are often executed as a deed to avoid any arguments regarding due consideration.

2.5 Are net worth, solvency or similar limitations imposed on the amount of a guarantee?

No, although directors should consider the solvency of the company as part of promoting its success and best interests.

2.6 Are there any exchange control or similar obstacles to enforcement of a guarantee?

No, although it is prudent to check whether non-English exchange control or sanctions considerations will apply to a guarantee given by a non-UK company or which relies on recourse to non-UK assets.

3 Collateral Security

3.1 What types of collateral are available to secure lending obligations?

It is possible to take security over all types of asset of an English company.

3.2 Is it possible to give asset security by means of a general security agreement or is an agreement required in relation to each type of asset? Briefly, what is the procedure?

Security over all or substantially all of a company's assets may be given by a single document, known as a debenture (not the same as a fixed income share of a company, which confusingly is also known as a debenture).

A debenture usually includes:

(a) a fixed charge over assets which are identifiable and can be controlled by the creditors (e.g. restricted accounts);

(b) a floating charge which is used to capture fluctuating and less identifiable assets (e.g. inventory);

(c) an assignment of receivables and contracts; and

(d) mortgages over real estate and shares.

If the debenture includes a real estate mortgage or a power of attorney, it must be executed as a deed (see question 3.13). In practice, security documents are almost always executed as deeds.

There is no universal registration of perfection (like UCC filings in the United States), so perfection of security over assets is required depending on the type of asset (see questions 3.3 to 3.7). Consideration should also be given to whether additional formalities or documents should be used when securing assets of an English company which are not based in England or when taking security over particular types of assets, e.g. ships.

3.3 Can collateral security be taken over real property (land), plant, machinery and equipment? Briefly, what is the procedure?

Security over land is ideally taken by way of a legal mortgage. A legal mortgage transfers legal title to the creditor and restricts the chargor from taking certain actions while the asset is subject to the mortgage e.g. disposing of or mortgaging the asset further without consent. A legal mortgage cannot be granted over future acquired assets.

It is also possible to create an equitable mortgage over land where the beneficial title in the land is transferred to the creditor but legal title remains with the chargor. We often see an equitable mortgage where the parties have agreed that a legal mortgage will only come into effect if certain events occur or where the formalities required for a legal mortgage cannot be met. An equitable mortgage suffers from certain disadvantages compared to a legal mortgage but, except in the case of fraud by the chargor, these disadvantages are often accepted.

When taking security over land, consider whether the chargor is required to obtain third-party consents (for example, from the freeholder if security relates to leasehold title). Security should be registered with the Land Registry in most circumstances.

Security over plant, machinery and equipment may be caught by a legal mortgage over the land if those assets are sufficiently attached to the mortgaged land; however, a fixed charge is usually granted over these types of assets. A fixed charge is generally only used for identifiable assets and where a creditor is able to show sufficient control over the asset. There are no specific documentation formalities required for creating a fixed charge.

3.4 Can collateral security be taken over receivables? Briefly, what is the procedure? Are debtors required to be notified of the security?

Yes, usually by way of an assignment (subject to such receivables being assignable) but can also be covered by a fixed charge (see question 3.2 above) or a floating charge (see question 3.5 below).

An assignment of receivables can be legal or equitable. A legal assignment must be in writing, signed by the assignor, absolute (unconditional and irrevocable) and notice must be given to the relevant third parties. If any of these conditions are not met then the assignment will be an equitable assignment. The main benefits of a legal assignment are (a) the creditor can sue in its own name (if it is an equitable assignment the creditor would have to join the assignor as a third party to any suit), and (b) the third party (once notice has been served) will only be able to discharge its obligations to, or as directed by, the creditor.

It is common for certain assignments to be equitable assignments until a trigger event occurs and the assignor is then required to give notice to the third party (and the legal assignment is perfected), but this is dependent upon negotiation. Acknowledgment of the notice by the third party is often requested but does not affect the nature or validity of the assignment.

3.5 Can collateral security be taken over cash deposited in bank accounts? Briefly, what is the procedure?

Yes, by a fixed or floating charge.

A fixed charge over a bank account is generally only effective where the account is blocked such that the chargor can only make withdrawals with the creditor's permission. A floating charge allows the chargor to continue to deal with the account in the ordinary course until there is a trigger event (usually a default), at which point the creditor may notify the account bank that it controls the account. A trading account would only be subject to a floating charge, as the business would need constant access to the account and seeking lender consent would be impractical.

Whether a charge is fixed or floating will be dependent on the level of control the creditor has over the account. A floating charge ranks below certain other claims in an insolvency, such as a ring-fenced fund for unsecured creditors and (more importantly in large transactions) expenses of the liquidation or administration.

3.6 Can collateral security be taken over shares in companies incorporated in your jurisdiction? Are the shares in certificated form? Can such security validly be granted under a New York or English law governed document? Briefly, what is the procedure?

Shares in English companies are required to be registered and may be certificated or uncertificated (and held in a clearing system).

Security over shares in an English company should be effected by an English law security document.

Shares are usually charged by way of a mortgage or fixed charge. A legal mortgage over certificated shares involves transferring ownership of the shares to the creditor and registering the creditor in the shareholder register. The share certificate in the chargor's name will be cancelled and replaced with one in the creditor's name. A legal mortgage allows the lender to vote the shares, receive any dividends and any information about the shares until the debt is discharged.

Often an equitable mortgage is granted subject to the creditor being able to create a legal mortgage if certain trigger events occur. This is achieved by delivering share certificates and a signed but undated stock transfer form to the creditor. If the security becomes enforceable the creditor can complete the undated stock transfer form and any formalities required to become legal holder of the shares. Prior to the security being enforceable all voting rights, dividends and any communication about the shares will remain with the chargor.

Uncertificated shares can be secured by an equitable or legal mortgage. In order to hold uncertificated shares, the creditor will need a securities account with the clearing system (or with a financial institution which has such an account). A legal mortgage will be perfected by an instruction to the clearing system to transfer the shares to the securities account of the creditor.

An equitable mortgage of shares in a clearing system is created by depositing the shares into an escrow account with the clearing system and restricting withdrawals without the creditor's permission.

If a legal mortgage over shares is taken and perfected so that the shares are transferred to the mortgage, then the mortgage is likely to become a "person with significant control" (PSC) under the PSC regime. The mortgage will then be subject to legal obligation to provide information about itself to the mortgagor. That information will become public information. Failure to provide this information is a criminal offence. These obligations do not arise under an equitable mortgage (which is the more common approach to share security) and so are not usually a concern.

When taking security over companies subject to the PSC regime, mortgagees should ensure that they are protected against the risk of a restrictions notice being issued in respect of the shares. A restrictions notice effectively freezes the interest so the security cannot be enforced, dividends cannot be paid nor voting rights exercised. Protection against this risk requires market standard PSC provisions to be included in the credit or security agreement.

Other considerations include: stock exchange notification requirements; tax implications; and restrictions in the company's constitutional documents (such as liens, pre-emption rights or a right to refuse to register a transfer).

3.7 Can security be taken over inventory? Briefly, what is the procedure?

Yes. Typically a floating charge is most appropriate given the fluctuating nature of inventory and the inability of a secured creditor to exercise sufficient control for a fixed charge. See question 3.5 above.

3.8 Can a company grant a security interest in order to secure its obligations (i) as a borrower under a credit facility, and (ii) as a guarantor of the obligations of other borrowers and/or guarantors of obligations under a credit facility (see below for questions relating to the giving of guarantees and financial assistance)?

Yes, subject to corporate benefit and solvency considerations similar to those for a guarantee (see questions 2.1 to 2.3 above).

3.9 What are the notarisation, registration, stamp duty and other fees (whether related to property value or otherwise) in relation to security over different types of assets?

Registration requirements depend on the type of secured asset. The majority of charges created by an English company must be registered at Companies House within 21 days of its creation. Failure to register within this time means that the charge will be void against the liquidator, administrator or any creditor of the company and the money secured by the charge becomes immediately payable.

A prescribed form must be completed to register the security along with supporting documentation and payment of a fee (£23 paper filing and £15 online filing). This registration is a statutory requirement but is not a universal perfection filing (like UCC in the United States) – it does not remove the need to perfect security over specific assets.

Security over English real estate must be registered at the land registry and security over certain other assets, such as IP, ships and aircraft, needs to be registered at applicable registries.

There are no notarisation requirements for security documents under English law.

See question 6.2 regarding stamp duty.

3.10 Do the filing, notification or registration requirements in relation to security over different types of assets involve a significant amount of time or expense?

No, prescribed forms need to be completed (see question 3.9 above) and payment of minor fees.

3.11 Are any regulatory or similar consents required with respect to the creation of security?

Generally no; however, consider requirement for third-party consents under underlying contracts. Additional consents may be required if involving regulated entities or assets.

3.12 If the borrowings to be secured are under a revolving credit facility, are there any special priority or other concerns?

Generally, no.

3.13 Are there particular documentary or execution requirements (notarisation, execution under power of attorney, counterparts, deeds)?

Creditors generally expect to receive board and/or shareholder minutes approving the documentation for evidentiary purposes and to ensure corporate benefit issues have been considered.

A legal mortgage over land must be in writing, signed by all parties, incorporate all terms expressly agreed and fulfil the requirements of a deed.

A deed must be in writing, clear from its face that it is a deed, validly executed as a deed and must be delivered.

Security agreements usually contain a power of attorney and therefore will need to be executed as a deed.

Other guidelines should be considered, such as law society practice notes and recent case law which states that each party must approve and intend for their signature to be attached to a final form document. Exchanging pre-signed signature pages is not sufficient to execute certain documents effectively.

4 Financial Assistance

4.1 Are there prohibitions or restrictions on the ability of a company to guarantee and/or give security to support borrowings incurred to finance or refinance the direct or indirect acquisition of: (a) shares of the company; (b) shares of any company which directly or indirectly owns shares in the company; or (c) shares in a sister subsidiary?

(a) Shares of the company

A private company can provide financial assistance (including guarantees and security) for the acquisition of its own shares.

Subject to limited exceptions, a public company is prohibited from giving financial assistance for the acquisition of its own shares.

(b) Shares of any company which directly or indirectly owns shares in the company

Private companies can provide financial assistance for the acquisition of shares in a private holding company but not a public holding company.

Public companies are prohibited from providing financial assistance to both public and private holding companies subject to limited exceptions.

(c) Shares in a sister subsidiary

There is no prohibition on financial assistance provided for the purchase of shares in a sister subsidiary.

5 Syndicated Lending/Agency/Trustee/ Transfers

5.1 Will your jurisdiction recognise the role of an agent or trustee and allow the agent or trustee (rather than each lender acting separately) to enforce the loan documentation and collateral security and to apply the proceeds from the collateral to the claims of all the lenders?

Yes, this is usually governed by the agency provisions in the loan documentation and intercreditor or security agreement. The intercreditor agreement will govern how proceeds from security enforcement will be applied.

5.2 If an agent or trustee is not recognised in your jurisdiction, is an alternative mechanism available to achieve the effect referred to above which would allow one party to enforce claims on behalf of all the lenders so that individual lenders do not need to enforce their security separately?

Agency and trust relationships are well established in England.

5.3 Assume a loan is made to a company organised under the laws of your jurisdiction and guaranteed by a guarantor organised under the laws of your jurisdiction. If such loan is transferred by Lender A to Lender B, are there any special requirements necessary to make the loan and guarantee enforceable by Lender B?

Syndicated loans are generally structured so that they are transferrable from one lender to another by using a prescribed form of transfer certificate subject to any restrictions in the loan documentation. A transfer of the loan will also transfer the benefit of any English security or guarantee.

If a loan has not been structured in this way then (assuming no contractual prohibitions to the contrary) it is possible to assign the benefit of the loan and guarantee to Lender B by giving notice to the borrower and guarantor. Care should be taken if the loan is a revolving credit or not fully drawn, as (a) the obligation to lend cannot be transferred by assignment (so Lender A would still be required to make further advances) and (b) any future drawings may not benefit from the guarantee.

6 Withholding, Stamp and other Taxes; Notarial and other Costs

6.1 Are there any requirements to deduct or withhold tax from (a) interest payable on loans made to domestic or foreign lenders, or (b) the proceeds of a claim under a guarantee or the proceeds of enforcing security?

Yes, a company paying "yearly interest" that arises in the UK is required to withhold income tax from that interest at a rate of (currently) 20%. Interest will be "yearly interest" for these purposes if, in broad terms, the debt is capable of being outstanding for a year or more.

There are several exceptions. In the context of a commercial bank loan, the most important exception is that for interest payable on an advance from a "bank", where the person beneficially entitled to the interest is within the charge to UK corporation tax in respect of that interest, or would have been within the charge to UK corporation tax in respect of the interest but for the exemption from UK corporation tax for foreign branches of UK companies.

Other possible exemptions include: interest paid by a bank in the ordinary course of the bank's business; interest paid to a company within the charge to UK corporation tax; and interest payable without deduction under a direction to pay gross pursuant to a double tax treaty.

UK law is not clear on the treatment of payments made under a guarantee. They could be characterised as being of the same nature as the underlying obligation (i.e. interest or principal), or as a separate obligation.

6.2 What tax incentives or other incentives are provided preferentially to foreign lenders? What taxes apply to foreign lenders with respect to their loans, mortgages or other security documents, either for the purposes of effectiveness or registration?

There are no preferential tax incentives for foreign lenders lending into the UK.

Note that UK stamp duty could be payable on the transfer or assignment of certain loans (whether the lender is foreign or domestic). In addition, if the loan is a "chargeable security", UK stamp duty reserve tax (SDRT) could be chargeable in respect of an agreement to transfer the loan.

An exemption from UK stamp duty and SDRT applies to loans which are "exempt loan capital". A typical bank loan is likely to be "loan capital". However, if the loan has certain equity-like characteristics (e.g. convertibility, results-dependency, excessive rate of interest), it will not be "exempt". It is rare for bank loans to carry such rights, although there may be concerns where loans carry a margin ratchet or are limited recourse. Where a loan is not exempt loan capital, other exemptions from stamp duty and SDRT may be available.

The grant of security over assets should not be subject to UK stamp duties or taxes. There may be a liability to UK stamp duties or taxes on enforcement of security over shares or securities of a UK company or UK real estate.

6.3 Will any income of a foreign lender become taxable in your jurisdiction solely because of a loan to or guarantee and/or grant of security from a company in your jurisdiction?

By themselves, these factors should not bring a non-UK lender into the charge to UK tax (although, as discussed above, a foreign lender may be subject to UK withholding tax).

6.4 Will there be any other significant costs which would be incurred by foreign lenders in the grant of such loan/guarantee/security, such as notarial fees, etc.?

See question 3.9 above.

6.5 Are there any adverse consequences to a company that is a borrower (such as under thin capitalisation principles) if some or all of the lenders are organised under the laws of a jurisdiction other than your own? Please disregard withholding tax concerns for purposes of this question.

Results-dependent interest will be characterised as a non-deductible distribution of the borrower for UK tax purposes. There is an exemption from this rule where the recipient of the interest is within the charge to UK corporation tax. Therefore, a borrower might be disadvantaged in such circumstances where a lender is outside the UK tax net. There is, however, an exemption for certain margin ratchets which does not depend on the location of the lender. In certain circumstances, UK anti-arbitrage legislation may be potentially applicable to cross-border financing arrangements.

Otherwise, the location of an unconnected lender should not concern the borrower.

7 Judicial Enforcement

7.1 Will the courts in your jurisdiction recognise a governing law in a contract that is the law of another jurisdiction (a "foreign governing law")? Will courts in your jurisdiction enforce a contract that has a foreign governing law?

The English courts will generally apply a foreign law as the governing law of a contract if it is expressly chosen by the parties, subject to the following: (i) where all elements relevant to the situation at the time of the choice are located in a country other than the country whose law has been chosen, the choice of law will not prejudice the application of non-derogable laws of that other country; (ii) where all elements relevant to the situation at the time of the choice are located in one or more EU Member States, the choice of a non-EU Member State law will not prejudice the application of non-derogable provisions of EU community law; (iii) the chosen law will not restrict the application of overriding mandatory provisions of English law; (iv) effect may be given to overriding mandatory provisions of the law of the country where the obligations arising out of the contract have to be or have been performed, insofar as those overriding mandatory provisions render the performance of the contract unlawful; (v) the English courts may refuse to apply a provision of the chosen law if such application is manifestly incompatible with English public policy; (vi) in relation to the manner of performance and the steps to be taken in the event of defective performance, regard will be given to the law of the country in which performance takes place; and (vii) the chosen law may not be applied to determine certain questions in relation to the existence and validity of a contract.

As well as potentially applying local public policy and mandatory rules, the English courts may, in limited circumstances, also apply non-derogable or mandatory rules of another country. Given that the circumstances in which the English courts will refuse to apply the chosen law are narrow, the basic position is that the English court will generally respect the chosen law.

7.2 Will the courts in your jurisdiction recognise and enforce a judgment given against a company in New York courts (a "foreign judgment") without re-examination of the merits of the case?

A foreign judgment would generally be treated as constituting a cause of action against the judgment debtor and could be sued upon summarily in the English courts. The English courts should enter judgment in such proceedings, without re-examination of the merits of the original judgment, provided that: (i) the New York court was of competent jurisdiction and the foreign judgment is final and conclusive; (ii) the foreign judgment is not for multiple damages or on a claim for contribution in respect of multiple damages; (iii) the foreign judgment is for a fixed sum of money and not payable in respect of a tax, fine or penalty; (iv) the foreign judgment was not given in proceedings brought in breach of a dispute resolution agreement (unless the proceedings were brought with the agreement of judgment debtor or the judgment debtor counterclaimed in the proceedings or otherwise submitted to the jurisdiction); (v) the foreign judgment was not obtained by fraud, or in proceedings contrary (a) to natural justice, (b) to the Human Rights Act 1998, (c) to the principles of the European Convention on Human Rights, (d) to the Charter of Fundamental Rights of the European Union, (e) or to English public policy; (vi) enforcement proceedings are instituted within six years after the date of the judgment; (vii) the foreign judgment is not inconsistent with an earlier judgment in proceedings between the same parties or their privies; and (viii) the foreign judgment is not contrary to the Protection of Trading Interests Act 1980 or any powers exercised under the 1980 Act.

There is doubt as to the enforceability in England and Wales of U.S. judgments in respect of civil judgments predicated purely on U.S. securities laws.

Different considerations may apply if the judgment debtor is a state entity.

7.3 Assuming a company is in payment default under a loan agreement or a guarantee agreement and has no legal defence to payment, approximately how long would it take for a foreign lender to (a) assuming the answer to question 7.1 is yes, file a suit against the company in a court in your jurisdiction, obtain a judgment, and enforce the judgment against the assets of the company, and (b) assuming the answer to question 7.2 is yes, enforce a foreign judgment in a court in your jurisdiction against the assets of the company?

The answer is context-specific and dependent upon the court diary.

(a) If the enforcement of an English law-governed contract in England is uncontested and there is no dispute as to jurisdiction, a judgment in default could be obtained in 1–2 months. If the company files a defence but the foreign lender is able to obtain summary judgment, this could take 2–3 months. If the enforcement is heavily contested and there is a material dispute about the facts then it could take longer. If the governing law of the contract is not English law then the proceedings may take longer since the court will need to hear expert evidence on that foreign governing law. In terms of enforcing a judgment, once given, against assets, the time taken will depend upon which assets and what method of enforcement is chosen.

(b) For enforcement of a foreign judgment against assets, the timing would be no different.

7.4 With respect to enforcing collateral security, are there any significant restrictions which may impact the timing and value of enforcement, such as (a) a requirement for a public auction, or (b) regulatory consents?

Generally no, but regulatory consents may be required if the company is a regulated entity or the assets are regulated.

7.5 Do restrictions apply to foreign lenders in the event of (a) filing suit against a company in your jurisdiction, or (b) foreclosure on collateral security?

No, foreign lenders are essentially treated the same as domestic lenders. It may, however, be more likely that a court would make an order for security for costs against foreign lenders.

7.6 Do the bankruptcy, reorganisation or similar laws in your jurisdiction provide for any kind of moratorium on enforcement of lender claims? If so, does the moratorium apply to the enforcement of collateral security?

In liquidation, the aim is to realise the unsecured assets of the company for the benefit of creditors as a whole (save for secured creditors, who have recourse to the secured assets). Security rights against the company remain enforceable. In a compulsory liquidation, there is a limited moratorium meaning that no action or proceedings can be commenced or proceeded with against the company or its property without court permission. In the case of a creditors' voluntary liquidation, the liquidator may apply for a stay of such proceedings to ensure equal distribution of the assets.

In administration, an interim statutory moratorium on creditor action comes into effect on the presentation of an administration application in court or the filing in court of a notice of intention to appoint an administrator. This prevents, among other things, the enforcement of security and the commencement of legal proceedings without the permission of the court and a permanent moratorium will come into effect upon the appointment of an administrator (the interim moratorium falling away if the appointment is not made) which cannot be lifted without with consent of the court or the administrator.

A limited 28-day moratorium is available in a CVA but only for "small companies".

Subject to certain conditions, the enforcement of financial collateral security (which is, broadly, security over cash, shares, tradeable bonds and certain loans which meet other specified criteria) is exempt from the security enforcement moratorium.

A scheme of arrangement does not impose a moratorium on creditor action but may cram down dissenting secured creditors who will be bound by the scheme if approved by the requisite statutory majorities.

Special insolvency measures apply to credit institutions and investment firms under the Banking Act 2009, pursuant to which the resolution authorities have wide powers to impose a variety of stays.

7.7 Will the courts in your jurisdiction recognise and enforce an arbitral award given against the company without re-examination of the merits?

The award of an English seated arbitration tribunal may be enforced, with the permission of the English court, in the same manner as a judgment or order of the court to the same effect without any re-examination of the merits. This is subject to a challenge as to the substantive jurisdiction of the tribunal, on grounds of a serious procedural irregularity or an appeal on a question of law (the latter may be excluded by the parties in their agreement to arbitrate).

The grounds for refusing an award of a tribunal seated in a jurisdiction which has ratified the New York Convention are limited. They are: (a) that a party to the arbitration agreement was (under the law applicable to it) under some incapacity; (b) that the arbitration agreement was not valid under the law to which the parties subjected it or, failing any indication thereon, under the law of the country where the award was made; (c) that it was not given proper notice of the appointment of the arbitrator or the arbitration proceedings or was otherwise unable to present its case; (d) that the award deals with a difference not contemplated by or not falling within the terms of the submission to arbitration or contains decisions on matters beyond the scope of the submission to arbitration; (e) that the composition of the arbitral tribunal or the arbitral procedure was not in accordance with the agreement of the parties or, failing such agreement, with the law of the country in which the arbitration took place; and (f) that the award has not yet become binding on the parties, or has been set aside or suspended by a competent authority of the country in which, or under the law of which, it was made.

8 Bankruptcy Proceedings

8.1 How does a bankruptcy proceeding in respect of a company affect the ability of a lender to enforce its rights as a secured party over the collateral security?

The statutory moratorium (which will arise in an administration and in some CVAs; see question 7.6 above) will restrict a creditor from enforcing its security rights including, for example, by appointing a receiver (see question 7.6 above).

However, if during the interim moratorium a secured creditor appoints an administrative receiver before the appointment of the administrator becomes effective, it will not be possible for an administrator to be appointed (and the interim moratorium on enforcement of security will terminate and the permanent moratorium will not come into effect). This 'trumping' of appointments only applies where the receiver appointed is an administrative receiver. Where a non-administrative receiver is appointed, an administrator can still be appointed and the administrator can require the receiver to vacate office even though the receivership enforcement process has commenced, although there are certain protections for secured creditors.

The ability to appoint an administrative receiver is only available in limited circumstances. For this reason, a secured creditor who is a 'qualifying floating charge holder' (a holder of security, including a floating charge over the whole or substantially the whole of the company's assets) may instead appoint an administrator out of court as a means of enforcing its security. Unlike a receiver, an administrator is required to act in the interests of all creditors.

8.2 Are there any preference periods, clawback rights or other preferential creditors' rights (e.g., tax debts, employees' claims) with respect to the security?

Liquidators and administrators are granted wide anti-avoidance powers to challenge certain types of transactions entered into by a company before insolvency. Clawback could be available in relation to certain transactions, such as transactions at an undervalue, preferences or floating charges.

Certain conditions must be met for clawback to be available including:

- the company must be either in liquidation or administration;
- the company must have been unable to pay its debts when the transaction was entered into or as a result of entering into the transaction;
- an unfair advantage was gained by the party contracting with the company, or there is an absence of adequate consideration flowing to the company, as a result of the transaction; and
- the transaction was entered into during the relevant look-back period which varies (generally ranges from six months to two years).

Certain claims are treated as preferential and hence the order of priority in which a company's assets will be distributed is broadly: (i) fixed-charge holders' claims out of the fixed charge assets (if the assets are insufficient to meet these claims then the secured creditor will have a claim as an unsecured creditor for the surplus); (ii) insolvency expenses; (iii) preferential claims (primarily employee and certain pension contribution claims, but not tax claims); (iv) prescribed part fund (paid *pro rata* to unsecured claimants out of floating charge assets ahead of floating charge creditors – up to a maximum of £600,000 per company); (v) floating charge claims; and (vi) unsecured claims.

8.3 Are there any entities that are excluded from bankruptcy proceedings and, if so, what is the applicable legislation?

The starting position is that the corporate insolvency regimes under the Insolvency Act 1986 apply to companies registered in the United Kingdom.

However, by virtue of EC Regulation, insolvency proceedings can only be opened as main proceedings in the place where the debtor has its 'centre of main interests' (COMI). The Insolvency Act 1986 therefore provides that insolvency proceedings are available to a company which is incorporated in an EEA State other than the UK and a company not incorporated in an EEA State but having its COMI in a Member State (other than Denmark), subject to the overriding requirement that the COMI must be in the UK. Secondary proceedings can be opened in a Member State where the debtor has an "establishment" but these are limited to local assets in the jurisdiction.

Modified versions of the Insolvency Act regimes also apply to certain types of debtors/businesses, such as partnerships.

Special legislation and special insolvency regimes may apply to certain businesses (e.g. banks/credit institutions and investment firms).

8.4 Are there any processes other than court proceedings that are available to a creditor to seize the assets of a company in an enforcement?

The five main (out-of-court) remedies generally available to a creditor to enforce its security are:

1. going into possession;
2. exercising the power of sale;
3. appointment of a receiver;
4. appointment of an administrator; and
5. appropriation of financial collateral.

Foreclosure is also an enforcement process but requires a court order. Appropriation of an asset does not require a court order but can only be used to enforce financial collateral and is subject to certain conditions.

The preferred method for enforcing security is usually the appointment of a receiver or administrator (in circumstances where any receiver would be an administrative receiver and such an appointment would be prohibited).

9 Jurisdiction and Waiver of Immunity

9.1 Is a party's submission to a foreign jurisdiction legally binding and enforceable under the laws of your jurisdiction?

The English courts will usually decline jurisdiction if the parties have agreed that a foreign court is to have exclusive jurisdiction. However, the English courts may assume jurisdiction in special cases, for example: (i) if they have exclusive jurisdiction, such as in a dispute relating to rights *in rem* in land or corporate constitutional issues; (ii) in relation to certain insurance, consumer and employment contracts; (iii) if the defendant has taken steps in the proceedings in the English courts; and (iv) in certain narrow circumstances, if the court considers that it is the appropriate forum to hear the dispute. This principle is rarely applied where exclusive jurisdiction has been conferred on a foreign court. It is not applied where the chosen court is that of an EU Member State.

9.2 Is a party's waiver of sovereign immunity legally binding and enforceable under the laws of your jurisdiction?

The English courts will normally give effect to a clause in an agreement that provides for (i) the submission by a foreign state to what the courts describe as their "adjudicative jurisdiction" (i.e. the courts' power to adjudicate upon claims against foreign states, which includes recognising a foreign judgment or arbitral award), and (ii) the consent in writing of a foreign state to: (a) relief against the foreign state by way of injunction or order for specific performance or for the recovery of land or other property; and (b) the property of the foreign state being subject to any process for the enforcement of a judgment or arbitration award or, in an action *in rem*, for its arrest, detention or sale, provided, in the case of both (i) and (ii) that the agreement is sufficiently clear and the agreement is within the scope of and is permitted by the State Immunity Act 1978.

Central banks are afforded greater protection than foreign states under the 1978 Act. Different considerations apply to the immunity of international organisations, as well as to diplomatic or consular immunity.

The common law has a concept of "non-justiciability" or "act of state doctrine" which means that certain matters are not capable of being adjudicated by the English courts.

10 Licensing

10.1 What are the licensing and other eligibility requirements in your jurisdiction for lenders to a company in your jurisdiction, if any? Are these licensing and eligibility requirements different for a "foreign" lender (i.e. a lender that is not located in your jurisdiction)? In connection with any such requirements, is a distinction made under the laws of your jurisdiction between a lender that is a bank versus a lender that is a non-bank? If there are such requirements in your jurisdiction, what are the consequences for a lender that has not satisfied such requirements but has nonetheless made a loan to a company in your jurisdiction? What are the licensing and other eligibility requirements in your jurisdiction for an agent under a syndicated facility for lenders to a company in your jurisdiction?

There are generally no eligibility requirements, although certain types of lending are regulated in England (e.g. consumer credit).

11 Other Matters

11.1 Are there any other material considerations which should be taken into account by lenders when participating in financings in your jurisdiction?

Article 55 of the European Union's Bank Recovery and Resolution Directive (2014/59/EU) requires a wide range of non-EU law governed contracts entered into by certain EU financial institutions, investment firms and their related entities to include wording by which the counterparty recognises that the in-scope entity's liabilities may be subject to bail-in by relevant EU authorities (broadly, the counterparty's claims may be written down or converted to equity).

Brexit negotiations are continuing and, with the March 2019 deadline looming for formalising the UK's exit from the European Union, there is so far limited progress. The final terms of the exit, and the UK's future relationship with the European Union, may impact the law in the UK relevant to financing transactions and the predominantly English law-governed loan documentation used in the European loan markets but the extent of the impact may well take some time to discern. It is largely (although not exclusively) expected that English law will continue to be used for cross-border European finance transactions.

The UK Financial Conduct Authority (**FCA**) has recently indicated that the use of LIBOR as the benchmark rate across a broad range of financing transactions may no longer be sustainable beyond 2021. The unsecured wholesale term lending market for banks has not been sufficiently active to support a transaction-based LIBOR for a number of years and panel banks have been increasingly reluctant to submit rates based on expert judgement. The FCA has effectively aimed to focus market participants on identifying and transitioning to a viable replacement rate while minimising market disruption. The Bank of England has recently proposed SONIA (Sterling Over Night Index Average) as its preferred replacement rate for LIBOR but market discussions on finding a workable solution and agreeing corresponding amendments to finance documentation topic are at an early stage.

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Finland

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1 Overview

1.1 What are the main trends/significant developments in the lending markets in your jurisdiction?

Nordic banks remain strong, although international banks, especially German banks, continue to increase their market share. Competition among lenders is fairly intense as many Finnish blue chip companies have limited need for debt funding due to strong balance sheets and plenty of liquidity. The debt capital markets in Finland have also been developing strongly during the past five years and an increasing number of, particularly, publicly traded companies, but also private companies, have raised funding through bond financing. A number of large Finnish publicly traded companies have Euro Medium Term Note programmes in place and the Finnish corporate bond market, where bonds are issued under local law documentation, has developed favourably. In terms of industries, real estate financing has also grown increasingly over the past few years thanks to several significant real estate transactions in Finland.

2 Guarantees

2.1 Can a company guarantee borrowings of one or more other members of its corporate group (see below for questions relating to fraudulent transfer/financial assistance)?

Finnish limited liability companies are generally free to guarantee the financial obligations of one or more members of their corporate group, subject, however, to certain limitations described under questions 2.2 and 4.1 below.

2.2 Are there enforceability or other concerns (such as director liability) if only a disproportionately small (or no) benefit to the guaranteeing/securing company can be shown?

Potential concerns of, in particular, unlawful financial assistance and distribution of assets may arise in relation to upstream as well as cross-stream guarantees and security (on financial assistance, please see section 4 below). If the provision of a guarantee or security reduces the assets of a company or increases its liabilities without such company obtaining sufficient corporate benefit therefrom, such actions may constitute unlawful distribution of assets under the Companies Act (624/2006, as amended, the "**Companies Act**").

In addition to such corporate benefit requirement, provision of the guarantee/security: (i) must fall within the company's business purpose; (ii) may not contravene the provisions of the Companies Act regarding the equality of shareholders; and (iii) may not result in the company becoming insolvent, nor may the company be insolvent at the time of granting the guarantee/security.

Failure to comply with the above requirements may constitute breach of the general duty of care imposed on the Board of Directors and the managing director of a Finnish limited liability company pursuant to the Companies Act and result in liability to pay damages to the company, its shareholders or third parties or even criminal sanctions if such distribution constitutes deliberate violation of the protection of the company's shareholders or creditors.

In order to alleviate the above concerns, finance documents typically include wording limiting any guarantees and security provided by Finnish companies to the extent that the provision of such guarantees or security would be contrary to the mandatory provisions of the Companies Act regarding financial assistance and/or unlawful distribution of assets or, in the case of companies that do not apply the Companies Act (e.g. housing companies that apply the Housing Companies Act (1599/2009, as amended)), other mandatory provisions of Finnish corporate law. Kindly note that in this chapter, we focus only on Finnish limited liability companies applying the Companies Act unless otherwise specifically noted.

2.3 Is lack of corporate power an issue?

Lack of corporate power is generally not an issue *per se*, with the provision of guarantees and security usually being resolved upon by the Board of Directors or, if such action falls within the ordinary course of business, even the managing director. The general duty of care requirements and risk of unlawful financial assistance and distribution of assets described under question 2.2 above and section 4 below may, however, impose *de facto* limitations on the provision of guarantees and/or security.

2.4 Are any governmental or other consents or filings, or other formalities (such as shareholder approval), required?

No governmental or other consent or filing is required in order for a Finnish limited liability company to provide guarantees. Please, however, see question 3.9 below regarding registration requirements in respect of certain security assets. Although not an absolute legal requirement, shareholder approval is customarily requested as a condition precedent in financing arrangements.

2.5 Are net worth, solvency or similar limitations imposed on the amount of a guarantee?

Although there are no limitations on the amount of a guarantee *per se*, the provisions of the Companies Act may in practice limit the amount of a guarantee that can be considered valid and enforceable. In particular, Finnish limited liability companies may not provide guarantees if doing so would violate the provisions of the Companies Act relating to unlawful financial assistance or distribution of assets, or endanger the guarantor's solvency. Please see question 2.2 above and questions 4.1 and 8.2 below.

2.6 Are there any exchange control or similar obstacles to enforcement of a guarantee?

There are no exchange control or similar obstacles in Finland restricting the enforcement of guarantees issued by Finnish limited liability companies.

3 Collateral Security

3.1 What types of collateral are available to secure lending obligations?

Under Finnish law, various types of security assets (including but not limited to shares, real estate, business mortgage and receivables) may be pledged as security. In order to validly pledge an asset, such asset must be: (i) sufficiently individualised; (ii) separately transferable and capable of being foreclosed on; and (iii) have monetary value.

3.2 Is it possible to give asset security by means of a general security agreement or is an agreement required in relation to each type of asset? Briefly, what is the procedure?

Under Finnish law, it is possible and common market practice to grant security over various assets by way of a single omnibus security agreement.

3.3 Can collateral security be taken over real property (land), plant, machinery and equipment? Briefly, what is the procedure?

Under Finnish law, security over real property is taken by registering a real estate mortgage on the relevant real estate (or e.g. a part or parcel thereof or leasehold registered thereon) and perfected by: (i) in the case of an electronic real estate mortgage, registering the pledgee as the holder thereof (such application can be made by the then registered holder of the mortgage); or (ii) in case of existing physical real estate mortgage note(s), by delivering the real estate mortgage note(s) representing such real estate mortgage to the possession of the pledgee or its order. Electronic real estate mortgages have recently replaced physical notes and it is no longer possible to apply for the registration of a new real estate mortgage evidenced by a physical mortgage note. Currently existing physical mortgage notes can be used as security until the end of 2019, after which time they will need to be converted into electronic format.

Security over machinery and equipment can be taken in a number of ways. For one, machinery and equipment may be pledged as movable property subject to a fixed charge, such pledge to be perfected by delivering such machinery and equipment to the possession of the pledgee or its order or by otherwise precluding the pledgor from utilising such assets or, in the event that such assets are in the possession of a third party, by delivering a notice of pledge to such third party. Secondly, a business mortgage registered against a Finnish company will, in principle, cover all of its movable business assets (including plant, machinery and equipment), without limiting the pledgor's ability to dispose of such assets in the ordinary course of its business. Such security is perfected by delivering the business mortgage note(s) representing the business mortgage to the possession of the pledgee or its order.

Under certain circumstances, machinery and equipment may, however, be considered sufficiently integrated with the underlying real estate or leasehold to constitute fixtures or appurtenances thereof, thus falling within the scope of a real estate mortgage rather than a business mortgage. It should also be noted that, under Finnish law, it is possible to register such assets as belonging or, conversely, not belonging, to the underlying real estate or leasehold.

In addition to business mortgages and real estate mortgages, there are also certain limited movable assets (being aircraft, certain vessels and certain vehicles), over which security can be taken by registering a mortgage.

3.4 Can collateral security be taken over receivables? Briefly, what is the procedure? Are debtors required to be notified of the security?

Under Finnish law, security can be taken over receivables and is perfected by delivering a notice to the relevant debtor, with instructions to make all payments to the pledgee or its order. In practice, perfection is usually delayed and the debtor continues to make payments to the pledgor until the occurrence of a credit event, even though the security is thus subject to a risk of clawback. It should, however, be noted that Finnish law does not contain provisions regarding the pledge of future receivables which do not derive from pledged assets. The prevailing view of legal scholars is that receivables that exist before the pledgor-debtor is declared bankrupt or enforcement proceedings commence should be regarded as being subject to a perfected security interest *vis-à-vis* third parties, although it is recommended that another separate notice is served on the relevant debtor(s) each time after such receivables have been earned.

3.5 Can collateral security be taken over cash deposited in bank accounts? Briefly, what is the procedure?

Under Finnish law, security can be taken over cash deposited in bank accounts and is perfected by delivering a notice of pledge to the account bank with instructions to prohibit the pledgor from making withdrawals from or otherwise using the account. To the extent that, e.g., deposit accounts are pledged, the parties generally agree on delayed perfection, where the pledgor is only precluded from stipulating over the account(s) following certain credit events. It should, however, be noted that until the security is fully perfected, the pledge will not be considered effective in relation to the pledgor's third-party creditors.

3.6 Can collateral security be taken over shares in companies incorporated in your jurisdiction? Are the shares in certificated form? Can such security validly be granted under a New York or English law governed document? Briefly, what is the procedure?

Share pledges are commonly used as security in Finland. Security taken over shares in a company is perfected: (i) if no share certificates have been issued, by the pledgor notifying such company of the pledge and requesting that it record such pledge in its shareholder register; or (ii) if share certificates have been issued, by delivering the share certificates to the possession of the pledgee, usually endorsed in blank (although not a requirement, notice as referred to under (i) above is often delivered to the company even if it has issued share certificates). Dematerialised shares registered on a book-entry account may also be pledged, with such security being perfected by notice to the relevant book-entry register and registration of the pledge therein.

Choice of foreign law (such as English or New York law) is generally accepted (please also see sections 7 and 9 below) and valid *inter partes* unless the application of such foreign law would be contrary to the fundamental principles of Finnish law. It should, however, be noted that the parties cannot by choice of law circumvent mandatory provisions of Finnish law regarding e.g. protection of third-party creditors. Prevalent market practice is thus for share pledge agreements creating security over shares in Finnish entities to be governed by Finnish law.

3.7 Can security be taken over inventory? Briefly, what is the procedure?

In order to validly perfect a pledge over inventory, the pledgor must be precluded from stipulating over the pledged assets. This may be effected by transferring physical possession of the asset(s) to the pledgee or its order, or allowing the asset to remain in the pledgor's premises but preventing the pledgor from accessing and dealing with the asset(s) (such as disposing thereof) through factual arrangements (e.g. handing over the keys to such premises to a third party). Although inventory pledges may in many cases be considered impractical, oil reserves have been used as security in a novel manner in Finland where an independent third party was engaged to operate, manage and control the pledged oil reserves on behalf of the pledgee and the pledgor was entitled to request the release of a certain portion thereof from time to time. Nevertheless, a more common way to take security over movable assets such as inventory would be by way of a business mortgage as described under question 3.3 above.

3.8 Can a company grant a security interest in order to secure its obligations (i) as a borrower under a credit facility, and (ii) as a guarantor of the obligations of other borrowers and/or guarantors of obligations under a credit facility (see below for questions relating to the giving of guarantees and financial assistance)?

In general, yes. Please, however, see question 2.2 above and section 4 below regarding certain limitations to the provision of guarantees and security.

3.9 What are the notarisation, registration, stamp duty and other fees (whether related to property value or otherwise) in relation to security over different types of assets?

Under Finnish law, no notarisation, registration, stamp duty or other fees are payable in connection with granting security over receivables, shares or other movable assets which are not registered, save for customary court and enforcement authority fees. The creation of security over publicly registered assets (e.g. real property and business mortgages) is generally subject to minor registration fees.

3.10 Do the filing, notification or registration requirements in relation to security over different types of assets involve a significant amount of time or expense?

Notification and registration procedures, as referred to under questions 3.3–3.7 above, are usually initiated promptly and completed within a couple of weeks, and do not generate significant expense. Under Finnish law, there are no filing requirements in relation to the creation of security, except that in connection with legal proceedings, the relevant security agreements may need to be filed with the appropriate court or administrative body and translated into Finnish or Swedish.

3.11 Are any regulatory or similar consents required with respect to the creation of security?

No regulatory or similar consent is required in order to create a valid security interest in Finland.

3.12 If the borrowings to be secured are under a revolving credit facility, are there any special priority or other concerns?

Securing obligations under a revolving credit facility does not raise any particular priority or other concerns under Finnish law.

3.13 Are there particular documentary or execution requirements (notarisation, execution under power of attorney, counterparts, deeds)?

Although Finnish law does not impose any particular documentary or execution requirements in relation to the creation of security interests or the provision of guarantees, it is recommended that all security agreements and guarantees are made in writing.

4 Financial Assistance

4.1 Are there prohibitions or restrictions on the ability of a company to guarantee and/or give security to support borrowings incurred to finance or refinance the direct or indirect acquisition of: (a) shares of the company; (b) shares of any company which directly or indirectly owns shares in the company; or (c) shares in a sister subsidiary?

(a) Shares of the company

Pursuant to the Companies Act, a Finnish limited liability company cannot provide a loan, funds, security or a guarantee for the purpose of enabling a third party to acquire shares in such company or its Finnish parent company.

(b) Shares of any company which directly or indirectly owns shares in the company

Under the Companies Act, the prohibition of financial assistance described under paragraph (a) above applies to Finnish parent companies of Finnish limited liability companies. The Companies Act and the Accounting Act (1336/1997, as amended) define a parent company in relation to its subsidiary as an entity which: (i) holds over 50 percent of such subsidiary's shares or voting rights; (ii) has the ability to appoint a majority of such subsidiary's board of directors or similar; or (iii) otherwise holds *de facto* control over such subsidiary. Therefore, the financial assistance provisions under the Companies Act do not apply to the extent a shareholder is not considered a Finnish parent company in accordance therewith. Notwithstanding the foregoing, the provisions concerning corporate benefit and equal treatment of shareholders referred to under question 2.2 above should be taken into account.

(c) Shares in a sister subsidiary

The provision of guarantees and/or security for the purpose of enabling the acquisition of the shares in a sister company is not subject to the financial assistance prohibition described under paragraph (a) above. However, the provisions concerning corporate benefit and equal treatment of shareholders referred to under question 2.2 above should be taken into account.

5 Syndicated Lending/Agency/Trustee/Transfers

5.1 Will your jurisdiction recognise the role of an agent or trustee and allow the agent or trustee (rather than each lender acting separately) to enforce the loan documentation and collateral security and to apply the proceeds from the collateral to the claims of all the lenders?

Although the concept of a trustee is not recognised under Finnish law, lenders may appoint a facility and/or security agent to represent them in all matters relating to the finance documents and/or security. Agents may be appointed to enforce, for and on behalf of the lenders, any of their rights under the finance documents, including any security, and to apply the proceeds therefrom in satisfaction of the secured claims of the lenders, in each case as set out in the relevant finance documentation. However, pursuant to recent discussions with the relevant authorities, it seems unlikely that a bankruptcy administrator would depart from Finnish law regarding the priority of claims on the basis of an intercreditor agreement or any other document contractually subordinating claims among each other. Accordingly, particular emphasis should be placed on turnover provisions in such documentation.

5.2 If an agent or trustee is not recognised in your jurisdiction, is an alternative mechanism available to achieve the effect referred to above which would allow one party to enforce claims on behalf of all the lenders so that individual lenders do not need to enforce their security separately?

Please see question 5.1 above.

5.3 Assume a loan is made to a company organised under the laws of your jurisdiction and guaranteed by a guarantor organised under the laws of your jurisdiction. If such loan is transferred by Lender A to Lender B, are there any special requirements necessary to make the loan and guarantee enforceable by Lender B?

In order to perfect the transfer of a loan and ensure its enforceability against third parties, the borrower must be notified thereof and, although not a requirement, the guarantor may also be notified of such transfer in order to ensure that it does not fulfil its guarantee obligations to the original lender.

6 Withholding, Stamp and Other Taxes; Notarial and Other Costs

6.1 Are there any requirements to deduct or withhold tax from (a) interest payable on loans made to domestic or foreign lenders, or (b) the proceeds of a claim under a guarantee or the proceeds of enforcing security?

In principle, no withholding tax is deductible under Finnish law from interest payable on loans, proceeds of claims under guarantees or enforcement proceeds.

6.2 What tax incentives or other incentives are provided preferentially to foreign lenders? What taxes apply to foreign lenders with respect to their loans, mortgages or other security documents, either for the purposes of effectiveness or registration?

Please see question 6.3 below. No specific tax incentives are provided to foreign lenders in Finland.

6.3 Will any income of a foreign lender become taxable in your jurisdiction solely because of a loan to or guarantee and/or grant of security from a company in your jurisdiction?

No taxes apply to foreign lenders as long as they do not have a permanent establishment in Finland which is effectively connected to the proceeds of the loan, guarantee or security interest.

6.4 Will there be any other significant costs which would be incurred by foreign lenders in the grant of such loan/guarantee/security, such as notarial fees, etc.?

No. Please see question 3.9 above.

6.5 Are there any adverse consequences to a company that is a borrower (such as under thin capitalisation principles) if some or all of the lenders are organised under the laws of a jurisdiction other than your own? Please disregard withholding tax concerns for purposes of this question.

There are no adverse consequences for a Finnish borrower solely due to some or all of the lenders being established in a jurisdiction other than Finland. Finnish law does not contain any thin capitalisation rules *per se,* although there are certain restrictions on the deductibility of interest on related-party loans. Such limitations do not apply to, for example, certain companies within the real estate or financial services industries. A receivables pledge granted by a related party may, however, lead to the external loan in respect of which such pledge is granted being treated as a related-party loan. Further, the Finnish Ministry of Finance has, on 19 January 2018, proposed a new, draft government bill regarding, among others, the extension of similar interest deductibility limitations to third-party loans as well as all Finnish tax resident corporate entities.

7 Judicial Enforcement

7.1 Will the courts in your jurisdiction recognise a governing law in a contract that is the law of another jurisdiction (a "foreign governing law")? Will courts in your jurisdiction enforce a contract that has a foreign governing law?

The parties to a contract are generally free to choose the governing law provided that such choice is made expressly or otherwise clearly demonstrated by the contract. Finnish courts would uphold choice of foreign law, except to the extent that such would be contrary to the mandatory laws or public policy of Finland. Notwithstanding any choice of foreign law, Finnish law will be applied in any bankruptcy, insolvency, liquidation, reorganisation or other similar proceeding in respect of, or any execution proceeding against, a Finnish entity. Further, in the event that a Finnish court is unable to obtain an account of the content of applicable foreign law, Finnish law may be applied.

7.2 Will the courts in your jurisdiction recognise and enforce a judgment given against a company in New York courts or English courts (a "foreign judgment") without re-examination of the merits of the case?

Foreign judgments are in principle not recognised or directly enforceable in Finland unless otherwise agreed. For example, Finland and the United States have not entered into such an agreement and, thus, Finnish courts would not recognise or directly enforce a judgment rendered by a court of the State of New York.

Judgments rendered by the courts of Member States of the European Union on or after 10 January 2015 are, however, as a general rule directly enforceable in Finland in accordance with Regulation (EU) No. 1215/2012 of 12 December 2012 of the European Parliament and of the Council on Jurisdiction and the Recognition and Enforcement of Judgments in Civil and Commercial Matters (the "**Brussels I Recast**"). Thus, as long as the United Kingdom remains a member of the European Union, judgments rendered by English courts, fulfilling the requirements of the Brussels I Recast, remain directly enforceable in Finland in accordance with the Enforcement Code (705/2007, as amended) (the "**Enforcement Code**").

7.3 Assuming a company is in payment default under a loan agreement or a guarantee agreement and has no legal defence to payment, approximately how long would it take for a foreign lender to (a) assuming the answer to question 7.1 is yes, file a suit against the company in a court in your jurisdiction, obtain a judgment, and enforce the judgment against the assets of the company, and (b) assuming the answer to question 7.2 is yes, enforce a foreign judgment in a court in your jurisdiction against the assets of the company?

According to the Finnish Ministry of Justice, in 2016 district courts resolved civil cases within approximately 12 months and summary civil cases within approximately three months. Most civil cases are resolved through written proceedings where the processing time is shorter and only very few proceed to a main hearing. The statistics do not take into account any potential enforcement proceedings. Both Finnish and foreign judgments fulfilling the requirements of the Brussels I Recast are directly enforceable in Finland in accordance with the Enforcement Code upon submission of an application to the competent enforcement authority. The length of the enforcement proceedings may, however, vary significantly depending on the assets subject to enforcement.

7.4 With respect to enforcing collateral security, are there any significant restrictions which may impact the timing and value of enforcement, such as (a) a requirement for a public auction, or (b) regulatory consents?

Subject to limited exceptions, the parties to a security agreement may agree on applicable enforcement procedures. Security over most movable assets may be enforced by the creditor itself through private sale or, alternatively, the creditor may seek enforcement by bailiff in accordance with the Enforcement Code. As an exception to the foregoing, security created by way of a mortgage registered in a public register (e.g. business mortgages and real estate mortgages) requires an enforceable enforcement order for execution and, accordingly, such security may only be enforced by bailiff in accordance with the Enforcement Code. Security taken by way of title transfer in accordance with the Finnish Financial Collateral Act (11/2004, as amended, the "**Financial Collateral Act**") does not require enforcement through public or private sale, instead the purchaser-pledgee may directly take ownership over the relevant securities or receivables and off-set their value against the debt due if the parties have agreed on such procedure.

7.5 Do restrictions apply to foreign lenders in the event of (a) filing suit against a company in your jurisdiction, or (b) foreclosure on collateral security?

No such restrictions apply to foreign lenders in the event of filing suit against a company in Finland or foreclosure on security, which would not apply to local lenders.

7.6 Do the bankruptcy, reorganisation or similar laws in your jurisdiction provide for any kind of moratorium on enforcement of lender claims? If so, does the moratorium apply to the enforcement of collateral security?

In principle, reorganisation proceedings under the Corporate Reorganization Act (47/1993, as amended, the "**Reorganization Act**") impose a moratorium on legal proceedings and enforcement actions against a debtor and, save for limited exceptions, no creditor may enforce security or collect debt until the court has confirmed the reorganisation plan. Notwithstanding such stay, secured creditors remain entitled to receive interest payments and other debt-related fees provided for in the original credit documentation and, under certain circumstances, with permission of the court, may even be entitled to enforce security. The commencement of bankruptcy proceedings does not, however, impose a similar moratorium – please see question 8.1 below.

Notwithstanding the foregoing, if security is granted in accordance with the Financial Collateral Act, insolvency proceedings do not affect the right of the pledgee to enforce the security or take ownership over the security assets in the manner agreed between the parties. The Financial Collateral Act is, however, only applicable to the granting of security over certain assets (being securities, cash collateral and certain receivables) provided further that the pledgor qualifies as an "institution" (e.g. a financial institution) under such act or the pledgee is such an institution (unless the securities are not publicly traded, in which case the act only applies if the pledgor is an institution).

7.7 Will the courts in your jurisdiction recognise and enforce an arbitral award given against the company without re-examination of the merits?

According to the New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards of 1958 and the Finnish Arbitration Act (967/1992, as amended), foreign arbitral awards will, unless contrary to the public policy of Finland, be recognised and enforced by the courts of Finland subject to application for enforcement thereof with the District Court.

8 Bankruptcy Proceedings

8.1 How does a bankruptcy proceeding in respect of a company affect the ability of a lender to enforce its rights as a secured party over the collateral security?

In principle, the commencement of bankruptcy proceedings does not limit the right of creditors secured by a fixed charge over movable or immovable property to enforce their rights over security. A creditor seeking to enforce security must, however, provide the bankruptcy administrator with certain information on the claim and the security in a letter of lodgement as well as notice of its intention to enforce the security, including the time and place thereof. The administrator may within two weeks of receipt of such notice prohibit such enforcement for no longer than two months for the purposes of clarifying the creditor's right to the security or safeguarding the rights of the bankruptcy estate. Such restrictions do not, however, apply to creditors secured by publicly traded securities or other security granted in accordance with the Financial Collateral Act. Under certain circumstances, the bankruptcy estate may also seek the court's permission to sell the security assets or enforce the security through bailiff.

The foregoing does not, however, apply to creditors secured by a business mortgage, which may only be enforced as part of the general bankruptcy enforcement. Therefore, creditors secured by a business mortgage are entitled to proceeds from the bankruptcy estate only at the same time and through the same process as unsecured creditors, although with better priority. It should also be noted that security over business mortgages requires an enforceable enforcement order for execution (please see question 7.4 above) and that, in insolvency, receivables secured by a business mortgage are considered secured only up to 50 percent of the value of the mortgaged property and rank after receivables secured by fixed charges. Please also see question 7.6 above.

8.2 Are there any preference periods, clawback rights or other preferential creditors' rights (e.g., tax debts, employees' claims) with respect to the security?

Under the Act on Recovery to a Bankruptcy Estate (758/1991, as amended) (the "**Recovery Act**"), a security interest may be recovered or reversed in connection with reorganisation, bankruptcy or enforcement proceedings as follows:

(a) security interests granted by a debtor for its own debt, if such security was granted less than three months, or less than two years if granted to an affiliated party, prior to the filing for reorganisation, bankruptcy or execution and:
   (i) was not originally agreed on in the underlying loan (or other) agreement; or
   (ii) subsequently perfected without undue delay,

   provided, however, that security granted to an affiliated party over three months but less than two years prior to the filing for such proceedings may be recovered or reversed unless it can be shown that the debtor was not insolvent at the time of granting the security and did not become insolvent due to the security arrangement; or

(b) if the granting of such security interest in an inappropriate manner:
   (i) favoured a particular creditor;
   (ii) involved the transfer of assets beyond the reach of the debtor's other creditors; or
   (iii) increased the debtor's indebtedness to the other creditors' detriment,

   provided, however, that the debtor was either insolvent at the time or the act contributed to the debtor becoming insolvent, and the other party to the transaction was, or should have been, aware of this and of the adverse effect on the debtor's financial situation as well as of the factors that resulted in such security being considered inappropriate. Security granted more than five years prior to the filing for reorganisation, bankruptcy or execution may, however, only be recovered or reversed if granted to an affiliated party.

8.3 Are there any entities that are excluded from bankruptcy proceedings and, if so, what is the applicable legislation?

Subject to certain exceptions (e.g. the State of Finland, Finnish municipalities, the Evangelical Lutheran Church and the Orthodox Church and their parishes), any natural person or legal entity may be subject to bankruptcy proceedings under the Bankruptcy Act (120/2004, as amended). After the commencement of reorganisation proceedings under the Reorganization Act, a debtor may, however, only be declared bankrupt in limited situations.

8.4 Are there any processes other than court proceedings that are available to a creditor to seize the assets of a company in an enforcement?

In general, a pledgee may enforce security over movable property (save for business mortgages and certain other movable assets in respect of which a mortgage is registered) through private sale. Further, if security is taken by way of title transfer in accordance with the Financial Collateral Act (applicable only to limited assets and financing arrangements as discussed above), the purchaser-pledgee may take direct ownership over the relevant securities rather than enforcing them through private or public sale if the parties have agreed on such procedure. Otherwise, enforcement (in respect of, e.g., real estate mortgages) is carried out by bailiff in accordance with the Enforcement Code, and requires an enforceable judgment or arbitral award against the debtor. However, if there is a danger that the debtor may seek to hide, destroy or dispose of its assets or take any other action which would e.g. endanger repayment of indebtedness, injunctive relief can also be sought to safeguard the assets.

9 Jurisdiction and Waiver of Immunity

9.1 Is a party's submission to a foreign jurisdiction legally binding and enforceable under the laws of your jurisdiction?

Under Finnish law, the parties may agree on the submission of disputes to the courts of a foreign jurisdiction subject to certain criteria. The agreement must generally be made in writing. In addition, there are certain provisions in order to protect weaker parties, such as consumers or employees, and to ensure their access to Finnish courts at all times, which cannot be deviated from by submission to a foreign jurisdiction.

9.2 Is a party's waiver of sovereign immunity legally binding and enforceable under the laws of your jurisdiction?

Finnish legislation does not contain specific provisions on the waiver of sovereign immunity, nor has Finland ratified the United Nations Convention on Jurisdictional Immunities of States and Their Property. The Supreme Court of Finland (KKO 2007:49) has, however, ruled that an entity may validly waive its sovereign immunity. It should, nevertheless, be noted that due to limited case law and the lack of specific legislation on the matter, to what extent waiver of sovereign immunity may be considered legally binding and enforceable under Finnish law may be subject to legal interpretation.

10 Licensing

10.1 What are the licensing and other eligibility requirements in your jurisdiction for lenders to a company in your jurisdiction, if any? Are these licensing and eligibility requirements different for a "foreign" lender (i.e. a lender that is not located in your jurisdiction)? In connection with any such requirements, is a distinction made under the laws of your jurisdiction between a lender that is a bank *versus* a lender that is a non-bank? If there are such requirements in your jurisdiction, what are the consequences for a lender that has not satisfied such requirements but has nonetheless made a loan to a company in your jurisdiction? What are the licensing and other eligibility requirements in your jurisdiction for an agent under a syndicated facility for lenders to a company in your jurisdiction?

Under Finnish law, pure corporate lending (whether by domestic or foreign lenders) has generally been considered exempt from licence and other authorisation requirements, whereas operating as a credit institution (including receiving repayable funds from the public and offering credit and financing for such credit institution's own account) is subject to a licensing and/or notification requirement under the Act on Credit Institutions (610/2014, as amended). Specific requirements concerning e.g. the owners, management and financial standing of such entity further depend on whether its registered office is located in an EEA Member State. Failure to comply with such requirements may lead to administrative and criminal sanctions as well as liability for damages.

Previous guidance of the Finnish Financial Supervisory Authority (the "**FFSA**") has indicated that a foreign credit institution would not generally be subject to a licensing and/or notification requirement under Finnish law solely by reason of providing a loan to a Finnish company on an *ad-hoc* basis, assuming that it does not actively solicit clients in Finland. More recent discussions with the FFSA suggest, however, that foreign credit institutions engaging in pure corporate lending in Finland may, under certain circumstances, also be subject to licensing and/or notification requirements. The FFSA has not, however, provided further guidance regarding the criteria to be taken into account when making such determination and, accordingly, the situation remains largely unclear and subject to case-by-case analysis.

There are no particular licensing or eligibility requirements for facility agents under Finnish law.

11 Other Matters

11.1 Are there any other material considerations which should be taken into account by lenders when participating in financings in your jurisdiction?

The material legal issues to be considered when participating in financing and taking security in Finland have been addressed herein.

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Chapter 46

France

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1 Overview

1.1 What are the main trends/significant developments in the lending markets in your jurisdiction?

With the French economy confirming its recovery, the number of financing transactions in France has significantly increased in 2017 compared to the previous years. However, it is worth pointing out that high-yield bond issues have decreased as a result of the growing request from borrowers for covenant-lite loans. As a result, banks have been quite active in 2017 alongside debt funds which continue to be key players in the French financing market.

1.2 What are some significant lending transactions that have taken place in your jurisdiction in recent years?

The French financing market saw numerous small-cap, mid-cap and large-cap LBO financing transactions in 2017. There have been several significant large-cap LBO financing transactions such as the financing of the acquisition of DRT by Ardian and the financing of the second buy-out of Domus Vi by PAI Partners.

2 Guarantees

2.1 Can a company guarantee borrowings of one or more other members of its corporate group (see below for questions relating to fraudulent transfer/financial assistance)?

Yes, subject to certain conditions, restrictions and limitations relating in particular to the French law requirement of corporate benefit and the prohibition of financial assistance – see questions 2.2, 2.3, 2.4, 2.5 and section 4 below for details.

2.2 Are there enforceability or other concerns (such as director liability) if only a disproportionately small (or no) benefit to the guaranteeing/securing company can be shown?

All guarantees and security interests granted by a French company must be in that company's corporate benefit. If only a disproportionately small (or no) benefit to the guaranteeing/securing company can be shown, the guarantee/security may be deemed as not being in the corporate benefit of the guaranteeing/securing company and may trigger the criminal liability of the managers/directors of the company (for misuse of corporate assets). Some French courts have also declared void guarantees/security interests which were not in the corporate benefit of the guaranteeing/securing company on the ground that such guarantees/security interests had been granted for an illicit cause. Although the concept of "illicit cause" no longer exists under French law since a reform of the French civil code which came into force on 1 October 2016, an equivalent concept of "illicit content of an agreement" has been introduced by the reform and may be applied by the French courts with respect to the guarantees/security interests granted after 1 October 2016 which would not comply with the corporate benefit requirements.

In case of a group of companies, French courts assess such corporate interest at the group level, but some strict criteria must be met, among which: (i) the guarantee/security interest must be granted in the common interest of the group within the framework of a common policy defined for the group as a whole; (ii) there must be some consideration for the guarantee/security interest; and (iii) the guarantee/security interest must not exceed the financial capabilities of the grantor.

A guarantee/security interest granted in order to guarantee the obligations of a subsidiary is usually unlimited as it is generally admitted that a holding company has a corporate interest in guaranteeing its subsidiary's obligations. As for upstream and cross-stream guarantees/security interests, the most commonly accepted corporate benefit justification is the granting of an intercompany loan by the guaranteed company to the guarantor out of loan proceeds made available to the guaranteed company (the guaranteed amount under the guarantee/security interest being in such case limited to the amount of such intercompany loan).

2.3 Is lack of corporate power an issue?

Guarantees granted by the legal representatives of a company are deemed to be validly granted and enforceable (as long as the granting of such guarantees does not fall outside the corporate object of the company, save for the case where (i) it has been authorised by a unanimous shareholders' resolution, or (ii) it was granted by a joint stock company (i.e., a *société anonyme,* a *société par actions simplifiée* or a *société européenne*) or by a limited liability company (i.e., a *société à responsabilité limitée*)). This rule does not, however, cover (i) guarantees which are prohibited by law, or (ii) guarantees which are subject to prior authorisation by the board of directors or by the shareholders (see question 2.4 below).

If a guarantee agreement is signed by a person who is not the legal representative of the company (and if such person does not act under a power of attorney granted by a legal representative of the company) such guarantee may be voided, save for cases where the company has confirmed the guarantee either explicitly or implicitly by performing its obligations thereunder.

2.4 Are any governmental or other consents or filings, or other formalities (such as shareholder approval), required?

No governmental consents or filings are required. Shareholder approval is not required by law (save for the case of a *société civile* offering securities to the public), but the by-laws of a company may contain clauses pursuant to which shareholder approval is required with respect to the granting of guarantees. Also, guarantees granted by a *société anonyme* are subject to authorisation by the board of directors.

If the guarantee is granted by an individual, the signature of such person must be preceded by a specific handwritten statement specifying the maximum guaranteed amount and the duration of the guarantee. A similar requirement is provided by French law with respect to guarantees granted by non-commercial companies.

2.5 Are net worth, solvency or similar limitations imposed on the amount of a guarantee?

See the answer to question 2.2 above with respect to upstream and cross-stream guarantees granted in the context of a group of companies.

Guarantees granted by a French company which is insolvent (*en état de cessation des paiements*) may be declared null and void by a French court – see question 8.2 below for more details.

A guarantee granted by an individual must be proportionate to its income and assets (otherwise, a court may declare that such guarantee is not enforceable).

2.6 Are there any exchange control or similar obstacles to enforcement of a guarantee?

There are no exchange control or similar obstacles to enforcement of a guarantee.

3 Collateral Security

3.1 What types of collateral are available to secure lending obligations?

Collateral security can be taken over tangible or intangible assets, among which are: real property; shares; financial securities; bank accounts; receivables; intellectual property rights; business as a going concern; equipment and machinery; inventory; cash; and various tangible assets. Security interests may be granted in the form of a pledge, a mortgage (real property), a lien (real property), a transfer by way of security (receivables, cash), a delegation (receivables) or a security trust (*fiducie*).

3.2 Is it possible to give asset security by means of a general security agreement or is an agreement required in relation to each type of asset? Briefly, what is the procedure?

A separate agreement must be entered into in relation to each type of asset. There are, however, some types of security interest agreements which encompass several types of assets: (i) a pledge over business as a going concern, which includes security over assets such as the company's logo and commercial name, goodwill (customer relationship) and lease rights and may also include intellectual property rights, equipment and machinery; and (ii) a securities account pledge which includes a pledge over shares or other financial securities and a pledge over the bank account on which cash proceeds relating to such shares/financial securities are credited (such as dividends).

3.3 Can collateral security be taken over real property (land), plant, machinery and equipment? Briefly, what is the procedure?

Collateral security can be taken over real property (land or buildings) by way of a mortgage (*hypothèque*), a lender's lien (*privilege du prêteur de deniers*) or a *gage immobilier*. These security interests must be entered into by way of a notarised deed and must be registered with the relevant land registry.

Collateral can also be taken over machinery and equipment by way of a pledge, but (if not included in a pledge over business as a going concern) only in favour of certain beneficiaries among which is the vendor of the machinery and equipment, and the lender having made available the facilities used to finance the acquisition of the machinery and equipment. The pledge agreement relating to machinery and equipment must be entered into within a maximum period of two months following the delivery of the machinery and equipment to the pledgor and must be registered with the relevant commercial registry within 15 days from its execution for validity purposes.

3.4 Can collateral security be taken over receivables? Briefly, what is the procedure? Are debtors required to be notified of the security?

Yes, collateral can be taken over receivables by way of: (i) a pledge over receivables; (ii) an assignment of receivables by way of security (*Dailly* assignment); (iii) a delegation (*délégation*); or (iv) a security trust (*fiducie-sûreté)*.

A pledge over receivables may be granted by an obligor in favour of any type of beneficiaries (as opposed to a *Dailly* assignment of receivables – see the paragraph below). The notification of the pledge to the debtor(s) is required in order to render the pledge enforceable against the debtor(s), but not for validity purposes. As from such notification, the debtor(s) must make payments directly to the secured creditor, unless otherwise agreed in the pledge agreement.

A *Dailly* assignment of receivables by way of security may only be granted by a borrower (and not by a guarantor or a third party security grantor) and only in favour of: (i) a French licensed credit institution (*établissement de credit*); (ii) a French licensed financial company (*sociéte de financement*); (iii) a foreign financing institution "passported" to carry out banking activities in France under the 2000/12/EC directive; and (iv) the following French alternative investment entities: the professional specialised investment funds (*fonds professionnels spécialisés – FPS*); the professional private equity investment funds (*fonds professionnels de capital investissement – FPCI*); the French limited partnerships (*sociétés de libre parteneriat – SLP*); and the securitisation vehicles (*organismes de titrisation – OT*). The notification of the assignment to the debtor(s) of the assigned receivables is required in order to render the assignment enforceable against such debtor(s), but not for validity purposes.

A delegation of receivables is generally used to take security over receivables under insurance policies or vendor warranties. The parties to the delegation agreement are not only the delegating obligor (*délégant*) and the secured creditor (*délégataire*), but also the debtor (*délégué*) and therefore no notification of the latter is required. Under a delegation agreement, the debtor agrees to make direct payments to the secured creditor.

A security trust (*fiducie-sûreté*) over receivables may also be granted. The notification of the security trust (*fiducie-sûreté*) to the debtor(s) is also required in order to render the security trust (*fiducie-sûreté*) enforceable against the debtor(s), but not for validity purposes.

3.5 Can collateral security be taken over cash deposited in bank accounts? Briefly, what is the procedure?

A pledge over the balance of a bank account is possible under French law. No particular formalities are required in connection therewith, although the bank account holder is usually notified of the pledge so as to render such pledge enforceable against such person. A pledge may also be granted over cash (*gage-espèces*) by transferring the ownership of such cash to the secured creditor who may then freely dispose of it, subject to returning the same amount of cash to the pledgor upon discharge of all the secured liabilities.

3.6 Can collateral security be taken over shares in companies incorporated in your jurisdiction? Are the shares in certificated form? Can such security validly be granted under a New York or English law governed document? Briefly, what is the procedure?

Collateral security can be taken over shares in companies incorporated in France either by way of a securities account pledge with respect to shares of a joint stock company (a *société anonyme*, a *société par actions simplifiée* or a *société européenne*) or by way of a share pledge with respect to other type of companies (such as a *société à responsabilité limitée*, a *société en nom collectif* or a *société civile*, etc.).

A securities account pledge is a pledge over a securities account in which shares (and/or other securities) are credited and over a cash proceeds account in which dividends or other cash proceeds relating to such shares (and/or other securities) are credited. The securities account is either held by the company whose shares are pledged or by a financial institution. Such security interest automatically extends to any additional shares and any additional cash proceeds which are credited to the pledged accounts during the life of the pledge. In order for such pledge agreement to be valid under French law, a mandatory form of statement of pledge (*déclaration de nantissement*) must be signed by the pledgor. It is also customary for the securities account holder and the cash proceeds account holder to sign confirmations of the pledge.

A share pledge actually pledges the shares (as opposed to the pledge of a securities account in which such shares are credited, as explained above with respect to securities account pledges) and therefore new additional shares are not included automatically in the scope of the pledge. It may also cover cash proceeds related to the pledged shares, but only if this is expressly specified in the pledge agreement. In addition to the registration of such pledge with the clerk of the relevant commercial court as mentioned below, other perfection formalities may be required depending on the type of company whose shares are pledged. For instance, a pledge over the shares of a *société civile* must be notified by bailiff (*signifiée par huissier*) to the company whose shares are pledged.

Shares of French companies are not in certificated form, but in dematerialised form. The pledge must be registered (i) with respect to shares of joint stock companies, in the share transfer registry (*registre des mouvements de titres*) and the shareholders' accounts (*comptes d'actionnaires*) of the company whose shares are pledged, and (ii) with respect to shares of other type of companies, in a special register held by the clerk of the relevant commercial court where the company whose shares are pledged is registered.

It is not recommended to have a securities account pledge or a share pledge governed by New York or English law because of difficulties, both practical and legal, which would arise with respect to the perfection and the enforcement of such security interests.

3.7 Can security be taken over inventory? Briefly, what is the procedure?

Yes, security can be taken over inventory. A recent reform has introduced more flexibility for this type of security interest. The parties may now choose between a pledge over inventory governed by the provisions of the French commercial code or a pledge over inventory governed by the provisions of the French civil code.

As opposed to a pledge over inventory governed by the provisions of the French civil code, the pledge over inventory governed by the provisions of the French commercial code may only be granted by a borrower (and not by a guarantor or a third-party security grantor) and only in favour of French licensed credit institutions (*établissements de crédit*), French licensed financing companies (*sociétés de financement*) or foreign financing institutions "passported" to carry out banking activities in France under the 2000/12/EC directive.

Both types of pledge (i) may be enforced through private foreclosure (*pacte commissoire*), and (ii) must be registered for enforceability against third parties' (*opposabilité aux tiers*) purposes with the French commercial registry.

3.8 Can a company grant a security interest in order to secure its obligations (i) as a borrower under a credit facility, and (ii) as a guarantor of the obligations of other borrowers and/or guarantors of obligations under a credit facility (see below for questions relating to the giving of guarantees and financial assistance)?

Yes, subject to corporate benefit and financial assistance rules and save for the lenders' lien (*privilège du prêteur de deniers*), the pledge over machinery and equipment, the pledge over inventory governed by the provisions of the French commercial code or the *Dailly* assignment of receivables by way of security which may only be granted in order to secure the grantor's obligations as borrower.

3.9 What are the notarisation, registration, stamp duty and other fees (whether related to property value or otherwise) in relation to security over different types of assets?

The most expensive fees are those relating to security interests over real estate properties. Registration costs and notary fees with respect to a mortgage are calculated as a percentage of the secured amounts and are therefore expensive (as at 1 March 2017, these costs include land registry tax fees (*taxe de publicité foncière*) of 0.715% of the secured amount, plus land registrar's fees (*contribution de sécurité immobilière*) of 0.05% of the secured amount, plus statutory notary fees of 0.447% of the secured amount (for a secured amount exceeding €60,000) (the statutory notary fees may be negotiated since a recent reform implemented in 2016 and discounts may be obtained in certain circumstances), plus a fee of €125 for the registration of the mortgage with the French tax authorities). The costs relating to a lenders' lien (*privilège du prêteur de deniers*) are also based on the secured amount but are not as high as the registration costs of a mortgage, as they do not include the 0.715% mandatory fees corresponding to the land registry tax fees (*taxe de publicité foncière*).

Registration fees with respect to a pledge over intellectual property rights are not expensive unless the pledge covers an important number of intellectual property rights and the accelerated registration procedure is chosen, as opposed to the ordinary registration procedure (the ordinary registration procedure may take between three and five months while the accelerated registration procedure takes up to five days). The cost for the registration under the ordinary procedure is €27 per intellectual property right with a maximum amount of €270 and the cost for the registration under the accelerated procedure is an additional €52 per intellectual property right with no maximum amount.

The registration fees with respect to other types of security interests are not significant: e.g., registration costs with the commercial court of Paris of a pledge over business as a going concern, a pledge over inventory, a pledge over machinery and equipment or a pledge over shares (other than shares of a joint-stock company which do not require registration with a public register) amount to approximately €160 for each pledge (for an amount of the secured obligations exceeding €41,600). The commercial courts may require, prior to the registration of the above-mentioned security interests with the relevant commercial registry, a registration of such security interest agreements with the tax authorities – the cost of such registration is not significant (€125 for each security interest agreement).

3.10 Do the filing, notification or registration requirements in relation to security over different types of assets involve a significant amount of time or expense?

Generally no, save for (i) security over real estate properties with respect to which registration requirements involve a significant amount of expense (see above), and (ii) a pledge over intellectual property rights which may take up to five months if the ordinary procedure is chosen or may be expensive if the accelerated procedure is chosen (please see question 3.9 above).

3.11 Are any regulatory or similar consents required with respect to the creation of security?

No, but it should be noted that the granting of a share pledge or a securities account pledge may require the prior consultation of the works council of the company whose shares are pledged (if such works council exists and if the pledge is over more than 50% of the shares of such company). The opinion of the works council is not binding, but its consultation is mandatory and may take from 15 days to four months depending on the complexity of the contemplated transaction.

3.12 If the borrowings to be secured are under a revolving credit facility, are there any special priority or other concerns?

No, there are not.

3.13 Are there particular documentary or execution requirements (notarisation, execution under power of attorney, counterparts, deeds)?

A security interest agreement over real estate property requires notarisation. If such agreement is signed under a power of attorney, such power of attorney agreement must also be notarised.

French law agreements may not be signed in counterparts.

4 Financial Assistance

4.1 Are there prohibitions or restrictions on the ability of a company to guarantee and/or give security to support borrowings incurred to finance or refinance the direct or indirect acquisition of: (a) shares of the company; (b) shares of any company which directly or indirectly owns shares in the company; or (c) shares in a sister subsidiary?

(a) Shares of the company

Yes, a French joint stock company (a *société anonyme*, a *société par actions simplifiée* or a *société européenne*) may not provide any financial assistance in the form of a loan, guarantee or security interest for the acquisition of its own shares. The violation of this prohibition may lead to the criminal liability of the managers/directors of such company and to the voidability of such loan, guarantee or security interest agreement.

(b) Shares of any company which directly or indirectly owns shares in the company

The prohibition of financial assistance would also apply in case of the acquisition of shares in a company which directly or indirectly holds shares in the company.

(c) Shares in a sister subsidiary

There is no financial assistance prohibition as such, but this type of transaction remains subject to the corporate benefit rules described above.

5 Syndicated Lending/Agency/Trustee/Transfers

5.1 Will your jurisdiction recognise the role of an agent or trustee and allow the agent or trustee (rather than each lender acting separately) to enforce the loan documentation and collateral security and to apply the proceeds from the collateral to the claims of all the lenders?

France has not ratified the Hague Convention on the Law Applicable to Trusts and on their Recognition. However, in a 2011 case, the French Supreme Court recognised the filing of claims in a bankruptcy proceeding by a New York law security trustee, but there is no case law yet with respect to the enforcement of the loan documentation and related collateral security by a trustee.

The role of an agent in a parallel debt mechanism, as well as the parallel debt mechanism itself, has also been recognised by the above-mentioned case law of the French Supreme Court and may therefore be an alternative to the trust mechanism in credit agreements.

The agent concept is very largely used in French syndicated loans. It is, however, usually based on a power of attorney granted by the lenders and not on specific agency provisions. Although a special security agent regime has been introduced in France in 2007, it has been rarely used as it was more restrictive than the use of a power of attorney. However, a recent reform of the security agent regime, which came into force on 1 October 2017, amended some of the previous restrictive provisions and introduced new useful provisions relating to the rights of the security agent in France among which: (i) the possibility to appoint the security agent in any type of agreement including intercreditor agreements (while in the previous regime it could only be appointed in the agreement setting out the secured obligations); (ii) a widening of the scope of the security agent's regime to all security interests and guarantees (while in the previous regime its scope was limited to security interests *in rem*); (iii) the possibility for the security agent to carry out the registration of the security interests acting in its own name for the benefit of the secured creditors; and (iv) the creation of a concept of separate trust estate (*patrimoine d'affectation*) of the security agent different from its own estate and not impacted by the opening of French insolvency proceedings against the security agent.

5.2 If an agent or trustee is not recognised in your jurisdiction, is an alternative mechanism available to achieve the effect referred to above which would allow one party to enforce claims on behalf of all the lenders so that individual lenders do not need to enforce their security separately?

See the answer to question 5.1 above.

5.3 Assume a loan is made to a company organised under the laws of your jurisdiction and guaranteed by a guarantor organised under the laws of your jurisdiction. If such loan is transferred by Lender A to Lender B, are there any special requirements necessary to make the loan and guarantee enforceable by Lender B?

A loan may be transferred in France by way of (i) assignment (which is the method generally used), (ii) novation, (iii) transfer of agreement (*cession de contrat*), or (iv) transfer of debt (*cession de dette*).

Since the French civil code reform entered into force on 1 October 2016, a transfer made by way of assignment is no longer required to be notified to the French borrower(s) by bailiff (*signification par huissier*) (or alternatively to have such transfer agreement signed by the French borrower(s) in a notarised form). A simple notification of the French borrower(s) by any other means is now sufficient (or the signing by the French borrower(s) of the transfer agreement in a form which does no longer require to be notarised). Such notification (or signing of the transfer agreement by the French borrower(s)) is also required in case of a transfer of the loan by way of a transfer of agreement (*cession de contrat*) or by way of a transfer of debt (*cession de dette*).

If the transfer of the loan is made by way of novation, transfer of agreement (*cession de contrat*) or transfer of debt (*cession de dette*), the consent of the debtor is required. Also the consent of the guarantor(s) as well as the consent of the security provider(s) is required in order for Lender B to be able to enforce its rights under the guarantee or under the relevant security interests. Such consents may be granted concomitantly with the transfer or prior to such transfer (such prior consent may also be provided in the loan agreement and/or in the guarantee/security interest agreement).

In order for Lender A to be discharged from its obligations under the loan agreement in case of a loan transfer by way of a transfer of agreement (*cession de contrat*) or by way of a transfer of debt (*cession de dette*), an express consent of the debtor to such discharge must also be obtained.

6 Withholding, Stamp and Other Taxes; Notarial and Other Costs

6.1 Are there any requirements to deduct or withhold tax from (a) interest payable on loans made to domestic or foreign lenders, or (b) the proceeds of a claim under a guarantee or the proceeds of enforcing security?

(a) Interest payable on loans made to domestic or foreign lenders

<u>Interest paid to French tax resident individuals</u>: As of 1 January 2018, such payments are subject to personal income tax in the hands of the individuals under a flat tax with a rate of 12.8%, unless they elect for the progressive tax schedule for all their investment income. The paying establishment will withhold a compulsory tax advance at a rate of 12.8%, which will later be offset against the final income tax charge due by the borrower (12.8% flat tax or progressive tax schedule). In addition to the income tax, social contributions are levied at the rate of 17.2%.

<u>Interest paid to French tax resident companies</u>: As a matter of principle, such payments are not subject to any withholding tax (**WHT**).

<u>Interest paid to foreign lenders (individuals or companies)</u>: Such payments do not give rise to any French WHT.

<u>Interest paid to a Non Cooperative State or Territory (**NCST**)</u>: As a general rule, a 75% WHT applies in cases where interest is paid to an account located in a NCST (notwithstanding the tax residency of the corporate/individual lender), unless the French debtor can demonstrate that the operations in respect of which the interest is paid have a main purpose and effect other than allowing their localisation in a NCST. However, please note that if the lender is tax resident in a country that has entered into a double tax treaty with France, the provisions of that treaty (if available) may permit the reduction of the rate (down to nil) of such WHT. The list of NCSTs, as updated annually by the French government, currently comprises the following jurisdictions (as of 1 January 2017): Botswana; Brunei; Guatemala; the Marshall Islands; Nauru; Niue; and Panama.

(b) Proceeds of a claim under a guarantee or the proceeds of enforcing security

As a matter of principle, proceeds deriving from a claim under a guarantee or as a result of enforcing security are not subject to WHT in France (irrespective of the tax residence of the beneficiary).

However, it should be noted that:

- Proceeds resulting from the enforcement of a security, in cases where the security grantor is not a French tax resident, may be subject to capital gains WHT (provided that a capital gain is realised upon the sale of the asset on which the security is taken) at rates that vary depending on the nature of the asset. However, if the security grantor is tax resident in a country that has entered into a double tax treaty with France, the provisions of that treaty (if available) may permit the avoidance of (or at least, reduce the cost of) the WHT.
- When the proceeds deriving from enforcing a security are used to pay interest accrued under a loan agreement, the rules indicated in question 6.1 (a) above are applicable.
- Proceeds resulting from a claim under a guarantee are of a *sui generis* nature, but in the case where the purpose of the

guarantee is to ensure (in part or in total) the payment of interest accrued under a loan agreement entered into between a French debtor and a foreign beneficiary, it cannot be totally excluded that such guarantee payments would be viewed (at least in part) as interest payments and accordingly be subject to French interest WHT (under the rules summarised in question 6.1 (a) above). There is, however, no firm position of the French tax authorities in this respect, nor relevant case law on the matter.

6.2 What tax incentives or other incentives are provided preferentially to foreign lenders? What taxes apply to foreign lenders with respect to their loans, mortgages or other security documents, either for the purposes of effectiveness or registration?

(a) Incentives attributed to foreign lenders

The absence of WHT on interest (subject to the NCST exception) is very attractive for foreign lenders.

In addition, it is worth mentioning that interest payments made to an account located in a NCST or to a beneficiary residing or located in a NCST as remuneration of a loan agreement entered into outside of France either (i) before 1 March 2010 provided that the expiry date has not since been extended, or (ii) as of 1 March 2010 if said agreement is assimilated to an agreement entered into before that date, are also exempt from WHT in France.

(b) Taxes applicable to foreign lenders with respect to their loans, mortgages or other security documents, either for the purposes of effectiveness or registration

The same taxes apply to all lenders irrespective of whether they are French or foreign with respect to their loans, mortgages or other security documents for the purposes of effectiveness or registration – see the answer to question 3.9 above for details with respect to taxes in relation to registration with the tax authorities (if required).

6.3 Will any income of a foreign lender become taxable in your jurisdiction solely because of a loan to or guarantee and/or grant of security from a company in your jurisdiction?

No, it will not.

6.4 Will there be any other significant costs which would be incurred by foreign lenders in the grant of such loan/guarantee/security, such as notarial fees, etc.?

No other significant costs would be incurred by foreign lenders in the grant of such loan/guarantee/security (other than those mentioned above which apply to all lenders, irrespective of whether they are French or foreign). However, translation costs may be incurred with respect to security interests which require registration in a public register, if the security agreements are not already drafted in the French language.

6.5 Are there any adverse consequences to a company that is a borrower (such as under thin capitalisation principles) if some or all of the lenders are organised under the laws of a jurisdiction other than your own? Please disregard withholding tax concerns for purposes of this question.

No: thin capitalisation rules and other rules limiting tax deductibility of interest expenses apply irrespective of the lender's place of residence.

7 Judicial Enforcement

7.1 Will the courts in your jurisdiction recognise a governing law in a contract that is the law of another jurisdiction (a "foreign governing law")? Will courts in your jurisdiction enforce a contract that has a foreign governing law?

Under French law, a contract is governed by the law chosen by the parties.

This principle has been established by the Convention on the law applicable to contractual obligations of 19 June 1980 (the "**Rome Convention**") in relation to contracts entered into before 17 December 2009 and Regulation 593/2008 of 17 June 2008 on the law applicable to contractual obligations (the "**Rome I Regulation**") in relation to contracts entered into after 17 December 2009, which are applicable in France.

(a) Contracts entered into before 17 December 2009

French courts will enforce the foreign law chosen by the parties to contracts entered into before 17 December 2009 in accordance with the Rome Convention, subject to:

- the overriding mandatory rules (*lois de police*) of the law of another country with which the situation has a close connection, if, and insofar as, under the law of the latter country, those rules must be applied whatever the law applicable to the contract; and
- overriding mandatory provisions applicable in France irrespective of the law otherwise applicable to the contract.

In addition, notwithstanding any choice of law clause, in purely domestic contracts, i.e., where all the elements relevant to the situation (apart from the chosen law) are connected with one country only, the mandatory rules of said country shall be applicable.

(b) Contracts entered into after 17 December 2009

French courts will enforce the foreign law chosen by the parties to contracts entered into after 17 December 2009 in accordance with the Rome I Regulation, subject to:

- French overriding mandatory provisions (*lois de police*); and
- the overriding mandatory provisions of the law of the country where the obligations arising out of the contract have to be or have been performed, in so far as those overriding mandatory provisions render the performance of the contract unlawful.

In addition, notwithstanding any choice of law clause, in purely domestic contracts, i.e., where all the elements relevant to the situation (apart from the chosen law) are connected to one country only, the mandatory rules of said country shall be applicable.

7.2 Will the courts in your jurisdiction recognise and enforce a judgment given against a company in New York courts or English courts (a "foreign judgment") without re-examination of the merits of the case?

The criteria relating to the recognition and enforcement in France of judgments rendered by foreign courts vary depending on (i) the country where such judgments were rendered, and (ii) the time when they were rendered:

- judgments rendered within one of the Member States of the European Union **before 10 January 2015** are enforced in France in accordance with the Council Regulation 44/2001 of 22 December 2000 on Jurisdiction and the Recognition and Enforcement of Judgments in Civil and Commercial Matters ("**EC Regulation 44/2001**");

- judgments rendered within one of the Member States of the European Union **after 10 January 2015** are enforced in France in accordance with the Council Regulation 1215/2012 of 12 December 2012 ("**EC Regulation 1215/2012**");
- judgments rendered in countries with which France has signed a bilateral treaty are recognised and enforced in France in accordance with the provisions of the relevant treaty; and
- judgments rendered in countries with which France has not signed bilateral treaties, which is the case for the United States, require a specific procedure for their recognition and enforcement, namely the exequatur decision.

(a) Recognition and enforcement of a judgment given against a company in English courts

Judgments rendered before 10 January 2015

Under EC Regulation 44/2001, a simplified procedure, known as 'declaration of enforceability', is used to enforce judgments rendered by the EU Member States' courts. As a matter of principle, judgments rendered by the courts of a given Member State should circulate freely in other Member States. Accordingly, judgments made by the courts of a Member State shall be declared enforceable in another Member State, immediately upon production of certain documents.

The declaration of enforceability is granted in summary *ex parte* proceedings (*sur requête*) before the clerk (*greffier en chef*) of the relevant *Tribunal de grande instance* (article 509–2 paragraph 1 of the French Civil Procedure Code). The clerk does not check the validity of the judgment and must declare the judgment enforceable when provided with a request to that end as well as with (i) a copy of the judgment which satisfies the conditions necessary to establish its authenticity, and (ii) a certificate made by the competent authority certifying that the judgment is enforceable in its country of origin. Also, certain clerks (for instance, the clerk of the *Tribunal de grande instance de Paris*) must be provided with a certified translation of these documents.

An appeal may be lodged before the relevant *Cour d'appel* within one month as from the notification of the declaration of enforceability. At this stage, the appellant will be able to argue that the judgment should not be granted leave to enforce based on one or more of the limited grounds set out under articles 34 and 35 of EC Regulation 44/2001 (relating to due process, public policy, and the incompatibility with earlier decisions). These grounds are more restrictive than those applicable to the standard exequatur procedure.

Judgments rendered after 10 January 2015

Under EC Regulation 1215/2012, judgments rendered in civil and commercial matters by the courts of a given Member State are directly enforceable in France (article 39 of Regulation 1215/2012), provided that two conditions are met, namely: (i) that a French bailiff is provided with a copy of the original decision and a certificate filed by the jurisdiction having rendered the decision (found under Appendix I to Regulation 1215/2012); and (ii) that this certificate is duly served upon the person against whom enforcement is sought, together with the decision (if not already served). This second criterion is not applicable to conservatory measures, except where the measure was ordered by a court without the defendant being summoned to appear.

An application for the refusal of enforcement may be lodged before the enforcement judge ("*juge de l'exécution*"). Please note that for the seizure of salaries, however, the competent court is the instance court ("*tribunal d'instance*"). At this stage, the appellant will be able to argue that the judgment should not be enforced based on one or more of the limited grounds set out under Articles 45 of EC Regulation 1215/2012 (relating to due process, public policy and the incompatibility with earlier decisions).

(b) Recognition and enforcement of a judgment given against a company in New York courts

In the absence of a treaty signed between France and the United States, the procedure for the enforcement of judgments rendered by New York courts requires a formal writ of summons. Foreign judgments may be enforced in France only once exequatur (also known as the *formule exécutoire*) is granted by the *Tribunal de grande instance* of the defendant's residence (or, if the debtor is not resident in France, the place where his assets are located).

Pursuant to article 509 of the French Code of civil procedure, the following tests must be met in order for a French court to grant an exequatur order with respect to a foreign judgment:

- the court rendering the judgment had jurisdiction over the defendant;
- the foreign court had not been used fraudulently to escape the jurisdiction of a court more closely related to the dispute (i.e., for forum shopping); and
- the foreign judgment was consistent with French international public policy, including due process.

If the French court is satisfied as to the above, the judgment given against a company in New York courts will be granted exequatur without any review of the facts or legal merits.

7.3 Assuming a company is in payment default under a loan agreement or a guarantee agreement and has no legal defence to payment, approximately how long would it take for a foreign lender to (a) assuming the answer to question 7.1 is yes, file a suit against the company in a court in your jurisdiction, obtain a judgment, and enforce the judgment against the assets of the company, and (b) assuming the answer to question 7.2 is yes, enforce a foreign judgment in a court in your jurisdiction against the assets of the company?

If a company is in payment default, a lender may use the fast-track procedure known as *référé-provision* available for the recovery of debts which are not challengeable on serious grounds.

If the amounts are found to be indisputably due, the president of the *Tribunal de Commerce* orders the payment of the debt by an order ("*ordonnance de référé*") which has the advantage of being immediately enforceable, notwithstanding an appeal that may be lodged. It should, however, be noted that pursuant to article 524 of the French Code of civil procedure, a stay of enforcement can be ordered by the *Premier Président de la Cour d'appel* if the due process ("*principe du contradictoire*") has been breached and if the provisional enforcement is likely to result in clearly excessive consequences. *Ordonnances de référé* may in any case be appealed within 15 days (plus two additional months if the appellant's residence is located abroad). Such appeals are heard relatively rapidly by the *Cour d'appel*. There may be a further challenge by a *pourvoi* before the *Cour de cassation* and in such case the decision of the *Cour de cassation* may take up to one year.

Notwithstanding the above, lenders can always go through normal proceedings to obtain payments due under a loan agreement or a guarantee agreement, which may last between 12 and 18 months in the first instance. The enforcement of non-European judgments may also be of the same duration.

7.4 With respect to enforcing collateral security, are there any significant restrictions which may impact the timing and value of enforcement, such as (a) a requirement for a public auction, or (b) regulatory consents?

French law security interests may only be enforced upon the occurrence of a payment default (either resulting from a non-payment of interest, fees or principal or following an acceleration of the secured facilities) and not upon the occurrence of any event of default.

Enforcement of a pledge may be carried out under French law either through judicial foreclosure or public auction or by way of private foreclosure. Enforcement through judicial proceedings (i.e., judicial foreclosure or public auction) may take a significant amount of time (12–18 months with respect to a mortgage or up to 12 months for other types of security interests), whereas enforcement through private foreclosure may generally take up to two weeks.

The enforcement of a securities account pledge granted over the shares of a listed company may require a regulatory consent from the French stock exchange regulator (*Autorité des Marchés Financiers*) if the pledge is enforced through private foreclosure over more than 30% of the shares of the listed company. Under French takeover rules, where a person, acting alone or in concert, comes to hold directly or indirectly more than 30% of a company's equity securities or voting rights, such person is required, on its own initiative, to inform the French stock exchange regulator immediately and to file an offer for all the company's equity securities. In order to avoid the obligation to file a mandatory bid, an authorisation may be requested from the French stock exchange regulator to temporarily cross the 30% threshold upwards. Such an authorisation may be granted provided that the lenders undertake to sell the shares held in excess of the 30% threshold within a six-month period.

7.5 Do restrictions apply to foreign lenders in the event of (a) filing suit against a company in your jurisdiction, or (b) foreclosure on collateral security?

There are no specific restrictions applying to foreign lenders in the event of filing suit against a company in France or foreclosure on collateral security. It should, however, be noted that for the writ of summons before the Commercial Court ("*tribunal de commerce*") to be valid, the foreign plaintiff has to elect domicile in France.

7.6 Do the bankruptcy, reorganisation or similar laws in your jurisdiction provide for any kind of moratorium on enforcement of lender claims? If so, does the moratorium apply to the enforcement of collateral security?

Yes, the opening of certain bankruptcy proceedings – safeguard proceedings (*sauvegarde*), accelerated safeguard proceedings (*sauvegarde accélérée*), accelerated financial safeguard proceedings (*sauvegarde financière accélérée*), judicial administration proceedings (*redressement judiciaire*) or liquidation proceedings (*liquidation judiciaire*) – provide for a moratorium of enforcement with respect to lender claims and collateral security (save for collateral security created under a *Dailly* assignment of receivables, a cash collateral agreement (*gage-espèces*), a receivables delegation agreement (*délégation de créances*) or a *fiducie* agreement (but only in the case of a so-called possessory *fiducie* (*fiducie avec dépossession*) whereby the assets are effectively transferred to the *fiduciaire*).

7.7 Will the courts in your jurisdiction recognise and enforce an arbitral award given against the company without re-examination of the merits?

French courts do not carry out a judicial review of the merits of arbitral awards. They only play a supervision function regarding the validity of arbitral awards for which recognition and enforcement are sought in France. Pursuant to the French Civil Procedure Code, a French court can set aside an arbitral award only if:

- the arbitral tribunal wrongly upheld or declined jurisdiction;
- the arbitral tribunal was not properly constituted (i.e. it was irregularly composed or the sole arbitrator was irregularly appointed);
- the arbitral tribunal ruled without complying with the mandate conferred upon it;
- due process (*principe du contradictoire*) was not respected; or
- recognition or enforcement of the award would be contrary to international public policy (*ordre public international*).

8 Bankruptcy Proceedings

8.1 How does a bankruptcy proceeding in respect of a company affect the ability of a lender to enforce its rights as a secured party over the collateral security?

See the answer to question 7.6 above.

8.2 Are there any preference periods, clawback rights or other preferential creditors' rights (e.g., tax debts, employees' claims) with respect to the security?

If a security interest is granted by a French company during a so-called hardening period (*période suspecte*), such security interest may be declared null and void if (i) it has been granted in order to secure a previously incurred debt, or (ii) it has been granted in order to secure a current or future debt, but the beneficiary of the security had knowledge of the insolvency of the grantor. The hardening period is a period set by the bankruptcy court during which the guarantor/pledgor is deemed to be insolvent. According to the French law insolvency test (*cessation des paiements*), a company is insolvent if it is unable to pay its liabilities as they fall due with its immediately available assets (cash or other liquidity assets). A French bankruptcy court may set the insolvency date of a company as far as 18 months prior to the date on which the company has filed for insolvency.

French law provides for preferential creditor rights with respect to: employees' claims; legal expenses; new loans made available during a court-approved conciliation proceeding; security interests over real estate property; and security interests benefiting from a retention right (such as a share pledge, a securities account pledge or a bank account pledge).

8.3 Are there any entities that are excluded from bankruptcy proceedings and, if so, what is the applicable legislation?

Entities regulated by public law (*personnes morales de droit public*) (such as *collectivités territoriales* or *établissements publics*) are excluded from bankruptcy proceedings.

Entities which are not registered with the commercial register and do not have a legal personality (such as *sociétés en participation*, *sociétés de fait*, *sociétés en formation*) are also excluded from bankruptcy proceedings.

8.4 Are there any processes other than court proceedings that are available to a creditor to seize the assets of a company in an enforcement?

Yes, private foreclosure (*pacte commissoire*) is permitted under French law with respect to almost all types of security interests, save for certain exceptions such as a pledge over business as a going concern.

However, enforcement by private foreclosure is prohibited during certain insolvency and pre-insolvency proceedings such as safeguard proceedings, accelerated safeguard proceedings, accelerated financial safeguard proceedings, judicial administration proceedings and judicial liquidation proceedings.

9 Jurisdiction and Waiver of Immunity

9.1 Is a party's submission to a foreign jurisdiction legally binding and enforceable under the laws of your jurisdiction?

French law allows considerable freedom to the parties to a contract in selecting a jurisdiction for their disputes, with the notable exception of disputes relating to real property, which must be resolved by the appropriate court at the place where the property is located.

The choice of a foreign jurisdiction is valid provided that:

- the dispute is international, it being specified that French courts do not require that the dispute has a material link to the foreign jurisdiction chosen by the parties;
- the jurisdiction choice clause does not preclude the mandatory exclusive jurisdiction of a French court in relation to certain aspects (e.g. in relation to employment contracts); and
- the clause is not a unilateral dispute resolution clause giving only one party the choice between several jurisdictions while the other party is bound to bring actions before one jurisdiction only (this principle was recently confirmed by a decision rendered by the French Supreme Court on 26 September 2012).

9.2 Is a party's waiver of sovereign immunity legally binding and enforceable under the laws of your jurisdiction?

Waivers of sovereign immunity from jurisdiction are legally binding and enforceable under the laws of France.

But a waiver of sovereign immunity from jurisdiction does not entail a waiver of immunity from execution, which must be separately expressed in order for it to be equally binding and enforceable. A decision of the French supreme court (*Cour de cassation*) dated 13 May 2015 has, until recently, been seen as having overturned the previous requirement for the waiver of immunity from execution to specifically identify the assets or the category of assets in respect of which such waiver is granted.

This was, however, amended on 9 December 2016, following the enactment of the *Loi Sapin 2*, which entered into force on 11 December 2016 and introduced a new authorisation procedure that requires the creditor to seek, in an *ex parte* proceeding, an order for an interim or enforcement measure against the foreign sovereign State.

In this regard, *Loi Sapin 2* provides that interim or enforcement measures relating to property belonging to a foreign sovereign State may only be authorised if one of the following conditions is met:

- the foreign sovereign State has expressly consented to such measure;
- the foreign sovereign State has reserved or assigned the property in accordance with the request; or
- where a judgment or arbitral award has been rendered against the foreign sovereign State and the property at stake is specifically used or intended to be used by that foreign sovereign State otherwise than for the purposes of public service and there is a relationship with the foreign sovereign State entity against which the proceedings were instituted.

A specific regime has also been created by the *Loi Sapin 2* with respect to property (including bank accounts) used in the exercise of diplomatic missions of foreign States by requiring for this category of property an express and special waiver of immunity from the foreign State in order for any interim or enforcement measures to be taken with respect to such property.

Finally, no interim measures and no enforcement action against property belonging to a foreign sovereign State can be authorised by a French judge in favour of the holder of a debt obligation or an instrument or right with characteristics similar to a debt instrument if:

- the foreign sovereign State was receiving aid from the Development Assistance Committee of the OECD when it issued the debt document;
- the holder of the debt obligation acquired that security when the foreign sovereign State was in default on that debt obligation or proposed a change in the terms of the debt obligation; and
- the default status on the debt obligation is less than 48 months at the time the holder of the debt obligation seeks a court order authorising him to seek an order for enforcement.

10 Licensing

10.1 What are the licensing and other eligibility requirements in your jurisdiction for lenders to a company in your jurisdiction, if any? Are these licensing and eligibility requirements different for a "foreign" lender (i.e. a lender that is not located in your jurisdiction)? In connection with any such requirements, is a distinction made under the laws of your jurisdiction between a lender that is a bank *versus* a lender that is a non-bank? If there are such requirements in your jurisdiction, what are the consequences for a lender that has not satisfied such requirements but has nonetheless made a loan to a company in your jurisdiction? What are the licensing and other eligibility requirements in your jurisdiction for an agent under a syndicated facility for lenders to a company in your jurisdiction?

Pursuant to French banking monopoly rules, an entity which carries out banking activities on a regular basis in France (irrespective of whether such entity is located in or outside of France) in most cases must be either (i) duly licensed as a credit institution (*établissement de crédit*) or as a financing company (*société de financement*) in France, or (ii) duly "passported" under the European Directive 2000/12 to provide such services in France.

Recent reforms have however introduced some important exceptions to the French banking monopoly rules:

- The following alternative investment entities will now also be authorised, under certain conditions, to make loans to a French borrower: professional specialised investment funds (*fond professionnels spécialisés – FPS*); professional private equity investment funds (*fonds professionnels de capital investissement – FPCI*); French limited partnerships (*société de libre parteneriat – SLP*); securitisation vehicles (*organismes de titrisation – OT*); and professional specialised investment funds (*organismes de financement spécialisés – OFS*). Certain specific conditions for the granting of loans by these entities are to be set out in a decree which is expected to be published in the following months. In the meantime, these entities are permitted to grant loans as an exception to the French banking monopoly rules if they obtain a European long-term investment fund ("**ELTIF**") authorisation from the French securities regulator (*Autorité des Marchés Financiers – AMF*) in application of the European regulation 2015/760 on European long-term investment funds. However, it should be noted that since 3 January 2018, the securitisation vehicles are no longer authorised to apply for the ELTIF authorisation.

- A company may, as an ancillary activity to its main business, grant loans to another company with which it has economic ties justifying the granting of such loans. These provisions have become effective on 22 April 2016 when a decree listing all the conditions to be met for such loans to not fall foul of the French banking monopoly rules has been published. There are more than 20 conditions which have to be met, including the following:

  (a) the maturity of the loan must not exceed two years;

  (b) the lender must be a joint stock company (a *société anonyme* or a *société par actions simplifiée*) or a limited liability company (*société à responsabilité limite*) whose accounts, in each case, are certified by an auditor;

  (c) the borrower must be a small or medium-sized company;

  (d) the entry into the loan agreement is subject to a specific corporate approval process;

  (e) the amount of the loan must be specified in the management report and included in an auditor's certificate; and

  (f) the receivables under such loan may not be assigned to securitisation vehicles or to specialised funds or be subject to forward contracts (*instruments financiers à terme*) or instruments used to transfer insurance risks to such securitisation vehicles or specialised funds.

It should also be noted that there are some other limited exceptions to the banking monopoly rules which apply to specific entities or to specific types of loans (such as participating loans (*prêts participatifs*) – long-term subordinated loans with a fixed interest rate which can be granted by a commercial company to another commercial, agricultural or industrial company).

Non-compliance with the French banking monopoly rules may lead to criminal liability, but according to French Supreme Court case law, a banking transaction carried out in violation of the banking monopoly rules remains valid (however, it should be noted that French courts are not bound by precedent).

With respect to licensing requirements for agents, if such agents provide services which are regulated in France such as payment services, these entities are required to be licensed in order to carry out such services in France.

11 Other Matters

11.1 Are there any other material considerations which should be taken into account by lenders when participating in financings in your jurisdiction?

Among the other specificities with respect to French law financing transactions, the following should be taken into account: (1) interest under a French law loan agreement may only be compounded if it has accrued for a period of at least one year; and (2) a special effective global rate ("**TEG**") notice must be sent to French borrowers no later than the day of entering into of the credit agreement.

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1 Overview

1.1 What are the main trends/significant developments in the lending markets in your jurisdiction?

In 2017 generally, the lending business in Germany increased again compared to the previous year. Borrowers continue to profit from low interest rates and few companies report difficulties in having access to the lending market. There are three main factors which currently have a positive effect on new lending business: the continuing good economic situation; reduced political risks; and the increasing likelihood of higher borrowing costs in the future. While acquisition finance and promissory notes (*Schuldschein*) boom, at the same time, however, certain other segments of the market such as export finance still suffer from continuing sanctions.

1.2 What are some significant lending transactions that have taken place in your jurisdiction in recent years?

In 2017, **Bain and Cinven** took up a EUR 2.6 billion loan for the financing of the acquisition of **Stada**. The financing was granted by eight banks and comprised term loans as well as secured and unsecured credit lines. The acquisition of **Monsanto** by **Bayer** (yet to be closed) was financed by a EUR 51.6 billion loan which was partly forwarded by Bank of America, Credit Suisse, Goldman Sachs, HSBC and JP Morgan to more than 20 banks. In 2016, **Fresenius** acquired the Spanish clinic operator **Quirónsalud** for a purchase price of EUR 5.76 billion. In a first step, the financing was secured by a bridge loan in the amount of EUR 3.75 billion which was then refinanced by various other lending produces, e.g. a long-term syndicated loan in the amount of EUR 1.2 billion, a promissory note (*Schuldschein*) in the amount of EUR 1 billion and bonds in the amount of EUR 2.6 billion.

2 Guarantees

2.1 Can a company guarantee borrowings of one or more other members of its corporate group (see below for questions relating to fraudulent transfer/financial assistance)?

It is common in credit agreements under German law, that a company guarantees borrowing of other members of its corporate group. Downstream guarantees, in general, do not cause specific problems. In case of upstream and cross-stream guarantees granted by a limited liability company (GmbH) or a stock corporation (AG) or *societas europaea* (SE) capital maintenance rules applicable to the respective guarantor must be observed. The same applies for corporate structures where corporations of the relevant types ultimately assume the liability for the relevant guarantee, e.g. in case of a German law GmbH & Co KG (a limited partnership where a limited liability company is the general partner).

These rules do not only apply to guarantees, but also to other forms of security, including sureties (*Bürgschaften*).

2.2 Are there enforceability or other concerns (such as director liability) if only a disproportionately small (or no) benefit to the guaranteeing/securing company can be shown?

With regard to enforceability of guarantees and other form of security, including sureties (*Bürgschaften*), certain restrictions have to be observed in order to avoid possible personal liability of the managers of the respective company which has granted security. Differentiation has to be made with regard to the corporate form of the company.

GmbHs: It used to be standard market practice in Germany to include enforcement limitation language in the documentation for upstream and cross-stream guarantees which limits any enforcement action by a secured borrower to free funds of the limited liability company. Such limitation language is included in the relevant guarantee documentation to protect the managing directors of the company against personal liability which could otherwise be triggered in case an enforcement action would result in the share capital of the company falling below the statutory minimum share capital.

For a long time it was disputed in German legal literature which point in time should be relevant for assessing whether a shortfall of the statutory minimum share capital would occur or not: the point in time when the guarantee is granted or the point in time when it comes to realisation of the guarantee by way of enforcement. According to recent court decisions of the German Federal Supreme Court (*Bundesgerichtshof – BGH*), no liability of the managing director shall be triggered if the manager, after due and diligent assessment of the financial situation of the company, comes to the conclusion that, at the point in time of granting collateral, it can be assumed that the principal debtor will be in a position to repay its borrowing so that the collateral will not have to be realised and no shortfall of the statutory minimum share capital will occur. Although the relevant court decisions do not directly relate to guarantees, this has triggered discussions in the German market regarding the justification and future role of limitation language, and possible adjustments of the existing practice to these new court decisions. It is therefore recommended to seek legal advice to properly address the resulting changes to the legal framework.

GmbH & Co. KG: The explanations above are also true for the general partner of a limited partnership which would ultimately assume the liability for any security granted by the limited partnership.

AG: The capital maintenance rules to be observed in case of an AG are even stricter. In principle, any payments and the granting of any advantages by the company to its shareholders are prohibited (except for the distribution of dividends on the basis of a resolution of the general meeting of the shareholders). Such payments and advantages are only permitted in a limited number of cases, e.g. in case of an existing control and profit transfer agreement or in case the company granting the security has a valid compensation claim against its shareholders.

Societas Europaea (SE): Pursuant to Art. 5 of Council Regulation (EC) No 2157/2001 of 8 October 2001 on the Statute for a European company (SE) the capital of an SE, its maintenance and changes thereto, together with its shares, bonds and other similar securities shall be governed by the provisions which would apply to a public limited liability company with a registered office in the Member State in which the SE is registered. Hence the rules for German stock corporations apply accordingly on SEs registered in Germany.

2.3 Is lack of corporate power an issue?

Lack of corporate power is generally not an issue. German law does not recognise the concept of "*ultra vires*" for companies (save for certain specific exceptions). Limitations to the managing director's power to represent the company (e.g. based on articles of association or internal rules of procedure for the management) do, in principle, have no effect in relation to third parties. An exception applies if it is obvious for the third party that the managing director has exceeded their authority to represent the corporation or if the managing director and the relevant third party have cooperated in a collusive way to the detriment of the company. A further exception applies, at least according to German jurisdiction and legal scholars, to certain legal entities under public law which shall not be in a position to validly enter into legal transactions which go beyond their statutory field of activity.

2.4 Are any governmental or other consents or filings, or other formalities (such as shareholder approval), required?

A guarantor qualifies as a credit institution and hence requires a licence from the German Federal Financial Supervisory Authority (*BaFin*) if it issues guarantees in a commercial manner or in a way which requires a commercial business organisation (§ 31 in conjunction with § 1 para. 1 no. 8 of the Banking Supervisory Act – Kreditwesengesetz, "**KWG**"). A guarantor shall, however, not qualify as a credit institution if it conducts the relevant transactions only with its parent company, subsidiaries or sister companies (§ 2 para. 1 no. 7 of the KWG). However, the construction of this so-called group privilege is now much stricter than in former years.

Guarantees issued by private companies are not subject to individual government consent requirements. Exceptions may apply to public entities acting as guarantors, in addition to state aid rules applicable on public and publicly owned entities.

While there is no statutory requirement for a shareholders' resolution or resolution of the supervisory board or other corporate bodies in case of the assumption of guarantees, the articles of association of the respective corporation may require such consent.

2.5 Are net worth, solvency or similar limitations imposed on the amount of a guarantee?

No, except for the limitations imposed by the capital maintenance rules under German law (*cf.* above under questions 2.1 and 2.2).

2.6 Are there any exchange control or similar obstacles to enforcement of a guarantee?

Under German law there are generally no exchange controls that would restrict the enforcement of a guarantee.

This is without prejudice to restrictions resulting from existing German or European sanctions legislations, which affects guarantees also.

3 Collateral Security

3.1 What types of collateral are available to secure lending obligations?

Under German law, in principle, all transferable assets are eligible as collateral. Common types of classic security are pledges and transfers and assignments for security purposes in case of movable assets, and mortgages and land charges in case of real property. In addition thereto, there exist certain special types of security rights such as mortgages for aircrafts and vessels and other less common types of security, in addition to quasi-security arrangements.

Shares and bank accounts are commonly pledged. Financial institutions usually insist on the use of their own templates for the pledge of accounts held with them. Receivables, claims and intellectual property rights may be assigned as security and the ownership in fixed assets (such as movable property and equipment) is frequently transferred as security. Real property may be encumbered by a mortgage or land charge.

3.2 Is it possible to give asset security by means of a general security agreement or is an agreement required in relation to each type of asset? Briefly, what is the procedure?

Security over different kinds of assets could be created in the same agreement. However, particularities would need to be observed with respect of each asset class and with respect to each type of security. Furthermore, security over real property requires notarial form, for which reason it would be inefficient to combine this in the same document.

It is more common under German law, to create collateral in a separate agreement for each type of security, and furthermore the parties may wish to enter into different documents if third parties are involved.

German law does not recognise the concept of floating charges.

3.3 Can collateral security be taken over real property (land), plant, machinery and equipment? Briefly, what is the procedure?

Real property can be encumbered by a land charge (including rent charges) or a mortgage. Land charges are more common because – unlike mortgages – they are independent in their existence from the underlying claim which is secured by them. While a mortgage can only be transferred together with the underlying receivable, a land charge can be created and transferred without the receivable secured by it. Both, mortgages and land charges need to be established in notarised form and registered in the land register to become valid. A land charge can be created without certificate (*Buchgrundschuld*) or as a certified land charge (*Briefgrundschuld*) in which case the handover of the certificate to the beneficiary of the land charge is necessary. A land charge or mortgage also covers appurtenances (*Zubehör*), but attention should be paid to the distinction between immovable and movable assets, e.g. in case of temporary structures.

Ownership in plant, machinery and equipment which are not an essential part of the property, can be transferred as security by a simple transfer agreement. Here, special attention should be paid to possible conflicts of different security rights (e.g. conflicts with reservation of title arrangements).

3.4 Can collateral security be taken over receivables? Briefly, what is the procedure? Are debtors required to be notified of the security?

Yes. The common way of creating security over receivables and claims of the debtor is a security assignment which is usually executed in simple written form. The obligor generally does not need to be notified to create a valid assignment, and, according to market practice, many assignments remain undisclosed. However, a notification is required for perfection purposes. Since the obligor may still validly fulfil its obligation by payment to the former creditor (unless the obligor has knowledge of the assignment to the new creditor), it may be advisable to notify the obligor of the assignment in order to mitigate such risk. The relevant receivables to be assigned must be identifiable without doubt, a requirement that requires particular attention in case of future receivables.

Attention should be paid to contractual consent requirements which may apply on the assignment of individual receivables.

3.5 Can collateral security be taken over cash deposited in bank accounts? Briefly, what is the procedure?

The common form to create security over a bank account and cash deposited therein is an account pledge which is generally entered into in simple written form. Most financial institutions insist on the use of their own templates for pledges of accounts held with them. The pledge needs to be notified to the account holding bank as obligor. Such notification is a validity requirement.

3.6 Can collateral security be taken over shares in companies incorporated in your jurisdiction? Are the shares in certificated form? Can such security validly be granted under a New York or English law governed document? Briefly, what is the procedure?

With regard to shares in companies, a pledge is the most common form of security. A pledge over shares in a German limited liability company (GmbH) requires notarisation. It is generally not necessary to notify the pledge to the GmbH. However, the articles of association of the GmbH may require the prior consent of the company or its shareholders for a share pledge to become effective. The creation of the pledge is governed by the law governing the company, i.e. in case of a German GmbH by German law. It is not possible to agree on foreign law as applicable law for the creation of the pledge.

A pledge over shares in a stock corporation may be completed without observing specific formalities. However, any share certificates issued for the relevant shares need to be transferred to the pledgee. Generally the shares are certificated in one global certificate (*Globalurkunde*) which is deposited with a clearing system. In such case the (indirect) possession of (parts of) the certificate needs to be transferred which can be achieved by transferring the respective claim for handover. The creation of the pledge is governed by the law in which the share certificates are situated (*lex rei sitae*), i.e. in case of a German stock corporation the shares of which are deposited in Germany by German law. It is not possible to agree on foreign law as applicable law for the necessary transfer of ownership in the share certificate. In case of registered shares (*Namensaktie*) the transfer/pledge is regularly evidenced on the certificate by way of endorsement (*Indossament*).

3.7 Can security be taken over inventory? Briefly, what is the procedure?

Security transfers are generally used in order to create security over inventory or movable property. A security transfer agreement is generally executed in simple written form. A practical challenge is the precise and identifiable description of the assets, in particular with regard to inventory. In such case, the agreement will frequently be either all-inclusive, refer to a certain area on the business premises and state that title to all assets located therein will be transferred, or list individual inventory in an explicit way.

3.8 Can a company grant a security interest in order to secure its obligations (i) as a borrower under a credit facility, and (ii) as a guarantor of the obligations of other borrowers and/or guarantors of obligations under a credit facility (see below for questions relating to the giving of guarantees and financial assistance)?

Yes, a company can grant security to secure its own obligations as a borrower under a credit facility as well as its obligations as a guarantor for obligations of other borrowers/guarantors. For limitations, please see questions 2.1 and 2.2.

3.9 What are the notarisation, registration, stamp duty and other fees (whether related to property value or otherwise) in relation to security over different types of assets?

Where notarisation is required in order to create security (e.g. pledge of shares in a limited liability company (GmbH) or creation of a land charge or mortgage), notary fees are incurred. The amount of the notary fees depends on the value of the encumbered assets and is calculated according to a statutory fee schedule. In addition, registration fees of the land register will be triggered for the registration of a land charge or mortgage. However, German law does not know the concept of stamp duty.

3.10 Do the filing, notification or registration requirements in relation to security over different types of assets involve a significant amount of time or expense?

Land charges and mortgages need to be registered in a public register. The land register at the local court of the district where the encumbered real estate is situated will be competent for the registration. Depending on the land register in charge and the complexity of the legal questions to be assessed, the registration procedure might take anything from one or two days to several weeks. In case the encumbered real property itself is not yet registered (e.g. in case of the formation of one or more new plots of land as a result of a split, merger or other alteration of existing plots of land), there may be additional time required to effect necessary land survey, etc.

With regard to expenses please see our answer to question 3.9.

3.11 Are any regulatory or similar consents required with respect to the creation of security?

No general regulatory or similar consents are required with respect to the creation of security.

With regard to licence requirements applicable on a guarantor that qualifies as a financial institution, and with respect to public or publicly owned entities, please see answer to question 2.4.

3.12 If the borrowings to be secured are under a revolving credit facility, are there any special priority or other concerns?

There are generally no special priority or other concerns with regard to security, if borrowings are granted under a revolving credit facility. Under German law, it is even possible to grant security for future obligations and to extend security interest to future-acquired assets (e.g. a future claim or revolving inventory) as long as they can be identified at the time of the conclusion of the security agreement in a manner that ensures their determinability when acquired.

3.13 Are there particular documentary or execution requirements (notarisation, execution under power of attorney, counterparts, deeds)?

Regarding notarisation requirements, please see answers to questions 3.3 and 3.6. Execution under power of attorney is generally possible. However, notarial certificates of representation might be required if the signatories of the power of attorney are not registered in public registers (e.g. in the commercial register). Powers of attorney which shall be used for real estate transactions and for filings with public registers (commercial register, land register) generally need to be executed in notarial form. For notarisations effected in certain foreign countries, the notarial certification must be accompanied by an apostille.

4 Financial Assistance

4.1 Are there prohibitions or restrictions on the ability of a company to guarantee and/or give security to support borrowings incurred to finance or refinance the direct or indirect acquisition of: (a) shares of the company; (b) shares of any company which directly or indirectly owns shares in the company; or (c) shares in a sister subsidiary?

(a) Shares of the company

For stock corporations, section 71a para. 1 of the German Stock Corporation Act (AktG) contains a strict prohibition to grant a loan or security to third parties in order to enable such third party to acquire shares in the company. This prohibition does not apply in case financial assistance is granted (i) in the course of the regular business of a credit or financial services institution, (ii) on the basis of an existing control and profit and loss transfer agreement, and (iii) in connection with an employee participation programme.

German law does not provide for an explicit prohibition of financial assistance measures for limited liability companies (GmbH). However, the capital maintenance rules applicable to limited liability companies (for details *cf.* above under questions 2.1 and 2.2), often result in a similar effect.

(b) Shares of any company which directly or indirectly owns shares in the company

For stock corporations, section 71a para. 1 of the German Stock Corporation Act is not directly applicable. However, according to section 71d para. 1 sentence 2 and 4 of the German Stock Corporation Act, the financial assistance rules described above apply accordingly in case a controlled company grants a loan or security to a third party in order to enable such third party to acquire shares in the controlling company.

For limited liability companies, restrictions may result from the capital maintenance rules described above under questions 2.1 and 2.2.

(c) Shares in a sister subsidiary

The financial assistance rules for stock corporates as described above do not directly apply in such a scenario. However, for stock corporations as well as limited liability companies restrictions may result from the general capital maintenance rules (*cf.* questions 2.1 and 2.2 above).

5 Syndicated Lending/Agency/Trustee/Transfers

5.1 Will your jurisdiction recognise the role of an agent or trustee and allow the agent or trustee (rather than each lender acting separately) to enforce the loan documentation and collateral security and to apply the proceeds from the collateral to the claims of all the lenders?

German law generally recognises the role of an agent or trustee, also with regard to the enforcement of security.

Exceptions apply to "accessory" security interest (for details, see the answer to question 5.2).

5.2 If an agent or trustee is not recognised in your jurisdiction, is an alternative mechanism available to achieve the effect referred to above which would allow one party to enforce claims on behalf of all the lenders so that individual lenders do not need to enforce their security separately?

With regard to certain accessory security rights (which are legally inseparable from the secured claim), it is common practice to create, in addition to the underlying secured claim, a parallel debt, i.e. a second claim for the benefit of the security trustee as abstract acknowledgment of debt in the amount of the current or future payment obligations against the finance parties. In order to avoid risks of double payment, the security trustee must not realise its claim under the abstract acknowledgment of debt to the extent the original secured claim has been fulfilled. The parallel debt structure ensures that certain accessory security rights (e.g. pledges, guarantees) are not terminated by operation of law in case of changes to the lenders of a syndicated loan agreement involving the termination of the initial secured claim while creating a new claim with the acquirer. While the validity of parallel debt structures is generally accepted in German legal literature, it has not yet been confirmed by German courts.

5.3 Assume a loan is made to a company organised under the laws of your jurisdiction and guaranteed by a guarantor organised under the laws of your jurisdiction. If such loan is transferred by Lender A to Lender B, are there any special requirements necessary to make the loan and guarantee enforceable by Lender B?

The loan and a guarantee, which by nature is non-accessory, can generally each be transferred by simple assignment agreement. In contrast to a guarantee, a surety (*Bürgschaft*) (which is of an accessory nature) will automatically transfer upon assignment of the secured loan.

Also with regard to possible defences of a guarantor under German law, differentiation has to be made between guarantees and sureties. While the most common form is the independent (non-accessory) guarantee, the guarantor has only very limited defences in this case. Further details depend on the type of guarantee (e.g. guarantees on first demand, standard guarantees, etc.) involved and the underlying terms of the individual guarantee. In particular, in case of an independent guarantee, the existence of the main debt is not a condition for the guarantor's obligation to pay. Often the guarantor is restricted to the objection of abuse of law by the creditor.

In contrast thereto, a surety (*Bürge*) can principally invoke all defences and objections of the main debtor. The surety can also refuse payment in case the debtor is entitled to challenge the transaction creating its debt and in case the creditor can satisfy its claim by way of set-off against a claim of the debtor. Further, the surety is generally only obliged to pay the creditor if the creditor cannot realise its claim against the debtor. All these defences are subject to a possible waiver by the surety. However, a waiver might be invalid if agreed upon in general terms and conditions because such waiver would contradict the concept of accessoriness and transform the surety into an instrument that is tantamount to an independent, non-accessory guarantee.

6 Withholding, Stamp and Other Taxes; Notarial and Other Costs

6.1 Are there any requirements to deduct or withhold tax from (a) interest payable on loans made to domestic or foreign lenders, or (b) the proceeds of a claim under a guarantee or the proceeds of enforcing security?

In general, there is no requirement under German tax law to deduct or withhold tax from (a) interest payable on loans made to domestic or foreign lenders, or (b) the proceeds of a claim under a guarantee or the proceeds of an enforcement of security, provided the loan has no profit link feature and is not securitised as fungible debt instrument.

However, interest payments to a foreign lender may be considered German-sourced income, if the loan is directly or indirectly secured by German-situs real property, comparable rights or ships registered in Germany. In such a case, the foreign lender might be under an obligation to file a tax return (at least, where an applicable double taxation agreement also permits Germany to tax such income from interest payments). In such a case, the German tax authorities have the discretion to require the obligor to withhold tax. The tax rate for a corporate taxpayer is 15.825%. Any tax withheld might be credited or refunded upon tax assessment on the foreign lender.

6.2 What tax incentives or other incentives are provided preferentially to foreign lenders? What taxes apply to foreign lenders with respect to their loans, mortgages or other security documents, either for the purposes of effectiveness or registration?

There are no German tax incentives or other incentives provided to foreign lenders. No taxes apply with respect to their loans, mortgages or other security documents for the purposes of effectiveness or registration.

6.3 Will any income of a foreign lender become taxable in your jurisdiction solely because of a loan to or guarantee and/or grant of security from a company in your jurisdiction?

No. The income of a foreign lender will not become taxable in Germany solely because of a loan to or guarantee and/or generally the grant of security from a company in Germany.

However, the income of a foreign lender, notwithstanding the foregoing, may become taxable in Germany in case the loan is secured by real estate in Germany, comparable rights or ships registered in Germany (see above at question 6.1). This does, in general, not apply in case of the existence of a double taxation agreement between Germany and the country of residence of the foreign lender.

Furthermore, the income of the foreign lender may become taxable in Germany in cases where such income is attributable to the business property of a permanent establishment (including a permanent representative) of such a lender in Germany.

6.4 Will there be any other significant costs which would be incurred by foreign lenders in the grant of such loan/guarantee/security, such as notarial fees, etc.?

The costs for foreign lenders will generally not be different from the costs incurred by a German lender. For such costs, please see the answer to question 3.9.

6.5 Are there any adverse consequences to a company that is a borrower (such as under thin capitalisation principles) if some or all of the lenders are organised under the laws of a jurisdiction other than your own? Please disregard withholding tax concerns for purposes of this question.

There are generally no such adverse consequences under German law.

However, in cross-border transactions there may be conflicting sanction rules, and German law establishes a prohibition to submit to foreign boycotts.

7 Judicial Enforcement

7.1 Will the courts in your jurisdiction recognise a governing law in a contract that is the law of another jurisdiction (a "foreign governing law")? Will courts in your jurisdiction enforce a contract that has a foreign governing law?

According to article 3 para. 1 of regulation (EC) no 593/2008 on the law applicable to contractual obligations (Rome I), which is applicable in Germany, a contract shall be governed by the law chosen by the parties. A specific link to a foreign jurisdiction is generally not required in order for the choice of law to be valid. However, in case the only link to a foreign jurisdiction is the law chosen by the parties, mandatory provisions of the jurisdiction to which the case is linked will apply irrespective of the chosen law. Further, the freedom of choice of law may be limited with regard to collateral and the underlying agreements. For example, *in rem* security is mandatorily governed by the law of the location of the property (*lex rei sitae*).

Apart from the aforementioned limitations, German courts will recognise foreign law chosen by the parties for the contract and enforce the respective provisions.

7.2 Will the courts in your jurisdiction recognise and enforce a judgment given against a company in New York courts or English courts (a "foreign judgment") without re-examination of the merits of the case?

With regard to English courts (as well as courts of other EU Member States), the recognition of judgments is governed by regulation (EU) no 1215/2012 on jurisdiction and recognition and enforcement of judgments in civil and commercial matters. According to article 36 of such regulation, a judgment given in a Member State shall be recognised in the other Member State without any special procedure being required. However, the party who wishes to invoke a judgment given in one Member State in another Member State needs to produce a copy of the judgment which satisfies the conditions necessary to establish its authenticity as well as a certificate to be issued pursuant to article 53 of the regulation containing certain information with regard to the court proceedings. In addition, the court may require the party to provide a translation of the certificate or the judgment. On application of a party, the recognition of a judgment may be denied in certain cases, e.g. in case of an evident breach of the German *ordre public* (*cf.* article 45 of the regulation).

With regard to New York courts (as well as courts of non-EU Member States), the recognition of judgments would be governed by the provisions of the German Code of Civil Procedure (ZPO). Such judgments will generally be recognised, subject to limited exceptions, e.g. if the foreign judgment violates the German *ordre public* (*cf.* section 328 ZPO).

7.3 Assuming a company is in payment default under a loan agreement or a guarantee agreement and has no legal defence to payment, approximately how long would it take for a foreign lender to (a) assuming the answer to question 7.1 is yes, file a suit against the company in a court in your jurisdiction, obtain a judgment, and enforce the judgment against the assets of the company, and (b) assuming the answer to question 7.2 is yes, enforce a foreign judgment in a court in your jurisdiction against the assets of the company?

It is difficult to predict how long it would take for a foreign lender to obtain and enforce a judgment or to enforce a German judgment in Germany since the timing will be influenced by different factors, such as the workload of the court, whether the defendant might introduce even unjustified defences, and the complexity of the case. In case a judgment by default can be obtained, the proceedings may only take a couple of weeks. In case of ordinary court or enforcement proceedings, the duration of the proceedings will depend on the individual circumstances of the case, and in particular on the type of defences brought forward by the defendant.

7.4 With respect to enforcing collateral security, are there any significant restrictions which may impact the timing and value of enforcement, such as (a) a requirement for a public auction, or (b) regulatory consents?

Pledged security is generally sold in a public auction which is a formal proceeding and requires prior notification of the owner of the pledged security at least one month before the public auction takes place. If the asset has a market price, pledged security can be enforced by way of a private sale at the choice of the pledgee. Banks prefer private sales, as they usually lead to better results and are less formalistic.

Land charges and mortgages are enforced by way of a public auction or forced administration in formal proceedings organised and conducted by a special enforcement court. However, the parties may agree on alternative forms of enforcement (e.g., private sale) in order to simplify proceedings and realise better results.

Assigned receivables against third parties are generally realised by collecting them from the debtor which does not entail specific formalities.

Regulatory consents are generally not required in connection with the enforcement of security except for the providers of debt collection services which need to be registered according to the German Legal Services Act (*Rechtsdienstleistungsgesetz*) which is only possible if certain requirements are met.

7.5 Do restrictions apply to foreign lenders in the event of (a) filing suit against a company in your jurisdiction, or (b) foreclosure on collateral security?

In general, no such restrictions apply to foreign lenders. However, lenders from countries other than EU Member States or Member States of the Hague Convention of 1 March 1954 on Civil Procedure might be obliged to provide collateral for court costs.

7.6 Do the bankruptcy, reorganisation or similar laws in your jurisdiction provide for any kind of moratorium on enforcement of lender claims? If so, does the moratorium apply to the enforcement of collateral security?

After filing for insolvency, but before the opening of actual insolvency proceedings the court may prohibit enforcement measures against the debtor (except for security over real estate).

After the opening of insolvency proceedings, individual enforcement measures are prohibited. However, a secured creditor generally has a right to preferential treatment which must be asserted against the insolvency administrator. However, certain forms of security can only be enforced by the insolvency administrator (e.g., movebles in the possession of the insolvency administrator, receivables).

7.7 Will the courts in your jurisdiction recognise and enforce an arbitral award given against the company without re-examination of the merits?

According to section 1061 of the German Code of Civil Procedure (ZPO), the recognition and enforcement of foreign arbitral awards in Germany is governed by the New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards dated 10 June 1958. On that basis, foreign arbitral awards will generally be recognised and enforced without re-examination of the merits of the case. Certain exceptions apply, as set out in the New York Convention.

8 Bankruptcy Proceedings

8.1 How does a bankruptcy proceeding in respect of a company affect the ability of a lender to enforce its rights as a secured party over the collateral security?

Security granted by a debtor that falls into bankruptcy may be affected by the debtor's insolvency. In insolvency proceedings over the assets of a debtor, secured creditors will be satisfied with priority (*Absonderung*). Unsecured creditors will be satisfied on a *pro rata* basis from the remaining assets once the secured creditors have been satisfied. Shareholders of the debtor rank last in the satisfaction chain. Furthermore, the insolvency administrator may challenge certain transactions of the insolvent debtor which occurred during certain periods prior to the insolvency and which impair the position of other creditors.

Security granted by third parties is generally not affected by an insolvency of the principal debtor.

8.2 Are there any preference periods, clawback rights or other preferential creditors' rights (e.g., tax debts, employees' claims) with respect to the security?

The insolvency administrator may challenge certain transactions of the insolvent debtor which occurred during certain clawback periods prior to the opening of insolvency proceedings. Relevant clawback periods vary from one month to 10 years prior to the insolvency proceedings and depend on the nature of the relevant legal action (e.g. 10 years in case the action was taken with intent to the detriment of other creditors).

With regard to tax debts, differentiation has to be made whether the relevant tax triggering event has occurred prior to the opening of insolvency proceedings (in which case no preferential payment of such debt will be made) or whether such event occurred after the opening of insolvency proceedings, e.g. by an action taken by the insolvency administrator (in which case such debt has to be satisfied with priority from the insolvency estate).

The same applies, in principle, to employee's claims: Claims which result from periods prior to the opening of insolvency proceedings will be treated as non-priority insolvency claims, whereas claims which result from the continuation of the employment relationship after the opening of insolvency proceedings will be satisfied with priority. In addition, employees of the insolvent debtor may be entitled to insolvency payments (*Insolvenzgeld*) to be paid by the Employment Agency on non-satisfied employment claims for a period up to three months prior to the opening of insolvency proceedings.

8.3 Are there any entities that are excluded from bankruptcy proceedings and, if so, what is the applicable legislation?

Under German law, certain public entities (e.g. the federal states, municipalities) are excluded from insolvency proceedings. Furthermore, financial institutions are subject to special rules for insolvency and winding-up proceedings under European law.

8.4 Are there any processes other than court proceedings that are available to a creditor to seize the assets of a company in an enforcement?

With regard to the collection of receivables, creditors may engage debt collection agencies (*Inkassounternehmen*) which need to be registered under the German Legal Services Act (*cf.* answer to question 7.4 above). Apart from that, creditors usually rely on court proceedings to seize the assets of a company in an enforcement. Private seizure measures are generally not permitted. Further, agreements entered into prior to an event which entitles a pledgee to enforcement and according to which the pledgee shall automatically become an owner of the pledged asset if his claim is not fulfilled in time, are null and void (*cf.* section 1229 of the German Civil Code).

9 Jurisdiction and Waiver of Immunity

9.1 Is a party's submission to a foreign jurisdiction legally binding and enforceable under the laws of your jurisdiction?

According to article 25 of regulation (EU) no 1215/2012 on jurisdiction and recognition and enforcement of judgments in civil and commercial matters a court shall have jurisdiction if the parties contractually agreed on the jurisdiction of such court. Certain requirements (e.g. agreement in writing or evidenced in writing, no exclusive jurisdiction of another court) need to be fulfilled.

9.2 Is a party's waiver of sovereign immunity legally binding and enforceable under the laws of your jurisdiction?

Sovereign immunity may become relevant in legal transactions involving states or state property. Enforcement into assets which serve a sovereign purpose is prohibited. However, a waiver of sovereign immunity is possible. To avoid conflicts, such waiver should be made in explicit (written) form.

10 Licensing

10.1 What are the licensing and other eligibility requirements in your jurisdiction for lenders to a company in your jurisdiction, if any? Are these licensing and eligibility requirements different for a "foreign" lender (i.e. a lender that is not located in your jurisdiction)? In connection with any such requirements, is a distinction made under the laws of your jurisdiction between a lender that is a bank *versus* a lender that is a non-bank? If there are such requirements in your jurisdiction, what are the consequences for a lender that has not satisfied such requirements but has nonetheless made a loan to a company in your jurisdiction? What are the licensing and other eligibility requirements in your jurisdiction for an agent under a syndicated facility for lenders to a company in your jurisdiction?

The German Banking Act (KWG) provides that the extension of loans in a commercial manner, or to an extent that requires a commercially organised business, requires a banking licence issued by the German Federal Financial Supervisory Authority or a corresponding licence issued by the responsible authority of another EEA Member State. The requirements are the same for German and foreign lenders if the loans are granted in Germany. No distinction is made between banks and non-banks if the extension of loans is made in the aforementioned manner.

Non-compliance with the licensing requirements is a criminal offence under German law and may, in addition, be sanctioned by fines.

No specific licensing or other eligibility requirements apply to an agent under a syndicated facility. However, in case the agent also acts as lender under the facility agreement, the aforementioned licensing requirements apply.

11 Other Matters

11.1 Are there any other material considerations which should be taken into account by lenders when participating in financings in your jurisdiction?

Some particularities under German law become particularly relevant in restructuring situations. Thus, in case fresh money shall be granted in the crisis of a company (by way of a bridge loan (*Überbrückungskredit*) or a restructuring loan (*Sanierungskredit*)), certain requirements have to be met in order to avoid that the lender is held liable for delaying insolvency proceedings of the company. Further, a lender (or its managers) who has significant influence on the business decisions of the borrower in the crisis of the borrower might qualify as *de facto* managing director of the borrower and incur liability in this regard. Details with regard to the granting of loans in the crisis of the company as well as with regard to the concept of a *de facto* managing director are not always clear and consistent, so that legal advice should be searched when it comes to such a situation. Finally, shareholders should be aware of the fact that shareholder loans are subordinated to all other claims of creditors of the borrower in insolvency proceedings of the borrower as a matter of statutory law.

Another particularity under German law and a unique type of borrowing used in the German market is a *Schuldscheindarlehen*. In such case the loan is traded in the form of a promissory note setting out the terms and conditions of the debt. A *Schuldscheindarlehen* might be advantageous for the borrower as it can enlarge the number of possible lenders and result in better conditions for the borrower.

Finally, in particular in cross-border transactions, the German and European sanctions regime needs to be observed, including German and European anti-blocking rules regarding foreign sanctions.

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Dietrich Stiller advises enterprises, sponsors, project companies and banks in a wide range of finance transactions. Alongside conventional corporate finance this also includes project finance, e.g. in the areas of renewable energies, conventional power plants, pipelines or airports, other transport infrastructure, telecommunication or industrial facilities. Many of those finance transactions are transnational and involve ECA or other guarantees of the German federal government, foreign export credit agencies (ECAs) or multinational institutions – also taking into account German and international sanctions. Legal advice in relationship to international projects furthermore includes the prevention of events of loss, or the mitigation of events of loss as well as legal support in case of actual or imminent expropriations, including legal advice in related arbitration proceedings.

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Prior to joining SZA Schilling, Zutt & Anschütz, Andreas Herr worked for several years in the Frankfurt and London office of a leading German law firm as well as for an investment bank in London.

SZA

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For almost a century, Schilling, Zutt & Anschütz has been one of the most reputable German law firms. We advise domestic and international clients in all areas of corporate and commercial law with currently 75 attorneys. Over the last years, our clients included 14 of the 30 enterprises listed on the DAX. We are legal counsel for leading industrial and trade enterprises, banks, insurance companies and financial services providers as well as large family-owned businesses and wealthy private clients.

In addition to issues dealing with general finance, bank and bank supervisory law, we advise our clients in all matters concerning financing transactions such as (tax-optimised) structuring of financing and financing instruments, including corresponding capital market products. We draft, negotiate and finalise the necessary financing and security agreements and comprehensively guide our clients in implementing and carrying out their financing and projects. Our expertise in financial law further comprises advice on work-outs / restructuring. We are well aware of what it takes in a company crisis.

Greece

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1 Overview

1.1 What are the main trends/significant developments in the lending markets in your jurisdiction?

Over recent years there have been two major developments in the Greek lending markets. First of all, institutional lenders, such as the European Bank for Reconstruction and Development ("**EBRD**") and the European Investment Bank ("**EIB**") are investing in Greek lending projects, supporting the Greek economy. Secondly, the real estate sector is developing at a fast pace and Greek banks are investing in real estate projects being developed by real estate investment companies ("**REICs**"). Notably, it should also be mentioned that, in virtue of Law no. 4354/2015, a new legal framework for the management and transfer of claims from non-performing loans ("**NPLs**") has been introduced into the Greek market, so as to help credit institutions clean up their balance sheets from non-performing, or so-called "red", loans. Further, Law no. 3869/2010 is also worth mentioning, considering that it was the first Greek legislative act to uniformly regulate the issue of over-credited individuals (non-merchants). The imperative need for a legal framework, regulating individuals' bankruptcy, which was itself a product of the financial crisis that has plagued Greece over much of the past decade, dictated the passage of Law no. 3869/2010, which involves a judicial settlement of the debts that the bankrupt individual is unable to repay.

1.2 What are some significant lending transactions that have taken place in your jurisdiction in recent years?

One of the most significant lending transactions that is ongoing is the privatisation of 14 Greek regional airports. Fraport Greece, the concessionaire for the 14 Greek regional airports, is owned by Fraport AG, Copelouzos Group and Marguerite, the 2020 European Fund. This group of lenders provides long-term financing to the concessionaire of a total amount of €813,000,000. The project is a significant large-scale infrastructure project in Greece, to be financed under a Public Private Partnership ("**PPP**") arrangement. The transition impact of the project is expected to come mainly from greater private sector involvement in the airports sector through demonstrating the effect of: (i) the benefits of private sector financing of infrastructure assets which may be replicated by the Greek government in other sectors and also by governments in neighbouring countries considering infrastructure PPPs; and (ii) the development and restructuring of the sector, as the project involves upgrading the airport facilities to increase capacity and improve the service quality offered to airlines and passengers.

The successful completion of the project is expected to demonstrate that well-structured PPPs in Greece will generate investor appetite and bring large-scale external investment into the Greek economy.

2 Guarantees

2.1 Can a company guarantee borrowings of one or more other members of its corporate group (see below for questions relating to fraudulent transfer/financial assistance)?

Under article 23A of codified Law no. 2190/1920 on *société anonymes* (the "**Company Law**"), parent companies and holding companies may guarantee the borrowings of one or more subsidiaries of its corporate group without any restrictions. This is also the case for corporate groups, whose financial statements are subject to consolidation (provided that the General Assembly of the shareholders of the legal entity/guarantor approves such guarantee by an increased majority). All other intragroup company guarantees (i.e. guarantees from subsidiaries to the parent company, guarantees between sister companies, etc.) are subject to the specific strict requirements set by the Company Law. Failure to comply with such requirements may result in the invalidity of such guarantee.

2.2 Are there enforceability or other concerns (such as director liability) if only a disproportionately small (or no) benefit to the guaranteeing/securing company can be shown?

As a general rule, corporate guarantees (both downstream and upstream) must serve the corporate purpose of the corporate guarantor. In case such condition is not met, the guarantee may be invalid and directors' liability may arise.

2.3 Is lack of corporate power an issue?

Lack of corporate power may arise only in respect of the service of the corporate purpose of the corporate guarantor.

2.4 Are any governmental or other consents or filings, or other formalities (such as shareholder approval), required?

In case of upstream guarantees between companies that are not subject to consolidation, according to the Company Law and Law no. 4308/2014 on Greek Accounting Principles, the following procedure must take place: the Board of Directors must submit to the General Assembly a report confirming satisfaction of the conditions for the lawful granting of the guarantee (such as the service of corporate interests and the right of recourse of the guarantor); such report must be approved by the General Assembly. Such decision must be recorded in the General Commercial Registry. Finally, the Board of Directors will decide on the specifics for providing the company guarantee.

2.5 Are net worth, solvency or similar limitations imposed on the amount of a guarantee?

There are no such limitations.

2.6 Are there any exchange control or similar obstacles to enforcement of a guarantee?

In general, no.

3 Collateral Security

3.1 What types of collateral are available to secure lending obligations?

Under Greek law, lending obligations are secured by securities *in personam* and/or by securities *in rem*. Securities *in personam* are mainly guarantees and securities *in rem* are mortgages (or prenotation of mortgages) and pledge over assets, rights and claims. Legislative degree 17.7.1923 on pledge over claims, in favour of credit institutions, provides that such pledge also gives entitlement to assignment for the collection of such claims. It should be noted that, in practice, most term loan facilities to Greek companies (in the form of *société anonymes*) are structured as bond loans, under Greek Law no. 3156/2003 (the "**Bond Loan Law**"); i.e. through the issuance of debt securities subscribed by private placement. This is because the Bond Loan Law provides for cost and tax exemptions (see our answer below under question 3.9).

3.2 Is it possible to give asset security by means of a general security agreement or is an agreement required in relation to each type of asset? Briefly, what is the procedure?

Asset security by means of a general security agreement is possible. Nevertheless, since each type of asset and each type of security is perfected by different procedures and registration requirements, a separate agreement is commonly used. As far as the procedure is concerned, see our answers below regarding different types of assets and different types of security.

3.3 Can collateral security be taken over real property (land), plant, machinery and equipment? Briefly, what is the procedure?

Security over real property (land) and plant is created by mortgage (by virtue of a notarial mortgage deed) or by mortgage prenotation (by virtue of a county court decision) and perfected by registration in the public books of the competent land registry or cadastre, where the land and plant are located. Prenotation of mortgage provides its beneficiary with the preemptive right to obtain a mortgage perfected as of the date of registration of the prenotation of mortgage, once its claim becomes final. Such security extends to all component parts and accessories of the real estate (i.e. machinery and equipment).

In respect only of machinery and equipment, security can be created by a non-possessory pledge agreement by virtue of article 1 of Law no. 2844/2000 and perfected by registration to the public book of Law no. 2844/2000 kept by the competent public registry where the borrower has its registered office.

3.4 Can collateral security be taken over receivables? Briefly, what is the procedure? Are debtors required to be notified of the security?

Security over receivables (trade receivables and insurance proceeds) is created by a private agreement and perfected by notification to the debtor of the relevant claims. In banking practice, such security is granted in the form of pledge and assignment of the receivables due to such pledge, by virtue of legislative degree 17.7.1923. Security over business receivables may also be granted under articles 11–15 of Law no. 2844/2000 and perfected by registration to the public book of Law no. 2844/2000 kept by the competent public registry where the borrower has its registered office (in addition to notification to the debtor).

Security may extend to future receivables, provided that they are specifically defined in the security agreement and fall within the scope of the pledge.

3.5 Can collateral security be taken over cash deposited in bank accounts? Briefly, what is the procedure?

Collateral security over cash deposited in bank accounts is created by a private agreement and perfected by notification to the bank holding such accounts. Standard practice provides for such collateral in cash to be governed by legislative degree 17.7.1923 and/or Law no. 3301/2004 on financial collateral agreements.

3.6 Can collateral security be taken over shares in companies incorporated in your jurisdiction? Are the shares in certificated form? Can such security validly be granted under a New York or English law governed document? Briefly, what is the procedure?

Unless otherwise provided by the Articles of Association of the company incorporated under Greek law, collateral security (pledge) over the company's shares is created by a private agreement and perfected by physical delivery of the shares to the pledgee or a third-party custodian. In case of registered shares, such collateral security (pledge) must also be notified to the company that has issued the pledged shares, notified to its shareholders/shares register and annotated on the pledged shares certificate.

Security over shares listed on the Athens Stock Exchange is created by private agreement and perfected by notification and registration to the Dematerialised Securities System, pursuant to the regulation of the Hellenic Central Securities Depositary.

Security may extend to new shares issued by the company and dividends or other benefits but not to preference rights of the shareholders, since such rights do not exist at the time the security agreement is perfected (under Greek law, preference rights of the shareholders are considered as rights of expectation and are created when the General Assembly decides on a share capital increase).

The law governing the pledge over shares issued by Greek companies is subject to the rule of *lex rei sitae*; i.e. the law of the place where the property is situated. Therefore, such security may only be governed by Greek law.

3.7 Can security be taken over inventory? Briefly, what is the procedure?

Security over inventory is governed by articles 16–18 of Law no. 2844/2000 (floating charge over inventory) and created by a private agreement. In order for such security to be perfected, the private agreement must be registered to the public book of Law no. 2844/2000, kept by the competent public registry where the borrower has its registered office.

3.8 Can a company grant a security interest in order to secure its obligations (i) as a borrower under a credit facility, and (ii) as a guarantor of the obligations of other borrowers and/or guarantors of obligations under a credit facility (see below for questions relating to the giving of guarantees and financial assistance)?

A company may grant security to secure its obligations both as a borrower under a credit facility and as a guarantor of the obligations of other borrowers and/or guarantors of obligations. Also refer to our answers to section 2 above regarding intragroup company guarantees.

3.9 What are the notarisation, registration, stamp duty and other fees (whether related to property value or otherwise) in relation to security over different types of assets?

Mortgages, prenotation of mortgages, non-possessory pledges and floating charges are subject to registration to the public books of the competent land registry and/or cadastre. Registration fees for the land registry amount to 0.775% of the secured amount. Registration fees for the cadastre amount to 0.875% of the secured amount.

In case of mortgages, notarial fees range from 0.2% to 1% of the secured amount. In case of prenotation of mortgages, court fees do not exceed €300.

Under the Bond Loan Law, registration fees are fixed at €100 per registration.

3.10 Do the filing, notification or registration requirements in relation to security over different types of assets involve a significant amount of time or expense?

The filing, notification and registration process usually does not involve a significant amount of time in order for it to be completed. However, the time needed may vary depending on the efficiency of the competent authority/registry office in each individual case. As for the expenses, please refer to question 3.9 above.

3.11 Are any regulatory or similar consents required with respect to the creation of security?

In principle, no consents are required.

3.12 If the borrowings to be secured are under a revolving credit facility, are there any special priority or other concerns?

No. Revolving credit facilities are secured by the same means and procedure described herein in section 3.

3.13 Are there particular documentary or execution requirements (notarisation, execution under power of attorney, counterparts, deeds)?

Please refer to our answers above.

4 Financial Assistance

4.1 Are there prohibitions or restrictions on the ability of a company to guarantee and/or give security to support borrowings incurred to finance or refinance the direct or indirect acquisition of: (a) shares of the company; (b) shares of any company which directly or indirectly owns shares in the company; or (c) shares in a sister subsidiary?

(a) Shares of the company

Under applicable law, that is, pursuant to the relevant provisions of article 16a of the Company Law, a company (other than a credit institution) is prohibited from making down payments, providing guarantees and/or loans to support borrowings incurred to finance the direct or indirect acquisition of its shares by third parties, unless the following conditions are met:

1. The aforementioned transactions are carried out under the responsibility of the Board of Directors (hereinafter referred to as "**BoD**") of the company at reasonable market conditions, in particular with respect to the interest received by the company and the guarantees it receives to secure its claims. Proper due diligence must be conducted regarding the solvency of the third party or, in the case of multilateral transactions, of each counterparty.
2. The General Assembly of the Shareholders (hereinafter referred to as "**GA**") of the company provides its prior consent by an increased quorum and majority. It is noted that the BoD submits to the GA a written report setting out the reasons which, in light of the company's best interests, justify the said transaction, its terms (including the price at which the third party will acquire the shares) as well as the risks that the contemplated transaction may pose to the liquidity and solvency of the company and the price. Please note that, in case the members of the BoD of the issuing or the parent company are directly or indirectly contracting parties to the respective transactions, an auditor's report must also be submitted to the GA.
3. The total financial assistance provided to third parties (or the total secured amount), which shall appear in the balance sheet as a non-distributable reserve, does not result in a reduction of the company's own funds to an amount lower than the aggregate amount of share capital and non-distributable reserves.

(b) Shares of any company which directly or indirectly owns shares in the company

Pursuant to the provisions of the same article 16a of the Company Law, the restrictions mentioned under (a) above also apply to down payments, guarantees and/or loans provided by subsidiaries for the acquisition of the parent company's shares by third parties.

(c) Shares in a sister subsidiary

The Company Law does not include provisions regulating the case in question.

5 Syndicated Lending/Agency/Trustee/Transfers

5.1 Will your jurisdiction recognise the role of an agent or trustee and allow the agent or trustee (rather than each lender acting separately) to enforce the loan documentation and collateral security and to apply the proceeds from the collateral to the claims of all the lenders?

Greek law does not recognise the notion of a security trustee. The role of the agent/trustee is provided only by the Bond Loan Law, under which any security granted by the borrower is granted in the name of the bondholders' agent, for the benefit of the bondholders. The bondholders' agent is responsible for enforcing loan documentation and collateral securities and applying the proceeds from the collateral to the claims of all the lenders *pro rata*, unless otherwise agreed.

5.2 If an agent or trustee is not recognised in your jurisdiction, is an alternative mechanism available to achieve the effect referred to above which would allow one party to enforce claims on behalf of all the lenders so that individual lenders do not need to enforce their security separately?

Since Greek law does not recognise the notion of a security trustee, an alternative mechanism to achieve such an effect is a contractual agreement between the lenders of a syndicated credit facility (*intercreditors' agreement*) providing that the collateral security is granted in the name of the security trustee, who is also a joint and several creditor with the other secured lenders. However, lenders are not protected in case of insolvency proceedings of the security agent.

5.3 Assume a loan is made to a company organised under the laws of your jurisdiction and guaranteed by a guarantor organised under the laws of your jurisdiction. If such loan is transferred by Lender A to Lender B, are there any special requirements necessary to make the loan and guarantee enforceable by Lender B?

The transfer of a loan from the initial lender to a successor lender or, to be more precise, the transfer of the relevant rights and obligations, is legally permitted in principle, subject to the specific provisions of each individual loan agreement. The procedure of such transfer of rights and obligations is regulated by the relevant provisions of the Greek Civil Code and is considered to be perfected, on the condition that the debtor and/or the guarantor is notified of the said transfer.

6 Withholding, Stamp and Other Taxes; Notarial and Other Costs

6.1 Are there any requirements to deduct or withhold tax from (a) interest payable on loans made to domestic or foreign lenders, or (b) the proceeds of a claim under a guarantee or the proceeds of enforcing security?

The current tax rate for tax withholding on interest from bond loans is 15%. Notably, interest payable on credit facilities concerning either domestic or foreign lenders is not subject to withholding tax. As for foreign lenders in particular, please refer to question 6.2 below.

6.2 What tax incentives or other incentives are provided preferentially to foreign lenders? What taxes apply to foreign lenders with respect to their loans, mortgages or other security documents, either for the purposes of effectiveness or registration?

Interest payments to lenders that are tax-resident outside of Greece and without a permanent establishment in Greece are subject to Greek withholding tax, currently at the rate of 15%, if not otherwise provided for in the tax treaty (if any) between Greece and the jurisdiction of tax-residence of the foreign lender.

6.3 Will any income of a foreign lender become taxable in your jurisdiction solely because of a loan to or guarantee and/or grant of security from a company in your jurisdiction?

No income of a foreign lender becomes taxable in Greece solely because of a loan to or guarantee and/or grant of security from a company in Greece.

6.4 Will there be any other significant costs which would be incurred by foreign lenders in the grant of such loan/guarantee/security, such as notarial fees, etc.?

An annual contribution of 0.6% is imposed on the average outstanding monthly balance of each loan granted by a bank to a Greek resident. Loans between banks, loans to the Greek State and loans funded by the EIB or by the EBRD are exempted from said contribution. As far as guarantees are concerned, there are no additional costs and fees. As for securities, please refer to question 3.9 above.

6.5 Are there any adverse consequences to a company that is a borrower (such as under thin capitalisation principles) if some or all of the lenders are organised under the laws of a jurisdiction other than your own? Please disregard withholding tax concerns for purposes of this question.

In case some or all of the lenders are organised under the laws of a jurisdiction other than Greece, there are no particular adverse effects for the borrower stemming from such a fact.

7 Judicial Enforcement

7.1 Will the courts in your jurisdiction recognise a governing law in a contract that is the law of another jurisdiction (a "foreign governing law")? Will courts in your jurisdiction enforce a contract that has a foreign governing law?

Under applicable law, that is, pursuant to the provisions of (a) Regulation EC 593/2008 "on the law applicable to contractual obligations (Rome I)" (which replaced the 1980 Rome Convention on the law applicable to contractual obligations, except as regards the territories of the Member States which fall within the territorial scope of that Convention and to which this Regulation does not apply pursuant to Article 299 of the Treaty), (b) the 1980 Rome Convention (to the extent that it was not replaced by Regulation EC 593/2008), and (c) the relevant articles of the Greek Civil Code (in the cases where (a) and (b) above do not apply), it can be concluded that, in principle, the parties to a contract are free to choose the law that shall govern their contract. However, there are certain limitations on this freedom of choice, concerning overriding mandatory provisions (i.e. provisions, the respect for which is regarded as crucial by the Hellenic Republic for safeguarding its public interests, such as its political, social or economic organisation, to such an extent that they are applicable to any situation falling within their scope, irrespective of the law otherwise applicable to the contract) as well as the Greek public order. Therefore, it can be concluded that, subject to the aforementioned limitations, Greek courts do recognise and enforce contracts that are subject to foreign governing law.

7.2 Will the courts in your jurisdiction recognise and enforce a judgment given against a company in New York courts or English courts (a "foreign judgment") without re-examination of the merits of the case?

Under applicable law, that is, pursuant to the provisions of (a) the relevant EU Regulations (e.g. Regulation EU 1215/2012 "on jurisdiction and the recognition and enforcement of judgments in civil and commercial matters" and Regulation EC 805/2004 "creating a European Enforcement Order for uncontested claims"), (b) bilateral international conventions, and (c) the relevant articles of the Greek Code of Civil Procedure, whichever applies in each case, it can be concluded that although in principle Greek courts will recognise and enforce a foreign judgment without re-examination of the case, such recognition and enforcement may be denied if any of the following applies: (a) the foreign judgment is not an enforceable title or *res judicata* according to the law of the foreign country where the judgment was issued; (b) it is issued by a foreign court not having jurisdiction as per Greek law; (c) the defendant was deprived of its rights to a fair trial; (d) the foreign judgment is irreconcilable with an earlier Greek judgment, which is *res judicata* and involves the same cause of action between the same parties; or (e) it violates Greek public order.

7.3 Assuming a company is in payment default under a loan agreement or a guarantee agreement and has no legal defence to payment, approximately how long would it take for a foreign lender to (a) assuming the answer to question 7.1 is yes, file a suit against the company in a court in your jurisdiction, obtain a judgment, and enforce the judgment against the assets of the company, and (b) assuming the answer to question 7.2 is yes, enforce a foreign judgment in a court in your jurisdiction against the assets of the company?

Pursuant to the provisions of Law no. 4335/2015, which entered into force on 01.01.2016 and constituted a significant reform of the Greek Code of Civil Procedure, particularly aiming to accelerate the dispensation of justice, strict timeframes were set regarding the procedural stages from filing a law suit in a Greek court to the issuance of a judgment of first degree (i.e. appealable, that is, not yet *res judicata*), resulting in shortening the aggregate time needed for the completion of the said judicial proceedings. In view of the above, as of now it is estimated that, in case of a law suit filed by a foreign lender in a Greek court and based on a contract governed by the Greek law, it might take on average <u>from twelve (12) to sixteen (16) months</u> for a judgment of first degree to be issued, whereas, in case of a payment order, this timeframe is reduced to approximately six (6) months. It should be noted that, in the case of contracts governed by foreign law, the aforementioned timeframes are expected to be significantly longer.

As far as the enforcement of a judgment (either Greek or foreign) is concerned, it can be said that the relevant procedure, which may involve seizure of the debtor's property and subsequently the auction of such property until the actual satisfaction of the lender, tends to be rather lengthy and may last on average up to <u>twelve (12) months</u>. It should also be noted that, in the case of a foreign judgment, the period required for its recognition by the Greek court may also prove to be considerable.

7.4 With respect to enforcing collateral security, are there any significant restrictions which may impact the timing and value of enforcement, such as (a) a requirement for a public auction, or (b) regulatory consents?

Under applicable law, that is, pursuant to the provisions of the relevant articles of the Greek Code of Civil Procedure, the individual stages of the enforcement procedure are described in detail and specific timeframes are set, within which enforcement proceedings shall be effectuated. As a general rule, in order for the enforcement procedure to commence, the creditor-beneficiary of the collateral security (i.e. the mortgagee/pledgee of mortgaged/pledged immovable/movable assets) must obtain an enforceable title (i.e. mainly non-appealable judgments, arbitral awards, payment orders, notarial deeds, etc.). Subsequently, as far as pecuniary claims are concerned, the enforcement procedure involves the following main stages: (a) the attachment of the debtor's assets; (b) the intervention of other creditors; (c) the liquidation of the attached assets through public auction; and (d) the distribution of proceeds. In particular, regarding the liquidation process, it is noted that liquidation is effected through a public sale procedure which is administered by a notary public. As to the distribution of proceeds from the public auction of a specific asset, it is noted that, in principle, the proceeds are distributed to all the creditors who participated in the liquidation process. In the case that the auction proceeds, after deducting the costs and expenses of the enforcement proceedings, are less than the total claims of the creditors, who participated in the respective proceedings, then they are proportionally distributed. However, certain categories of creditors have priority over the proportional distribution as follows: (a) claims provided with a general privilege (i.e. claims of the State and of other public entities, claims for wages and personal maintenance, etc.) have a minimum priority of 25% of the total proceeds; (b) claims provided with a special privilege, that is, secured claims (i.e. collateral security on the specific asset on which enforcement takes place) as well as claims regarding the maintenance of the property and the production and harvest of its fruits, have a minimum priority of 65% of the total proceeds; and (c) unsecured claims have a minimum priority of 10% of the total proceeds.

It should be noted that the legislative decree of 17.7.1923 introduces an exception to the aforementioned rule, according to which the liquidation of the attached assets is effectuated through public auction. More specifically, the legal effect of a pledge of claims under the provisions of the legislative decree of 17.7.1923 is that the pledgee-credit institution arguably acquires full ownership of the claim and is entitled to liquidate the claim, with the obligation to return to the pledgor-debtor any amount exceeding the secured claim.

Another exception to the above rule is introduced by Law no. 3301/2004 on financial collateral agreements, under which provisions the satisfaction of the pledgee-creditor is effectuated through sale, set off or application of the financial instruments and/or cash in discharge of the relevant obligations.

No regulatory consents are required.

7.5 Do restrictions apply to foreign lenders in the event of (a) filing suit against a company in your jurisdiction, or (b) foreclosure on collateral security?

No restrictions apply. However, it has been argued that foreign lenders do not enjoy the benefits of the legislative decree of 17.07.1923.

7.6 Do the bankruptcy, reorganisation or similar laws in your jurisdiction provide for any kind of moratorium on enforcement of lender claims? If so, does the moratorium apply to the enforcement of collateral security?

Pursuant to the provisions of Law no. 3588/2007 (i.e. the Greek Bankruptcy Code), in the case of declaration of bankruptcy, a suspension of all individual enforcement actions is imposed on all unsecured creditors and/or all priority creditors (i.e. creditors whose claims have a general privilege for satisfaction from the whole of the debtor's estate). As for the secured creditors (i.e. creditors whose claims are secured by special privilege or real security on a specific asset of the debtor's estate), they may undertake enforcement action against the specific secured asset, unless such secured assets are functionally and directly linked to the debtor's business. The aforementioned moratorium may last up to ten (10) months starting from the issuing date of the court decision which declares the bankruptcy. As far as pre-insolvency proceedings are concerned, under the relevant provisions of the Greek Bankruptcy Code, which provide for the conclusion of an agreement between the debtor and a certain percentage of its creditors (60% of the total claims including 40% of secured claims) (hereinafter referred to as the "Rehabilitation Agreement") and the subsequent ratification from the court of such agreement, from the filing of the Rehabilitation Agreement for ratification until the issuance of the decision of the Court, all individual and collective enforcement action is automatically suspended. This moratorium may not normally exceed four (4) months and may be extended, following application, for as long as the decision for ratification remains pending. It is also noted that the Rehabilitation Agreement may include more specific provisions concerning such moratorium.

7.7 Will the courts in your jurisdiction recognise and enforce an arbitral award given against the company without re-examination of the merits?

Under applicable law, that is, pursuant to the provisions of (a) the 1958 New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards, and (b) the relevant articles of the Greek Code of Civil Procedure, whichever applies in each case, it can be concluded that, in principle, Greek courts will recognise and enforce an arbitral award without re-examination of the case, subject to certain limitations, including, e.g., that the award has become binding on the parties, that it does not violate Greek public order, that the party against whom the award is invoked was able to present his case before the appointed arbitral authority, etc.

8 Bankruptcy Proceedings

8.1 How does a bankruptcy proceeding in respect of a company affect the ability of a lender to enforce its rights as a secured party over the collateral security?

As mentioned above under question 7.6, pursuant to the relevant provisions of the Greek Bankruptcy Code, in the case of declaration of bankruptcy, a moratorium on individual enforcement action is imposed on all unsecured creditors and/or all priority creditors, whereas the secured creditors (i.e. creditors whose claims are secured by special privilege or real security on a specific asset of the debtor's estate) may pursue their satisfaction solely by the liquidation of the specific secured asset, unless they waive their special privilege/security or such privilege/security proves to be insufficient for their complete satisfaction, in which case they are satisfied by the whole bankruptcy estate.

Moreover, please note that the Greek Bankruptcy Code provides that transactions carried out during the so-called "suspect period" (i.e. the period specified in the court decision declaring the bankruptcy, which may not precede the date of issuance of the said decision by more than two (2) years and during which it is assumed that the bankrupt debtor has discontinued its payments), including transactions concerning the establishment of *in rem* securities (including the pre-notation of mortgage) or provision of guarantees for pre-existing obligations, are subject to clawback, upon request of the bankruptcy administrator or a creditor, and thus rescinded and made null and void. It should also be noted that security agreements established by virtue of the provisions of Law no. 3301/2004 on financial collateral agreements are, in principle, not subject to the clawback provisions of the Greek Bankruptcy Code and generally remain unaffected by bankruptcy proceedings. The same holds true for the security agreements which were carried out pursuant to the provisions of the Rehabilitation Agreement, which is mentioned above under question 7.6.

8.2 Are there any preference periods, clawback rights or other preferential creditors' rights (e.g., tax debts, employees' claims) with respect to the security?

As mentioned above under question 8.1, pursuant to the relevant provisions of the Greek Bankruptcy Code, certain types of transactions, that is (a) donations or other transactions in which the consideration received by the bankrupt person or entity from its counterparty are disproportionately small in relation to its own obligations, (b) payments of non-outstanding debt, (c) non-cash payments of outstanding debts, or (d) establishment of *in rem* securities (including the pre-notation of mortgage) or provision of guarantees, for pre-existing obligations, if carried out during the "suspect period", are subject to clawback, upon request of the bankruptcy administrator or a creditor. Please note that the legal consequences of the clawback are that transactions in question are null and void and are rescinded. Further, transactions involving the bankrupt debtor and entered into during a period of five (5) years preceding the declaration of bankruptcy are subject to clawback if the bankrupt person has acted intentionally to damage its creditors or discriminate against some of them and the counterparty was aware of the bankrupt person's intention.

As far as the procedure regarding the liquidation of the bankrupt debtor's estate is concerned, it is noted that the liquidation proceeds in the context of the bankruptcy proceedings are distributed in accordance with the relevant provisions of the GCCP, which regulate the liquidation process in the context of the enforcement proceedings in general, and also the same system of privileges applies (for a detailed analysis regarding the distribution of proceeds under the provisions of GCCP, please refer to question 7.4).

8.3 Are there any entities that are excluded from bankruptcy proceedings and, if so, what is the applicable legislation?

Under applicable law, that is, pursuant to the relevant provisions of the Greek Bankruptcy Code, merchants (either individuals or legal entities), as well as associations with legal personality that pursue economic purposes, are subject to bankruptcy proceedings. Legal entities governed by public law, public authorities in general as well as local authorities are not subject to bankruptcy proceedings and cannot be declared bankrupt.

Please also note that there are separate laws providing and regulating a special liquidation process for certain categories of legal entities, that is: (a) Law no. 4261/2014 regarding credit institutions; (b) Law no. 4514/2018 regarding investment firms; and (c) Law no. 4364/2016 regarding insurance undertakings.

8.4 Are there any processes other than court proceedings that are available to a creditor to seize the assets of a company in an enforcement?

Please refer to question 7.4 above, where it is noted that, through the processes provided for by legislative decree of 17.7.1923, as well as by Law no. 3301/2004, the secured creditor/pledgee may satisfy the secured claims without having to necessarily resort to court proceedings and subsequently to the liquidation of the debtor's assets through public auction.

9 Jurisdiction and Waiver of Immunity

9.1 Is a party's submission to a foreign jurisdiction legally binding and enforceable under the laws of your jurisdiction?

Yes, a party's submission to a foreign jurisdiction is legally binding and enforceable under Greek law.

9.2 Is a party's waiver of sovereign immunity legally binding and enforceable under the laws of your jurisdiction?

Where no prevailing mandatory provisions apply, by virtue of which the right to sovereign immunity is under all circumstances and without exception awarded and/or recognised, a party's waiver of sovereign immunity is, in principle, legally binding and enforceable under Greek law.

10 Licensing

10.1 What are the licensing and other eligibility requirements in your jurisdiction for lenders to a company in your jurisdiction, if any? Are these licensing and eligibility requirements different for a "foreign" lender (i.e. a lender that is not located in your jurisdiction)? In connection with any such requirements, is a distinction made under the laws of your jurisdiction between a lender that is a bank *versus* a lender that is a non-bank? If there are such requirements in your jurisdiction, what are the consequences for a lender that has not satisfied such requirements but has nonetheless made a loan to a company in your jurisdiction? What are the licensing and other eligibility requirements in your jurisdiction for an agent under a syndicated facility for lenders to a company in your jurisdiction?

The main type of lenders to companies under Greek law are credit institutions, which are regulated by the provisions of Law no. 4261/2014 and are authorised and supervised by the Bank of Greece. There also exist venture capital companies under the provisions of article 5 of Law no. 2367/1995, which have as one of their objects the investment in bonds issued by Greek companies, as well as other licensed companies (e.g. investment firms), which in certain exceptional cases and for limited purposes are legally permitted to grant loans to their clients. Please note that Law no. 4261/2014 provides that, in case of non-EU credit institutions, a special authorisation by the Bank of Greece is required. Apart from the aforementioned lenders, Law no. 4261/2014 also provides that lending is permitted between members of the same corporate group. In addition to the above, please note that, by virtue of Law no. 4354/2015, a new legal framework for the management and transfer of claims from NPLs has been introduced into the Greek market, so as to help credit institutions clean up their balance sheets from non-performing, or so called "red", loans. Law no. 4354/2015 has also introduced two new types of companies into the Greek legal system, in relation to the management and transfer of claims arising from loans and credits, i.e.: (a) Loans Management Companies ("**L.M.C.s**"); and (b) Loans Transfer Companies ("**L.T.C.s**"), which may under certain conditions provide new loans to the debtors of such NPLs. As far as the licensing of said companies is concerned, please note that L.M.C.s must be granted a special operating licence by the Bank of Greece for the purpose of the NPLs' management. As for L.T.C.s, they are not required to obtain any operating licence from the Bank of Greece. However, if the L.T.C.s include loan/credit acquisitions within their scope of activity, they must enter into a loan management agreement with an L.M.C. which is properly licensed and supervised by the Bank of Greece.

Finally, in the case of a lender not appropriately authorised, that nonetheless makes a loan to a company, under Greek law, there are specified provisions for administrative sanctions, including but not limited to pecuniary ones (i.e. fines), which are imposed by the respective supervisory authority.

11 Other Matters

11.1 Are there any other material considerations which should be taken into account by lenders when participating in financings in your jurisdiction?

The lender should bear in mind that, although partially lifted, a broad range of capital controls still remain in place in Greece. Notably though, the capital controls framework is much more relaxed for inbound transfer of monies – such inbound monies are practically free of restrictions.

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sardelas liarikos petsa law firm

Sardelas Liarikos Petsa Law Firm has established a leading position in Greek legal services as a business law firm with a strong international dimension. The firm is well known in Greece and abroad for its top drawer specialised professional service in complex cross-border and domestic transactions, as well as commercial litigation. The firm is recognised by international legal directories and is considered by clients and peers alike as a legal practice with high expertise and experience, which creates innovative, practical and legally sage solutions in relation to complex transactions, some of which are considered to be innovative, not only by Greek, but also by international market standards. Its highest quality and innovative brand has been internationally recognised by experts and peers, as it is consistently recommended in prestigious legal directories, such as the *IFLR 1000*, *The Legal 500* and *Chambers & Partners*, while in 2009 it was selected for the IFLR Awards shortlist for the most innovative debt and equity-linked transaction in Europe.

Hong Kong


Richard Mazzochi


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1 Overview

1.1 What are the main trends/significant developments in the lending markets in your jurisdiction?

According to Thomson Reuters, syndicated loan volumes across Asia Pacific as a whole in 2017 declined 4.8% from 2016 to US$445.3 billion, continuing a slide from previous years. However, syndicated lending in Hong Kong remained strong, particularly in the area of acquisition financings. Acquisition financing volumes in Hong Kong were around US$4.9 billion, a significant increase on the US$625 million recorded in 2016. Overall loan volumes in Hong Kong reached US$116 billion, with substantial contributions coming from the Chinese technology sector. Of particular note was the US$13 billion borrowed by the Chinese internet giant, Tencent. Chinese M&A generally was down from the previous year, in large part caused by restrictions on outbound investment imposed by the PRC authorities. Notably, Chinese conglomerates that had been on aggressive acquisition sprees in recent years have been reined in, and in some cases have begun to dispose of their offshore investments. That said, Hong Kong has continued to position itself as a hub for One Belt One Road ("**OBOR**") financing, with market participants looking to benefit from Hong Kong's geographical proximity to the PRC and the territory's language skills and financing pedigree. The OBOR initiative is still in its growth stage and could have a marked impact on Hong Kong lending volumes going forward.

1.2 What are some significant lending transactions that have taken place in your jurisdiction in recent years?

One of the largest loans completed in Hong Kong was the US$3.6 billion loan for the privatisation of the shoe retailer, Belle International Holdings Limited. Ten banks (including the bookrunner) participated in this loan.

2 Guarantees

2.1 Can a company guarantee borrowings of one or more other members of its corporate group (see below for questions relating to fraudulent transfer/financial assistance)?

A company can give a guarantee or grant security over its assets in respect of the borrowings of another member of its corporate group.

2.2 Are there enforceability or other concerns (such as director liability) if only a disproportionately small (or no) benefit to the guaranteeing/securing company can be shown?

A director has a fiduciary duty towards the company and must act in its best interests. This applies when considering the giving of a guarantee or other security. If a director breaches its duty, then it may be personally liable towards the company.

The directors of the company will have to consider whether the giving of the guarantee will be in the best interests of the company and whether the company will benefit from the giving of such guarantee. It is important that the company itself, not only the group as a whole, will derive benefit from the giving of the guarantee. It is generally easier to establish that there is corporate benefit for a guarantor giving a downstream guarantee than a guarantor giving an upstream guarantee or a cross-stream guarantee.

2.3 Is lack of corporate power an issue?

Section 115 of the Companies Ordinance provides that a company has the capacity, rights, powers and privileges of a natural person of full age. If, however, the objects of a company are stated in its articles of association, the company must not do any act that it is not authorised to do by its articles of association. Also, if any power of a company is expressly modified or excluded by its articles of association, the company must not exercise any power contrary to such modification or exclusion.

2.4 Are any governmental or other consents or filings, or other formalities (such as shareholder approval), required?

No governmental approval, consent or registration is required.

In view of the issues raised in question 2.2 above, it is recommended that shareholder resolutions approving the giving of the guarantee are obtained where it secures the obligations of a parent or sister company.

2.5 Are net worth, solvency or similar limitations imposed on the amount of a guarantee?

These matters would not affect any limit on the amount of a guarantee. However, if a company is experiencing solvency issues, the matters referred to in question 8.2 should be borne in mind.

2.6 Are there any exchange control or similar obstacles to enforcement of a guarantee?

No, there are not.

3 Collateral Security

3.1 What types of collateral are available to secure lending obligations?

It is possible to take security over almost any type of asset in Hong Kong, whether tangible or intangible. This includes real estate, contractual rights and other receivables, securities, bank accounts, intellectual property, ships, aircraft and inventory.

3.2 Is it possible to give asset security by means of a general security agreement or is an agreement required in relation to each type of asset? Briefly, what is the procedure?

A company can execute a debenture (i.e. a single document containing a range of security provisions covering all assets). However, it is also possible to have individual security documents covering particular assets. Generally, the procedure would involve the due execution of the relevant document by the security provider, registration of the document where applicable, and other perfection steps that may be required depending on the type of security. For example, for an assignment of a contract, it is required to provide notice to the assignor's counterparty to perfect the security.

3.3 Can collateral security be taken over real property (land), plant, machinery and equipment? Briefly, what is the procedure?

It is possible to take security over land, and this is most commonly done by taking a legal charge over the property (commonly referred to as a mortgage). The mortgage should be in written form, executed as a deed and specified to be a statutory legal charge. On or before the execution of the mortgage, the mortgagor would have provided title deeds of the property to the mortgagee to facilitate the title investigation. Original title deeds will be retained by the mortgagee until the mortgage is released.

After the mortgage deed is executed, it should be registered with the Land Registry within one month of its execution in order to preserve the priority of the mortgagee against any interests in the land that may arise thereafter.

If the mortgagor/chargor is a Hong Kong incorporated company, or if it is a foreign company registered with the Companies Registry, then it would also be necessary to register the mortgage deed with the Companies Registry within one month of its execution in order to perfect the security.

It is possible to take security over plant, machinery and equipment in Hong Kong, and this would typically be done by a chargor granting a fixed or floating charge over those assets. A charge is a security interest over an asset that does not involve the transfer of ownership to the chargee. Generally speaking, a creditor will prefer to have a fixed charge because this will have a higher priority in the insolvency of the chargor as compared with a floating charge.

However, the nature of a fixed charge requires that the creditor maintain a high degree of control, and the courts may, regardless of whether the deed of charge describes a charge as a fixed charge, recharacterise such charge as a floating charge if it considers that this degree of control is not maintained.

Where a floating charge is used, the chargor is free to deal with the assets. If the chargor parts with ownership, then it will no longer be subject to the charge. The floating charge can crystallise and become a fixed charge if a specified crystallisation event (which would normally include an event of default) occurs.

For an effective charge over plant, machinery or equipment, there is no need to obtain any title documents, or notify any third party of the charge. Where the chargor is a company, it may be necessary to register the deed of charge with the Companies Registry, as in the case of a mortgage deed (please see above).

It is also possible to take a pledge or a lien over plant, machinery or equipment, but because these require physical possession, this is rarely done in a syndicated loan context.

3.4 Can collateral security be taken over receivables? Briefly, what is the procedure? Are debtors required to be notified of the security?

Security can be taken over receivables, and this is usually done by way of an assignment. A charge can also be used, in which case the same considerations referred to in question 3.3 above apply.

Where an assignment is taken, to be a legal assignment, it must comply with the requirements of the Law Amendment and Reform (Consolidation) Ordinance (Cap. 23), including that the assignment is absolute and over the assignor's entire legal interest, the assignment is in writing, the assignment is of a legal debt, and notice of the assignment is given to the contract counterparty. Where one or more of the above criteria is not met, the assignment may be an equitable assignment. This can still be effective security, and could be desirable where it is not practical to serve notice on each of the counterparties (which may be the case where there is a large number). On enforcement of the security, the creditor may wish to perfect the assignment by giving the notice, which will facilitate the collection of any claim, or the enforcement of the assigned rights by the creditor.

It is prudent for the creditor to have the underlying contract giving rise to the receivables reviewed to ensure that there is no prohibition on the assignment of the receivables. If so, then the assignment may not be effective, and it could cause the assignor to be in breach of its obligations under the contract, which could in turn create liabilities for the assignor or render the contract voidable. If an assignment is prohibited, then it may be possible to take security with a charge instead.

If the assignor is a company, the deed of assignment may be registrable with the Companies Registry (see question 3.3).

3.5 Can collateral security be taken over cash deposited in bank accounts? Briefly, what is the procedure?

A creditor will normally take an assignment or a fixed charge over a bank account in Hong Kong. To enhance the chances of having a fixed charge instead of a floating one, it is common to require that withdrawals from the account may only be made with the chargee's consent.

Typically, a notice of assignment or charge to the relevant bank is given at the outset, and the account bank is required to acknowledge the notice. In addition to perfecting the security, this would enhance the control of the creditor. For example, the notice may require the account bank to waive any rights of set-off that it may have, or instruct the account bank that after it is served with an enforcement notice, it should only follow the instructions of the creditor and not those of the assigning debtor.

3.6 Can collateral security be taken over shares in companies incorporated in your jurisdiction? Are the shares in certificated form? Can such security validly be granted under a New York or English law governed document? Briefly, what is the procedure?

It is possible to take security over shares. Where the shares are certificated, it is common to take a fixed charge over the shares. The chargee would normally require the delivery of the original share certificates, as well as various ancillary documents (such as share transfer forms, directors' resignation letters and written resolutions) to be executed in blank to facilitate enforcement. Otherwise, the procedural requirements are similar to those of other fixed charges.

It is possible for a creditor to take a legal mortgage. This would involve the shares being transferred to the creditor, who is then registered as the owner of the shares. This can be considered the strongest form of share security as it would be very difficult for the mortgagor to arrange to sell the shares to a third party without the consent of the creditor. However, this is not a common form of security as the creditor may not want to deal with any consolidation issues that arise if the company whose shares are charged becomes a subsidiary, and there may be stamping costs involved in the transfer.

For scripless shares, these are generally held in the clearing system, CCASS. In addition to taking a fixed charge over those shares, it would be possible to take an assignment in respect of the account at the broker in which such shares are held. The procedural requirements are substantially similar to those of taking security over a normal bank account. Where a significant proportion of shares in a listed company are the subject of the security, it may be necessary to make a notification to the stock exchange.

It is possible in principle to take security over shares with a New York or English law-governed document, but where the shares are located in Hong Kong, it is generally advisable to use a Hong Kong law-governed security document.

3.7 Can security be taken over inventory? Briefly, what is the procedure?

The forms of security that are available for the taking of security over inventory are broadly the same as those for taking security over plant, machinery and equipment as set out in question 3.3 above. Generally, a floating charge would be most appropriate as the chargor would expect to be able to freely sell the inventory without first having to obtain the consent of the chargee.

3.8 Can a company grant a security interest in order to secure its obligations (i) as a borrower under a credit facility, and (ii) as a guarantor of the obligations of other borrowers and/or guarantors of obligations under a credit facility (see below for questions relating to the giving of guarantees and financial assistance)?

Generally speaking, a Hong Kong company can do all of the above.

3.9 What are the notarisation, registration, stamp duty and other fees (whether related to property value or otherwise) in relation to security over different types of assets?

Notarisation is not required for the creation of security.

A registration fee of HK$340 is payable for each security agreement registered in the Companies Registry. Other registrations may be required against particular assets. Security over land should be registered in the Land Registry (which normally costs HK$210 to HK$450). Security over IP may be registrable in certain IP registers (for example, patents (costing HK$325) and registered trademarks (costing HK$800)).

Stamp duty is generally not payable on the creation of security, though it may be payable on the enforcement of such security. For example, on the transfer of land, and on the transfer of shares, stamp duty may be payable, with the rate depending on the amount of consideration provided.

3.10 Do the filing, notification or registration requirements in relation to security over different types of assets involve a significant amount of time or expense?

The above matters are not normally onerous, and should be straightforward provided they are commenced in good time. Notification requirements in respect of an assignment of contracts can be onerous when there are a large number of contracts being assigned.

3.11 Are any regulatory or similar consents required with respect to the creation of security?

No governmental approvals or consents are required.

3.12 If the borrowings to be secured are under a revolving credit facility, are there any special priority or other concerns?

No, though it is common practice for security documents to contain clauses to clarify that the security applies to any further advances granted under a loan facility.

3.13 Are there particular documentary or execution requirements (notarisation, execution under power of attorney, counterparts, deeds)?

Security over certain asset types are required to be documented in writing (see the above questions with respect to assignments, and mortgages over land). Furthermore, documents containing a power of attorney should also be executed by deed.

As a matter of common practice, security documents are executed as deeds to prevent the document from being invalid due to lack of consideration.

4 Financial Assistance

4.1 Are there prohibitions or restrictions on the ability of a company to guarantee and/or give security to support borrowings incurred to finance or refinance the direct or indirect acquisition of: (a) shares of the company; (b) shares of any company which directly or indirectly owns shares in the company; or (c) shares in a sister subsidiary?

(a) Shares of the company

If a person is acquiring or proposing to acquire shares in a company incorporated in Hong Kong, the company and any Hong Kong incorporated subsidiaries must not give any financial assistance directly or indirectly for the purpose of the acquisition before or at the same time as the acquisition takes place. Also, if a person has acquired shares in a company incorporated in Hong Kong, and any person has incurred a liability for the purpose of the acquisition, the company or any of its subsidiaries must not give financial assistance directly or indirectly for the purpose of reducing or discharging the liability. In other words, refinancing of loans made available for financing the acquisition is likely to be caught by this prohibition as well.

"Financial assistance" may take many forms and section 274 of the Companies Ordinance (Cap. 622) provides that it includes financial assistance given by way of "guarantee, security or indemnity". This usually prohibits the target company and its Hong Kong incorporated subsidiaries in an acquisition financing from giving guarantees and/or security to secure the facility financing the acquisition that is made available to the purchaser. Certain exceptions apply to this prohibition. This prohibition may also not apply if the company follows one of the three sets of relaxation procedures. The choice of which one to follow depends on the structure of the relevant transaction and timing requirements.

If a company unlawfully gives financial assistance, the validity of the financial assistance and of any transaction connected with it is not affected solely by reason of the contravention of the prohibition on the giving of the financial assistance. However, the company and its responsible persons may be the subject of criminal sanctions if it is found that the restrictions have been breached.

(b) Shares of any company which directly or indirectly owns shares in the company

Please see above.

(c) Shares in a sister subsidiary

The financial assistance prohibition does not apply where the shares acquired are only of a sister company.

5 Syndicated Lending/Agency/Trustee/Transfers

5.1 Will your jurisdiction recognise the role of an agent or trustee and allow the agent or trustee (rather than each lender acting separately) to enforce the loan documentation and collateral security and to apply the proceeds from the collateral to the claims of all the lenders?

Security agency and trust arrangements are recognised. In syndicated lending, security will typically be granted in favour of a bank acting as security trustee on behalf of all syndicate members from time to time. The existence of the trust means there is no need to grant separate security to each lender or to grant new security or make new security registrations each time there is a change in syndicate membership. The security trust provisions will provide that the security trustee (or a receiver appointed by it) is the only party entitled to enforce the security (acting on the instructions of the lenders).

5.2 If an agent or trustee is not recognised in your jurisdiction, is an alternative mechanism available to achieve the effect referred to above which would allow one party to enforce claims on behalf of all the lenders so that individual lenders do not need to enforce their security separately?

This is not applicable in Hong Kong.

5.3 Assume a loan is made to a company organised under the laws of your jurisdiction and guaranteed by a guarantor organised under the laws of your jurisdiction. If such loan is transferred by Lender A to Lender B, are there any special requirements necessary to make the loan and guarantee enforceable by Lender B?

The use of a security trustee to hold the benefit of the security and guarantee package on behalf of the syndicate (as described above) means that there are no notification or perfection requirements if membership of the syndicate changes from time to time. The security and guarantee package will continue to benefit the lenders, including new lenders joining the syndicate.

6 Withholding, Stamp and Other Taxes; Notarial and Other Costs

6.1 Are there any requirements to deduct or withhold tax from (a) interest payable on loans made to domestic or foreign lenders, or (b) the proceeds of a claim under a guarantee or the proceeds of enforcing security?

These are not applicable in Hong Kong.

6.2 What tax incentives or other incentives are provided preferentially to foreign lenders? What taxes apply to foreign lenders with respect to their loans, mortgages or other security documents, either for the purposes of effectiveness or registration?

No tax incentives exist that provide preferential treatment to foreign lenders, and no special taxes apply to foreign lenders in relation to the effectiveness or registration of security documents.

6.3 Will any income of a foreign lender become taxable in your jurisdiction solely because of a loan to or guarantee and/or grant of security from a company in your jurisdiction?

A foreign lender would not be subject to Hong Kong tax solely due to a single loan made to a Hong Kong company. However, if such lender is required to pay profits tax in Hong Kong by reason of its business generally, then it may be taxed on the profit made on the loan. Likewise, a foreign lender would not be subject to Hong Kong tax solely because it benefits from a guarantee or security from a Hong Kong grantor.

6.4 Will there be any other significant costs which would be incurred by foreign lenders in the grant of such loan/guarantee/security, such as notarial fees, etc.?

Please see section 3 above.

6.5 Are there any adverse consequences to a company that is a borrower (such as under thin capitalisation principles) if some or all of the lenders are organised under the laws of a jurisdiction other than your own? Please disregard withholding tax concerns for purposes of this question.

No, there are not.

7 Judicial Enforcement

7.1 Will the courts in your jurisdiction recognise a governing law in a contract that is the law of another jurisdiction (a "foreign governing law")? Will courts in your jurisdiction enforce a contract that has a foreign governing law?

Generally speaking, the Hong Kong courts will recognise a foreign governing law provided this would not be contrary to public policy in Hong Kong. The courts may apply Hong Kong law mandatorily in some circumstances, such as where the subject matter of the dispute relates to real property located in Hong Kong.

7.2 Will the courts in your jurisdiction recognise and enforce a judgment given against a company in New York courts or English courts (a "foreign judgment") without re-examination of the merits of the case?

The Hong Kong courts will generally enforce a final and conclusive foreign judgment without re-examination of the merits, subject to certain exceptions. These include where it would be contrary to public policy, where the foreign judgment was obtained by fraud, and where the judgment relates to foreign penal or revenue laws.

7.3 Assuming a company is in payment default under a loan agreement or a guarantee agreement and has no legal defence to payment, approximately how long would it take for a foreign lender to (a) assuming the answer to question 7.1 is yes, file a suit against the company in a court in your jurisdiction, obtain a judgment, and enforce the judgment against the assets of the company, and (b) assuming the answer to question 7.2 is yes, enforce a foreign judgment in a court in your jurisdiction against the assets of the company?

This will depend on the relative complexity of the facts of the case. If it is straightforward and the defendant does not mount a defence, then the creditor may be able to get default judgment within one month of the initiation of proceedings. If the defendant does mount a defence, then the creditor may be able to get summary judgment within three to nine months. Failing this, the time to get a judgment will depend very much on the facts of the case.

The time to complete an enforcement procedure depends on the procedure chosen, but it can be done in under two months. For foreign judgments, the enforcement process can be completed within four to six months, but it can be considerably longer depending on the circumstances.

7.4 With respect to enforcing collateral security, are there any significant restrictions which may impact the timing and value of enforcement, such as (a) a requirement for a public auction, or (b) regulatory consents?

In general, there are no strict requirements with respect to the timing or value of the enforcement procedure. Public auctions and (except for in the case of very limited classes of assets) regulatory consents would not be required. However, the creditor does have certain duties towards the provider of the security to obtain a reasonable price. In an enforcement situation, the creditor would generally appoint a receiver, have the asset valued independently, and consider holding an auction if appropriate.

7.5 Do restrictions apply to foreign lenders in the event of (a) filing suit against a company in your jurisdiction, or (b) foreclosure on collateral security?

No, they do not.

7.6 Do the bankruptcy, reorganisation or similar laws in your jurisdiction provide for any kind of moratorium on enforcement of lender claims? If so, does the moratorium apply to the enforcement of collateral security?

In a compulsory winding-up of the security provider, once a liquidator is appointed, no proceeding may be commenced against the company or its assets without the leave of the court. However, a creditor may appoint a receiver over the relevant assets, and the court would be expected to grant leave for such receiver to take possession of the assets.

Although rarely seen, where a scheme of arrangement in respect of a company has been agreed by the relevant classes of creditors, and been sanctioned by the court, a moratorium may be put into place in respect of such company's debts in accordance with the terms of the scheme of arrangement. Generally though, no moratorium will come into place until the scheme is effective.

7.7 Will the courts in your jurisdiction recognise and enforce an arbitral award given against the company without re-examination of the merits?

As Hong Kong is considered a party to the New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards (through accession by China), the Hong Kong courts would enforce an arbitral award without re-examination of the merits, assuming that the award was made in a country that was also party to the New York Convention. In such a case, the defendant would not be able to challenge the award on its merits.

8 Bankruptcy Proceedings

8.1 How does a bankruptcy proceeding in respect of a company affect the ability of a lender to enforce its rights as a secured party over the collateral security?

See question 7.6 above, and question 8.2 below.

8.2 Are there any preference periods, clawback rights or other preferential creditors' rights (e.g., tax debts, employees' claims) with respect to the security?

A transaction may be challenged under Section 265D of the Companies (Winding Up and Miscellaneous Provisions) Ordinance (the "**CWMO**") where a company which goes into liquidation had at a relevant time entered into a transaction with a person at an undervalue. Transactions at an undervalue can include transactions where the company received no consideration (e.g. gifts) or consideration of a value which is significantly less than the value of the consideration provided by the company. The relevant time is any time during the period of five years ending on the day on which the winding up of the company commences ("**Winding-Up Commencement Date**"), and where the company was unable to pay its debts or became unable to pay its debts as a result of that transaction.

Sections 266 of the CWMO may invalidate transactions relating to a company's property made at a relevant time if they are deemed to be "unfair preferences" and if the company is ultimately wound up. A company will be regarded as having given an unfair preference if (a) the company does anything or suffers anything to be done which has the effect of putting a person into a position which is better than the position such person would have been in if that thing had not been done, and (b) the company was unable to pay its debts or became unable to pay its debts as a result of giving that unfair preference.

The relevant time for an unfair preference means any time during the six-month period ending on the Winding-Up Commencement Day (or two years if the preference is given to a person connected with the company).

Unless an exception applies, section 267 of the CWMO will invalidate any floating charge given by a company at a relevant time if the company was unable to pay its debts at the time of the creation of the floating charge or became unable to pay its debts in consequence of the creation of the floating charge. The relevant time for this purpose means any time during the 12-month period ending on the Winding-Up Commencement Day (or two years if the floating charge is created in favour of person(s) connected with the company).

Upon insolvency, generally, the payment waterfall for creditors is as follows: first, creditors having the benefit of fixed charges and mortgages; second, the payment of liquidation costs (including realisation costs); and third, payments owed to preferential creditors. Payments to preferential creditors include wages, contributions to a mandatory provident fund, the return of deposits where the insolvent company is a bank and payments on insurance claims where the insolvent company is an insurance company. Any surplus remaining after all of these payments have been discharged will be paid to creditors secured by floating charges.

8.3 Are there any entities that are excluded from bankruptcy proceedings and, if so, what is the applicable legislation?

Unregistered companies (which includes foreign companies registered with the Companies Registry) may not be the subject of a voluntary liquidation procedure.

8.4 Are there any processes other than court proceedings that are available to a creditor to seize the assets of a company in an enforcement?

This can be possible, but only in very limited circumstances. A creditor or receiver would not generally be able take possession of an asset without a court procedure, especially where the asset is a physical one. However, there may be circumstances where the security arrangement was established in such a way that the involvement of a court is not required. For example, where a creditor has the benefit of the assignment of a bank account, the creditor may instruct the account bank to make payments to the order of the creditor instead of the assignor.

9 Jurisdiction and Waiver of Immunity

9.1 Is a party's submission to a foreign jurisdiction legally binding and enforceable under the laws of your jurisdiction?

Where the relevant contract provides that a foreign court will have exclusive jurisdiction, the courts of Hong Kong will generally give effect to such choice. However, there may be exceptions; for example where the Hong Kong court found that the choice of jurisdiction was illegal, not made in good faith, or contrary to public policy.

9.2 Is a party's waiver of sovereign immunity legally binding and enforceable under the laws of your jurisdiction?

The doctrine of absolute sovereign immunity applies in Hong Kong.

Waiver of sovereign immunity was considered in the cases of *Hua Tian Long (No 2)* and *FG Hemisphere Associates LLC v Democratic Republic of the Congo*. These cases suggest that if an obligor can establish to the satisfaction of the courts of Hong Kong that it is entitled to sovereign immunity, then any waiver of that immunity (in respect of jurisdiction, proceedings or execution) given by it in the relevant agreement may not be enforceable.

10 Licensing

10.1 What are the licensing and other eligibility requirements in your jurisdiction for lenders to a company in your jurisdiction, if any? Are these licensing and eligibility requirements different for a "foreign" lender (i.e. a lender that is not located in your jurisdiction)? In connection with any such requirements, is a distinction made under the laws of your jurisdiction between a lender that is a bank *versus* a lender that is a non-bank? If there are such requirements in your jurisdiction, what are the consequences for a lender that has not satisfied such requirements but has nonetheless made a loan to a company in your jurisdiction? What are the licensing and other eligibility requirements in your jurisdiction for an agent under a syndicated facility for lenders to a company in your jurisdiction?

Lending business in Hong Kong is governed by the Money Lenders Ordinance. This Ordinance requires every person who carries on business as a money lender to hold a money lender's licence. However, this Ordinance does not apply to authorised institutions (i.e. licensed banks, restricted licence banks and deposit-taking companies approved by the Hong Kong Monetary Authority) nor to loans made to such institutions, and in each such case no licensing under the Ordinance is required. The licensing requirement in this Ordinance does not apply to certain categories of loans (referred to in the Ordinance as "exempted loans", which include, without limitation, certain secured loans, intra-group lending and loans to employees) and certain categories of persons (referred to in the Ordinance as "exempted persons", which include, without limitation, certain types of financial institutions and insurance companies) making loans. The licensing requirements apply equally whether the lender is based in Hong Kong or overseas.

Any person who carries on a business as a money lender in contravention of the Money Lenders Ordinance is liable to a fine of up to HK$100,000 and imprisonment for up to two years. The lender may also be unable to enforce any relevant loan agreement.

There are no special licensing or eligibility requirements to become a facility agent in Hong Kong, though often a facility agent will be a bank that is an authorised institution.

11 Other Matters

11.1 Are there any other material considerations which should be taken into account by lenders when participating in financings in your jurisdiction?

Particular care should be taken when an individual person is providing a guarantee or other security. It is necessary to ensure that the person is properly identified, and that they are of age and sound mind. Furthermore, the Hong Kong Law Society has provided guidelines designed to mitigate the risk of undue influence. Depending on the facts of the case and whether the individual person has separate legal representation, it may be necessary to serve warning notices on them and have them sign confirmations before entering into the transaction documentation.

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Hungary


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1 Overview

1.1 What are the main trends/significant developments in the lending markets in your jurisdiction?

Lending activity, especially in the real estate sector, has been continuously increasing in the past few years in Hungary while interest rates have been decreasing. State-sponsored lending programmes still constitute a considerable part of the lending market.

1.2 What are some significant lending transactions that have taken place in your jurisdiction in recent years?

Financing of the new state-owned nuclear plant in Hungary has been by far the largest lending transaction in the past few years.

2 Guarantees

2.1 Can a company guarantee borrowings of one or more other members of its corporate group (see below for questions relating to fraudulent transfer/financial assistance)?

Yes. There are no specific restrictions on company guarantees.

2.2 Are there enforceability or other concerns (such as director liability) if only a disproportionately small (or no) benefit to the guaranteeing/securing company can be shown?

The enforceability of a guarantee does not depend on the benefit resulting from the fact of guaranteeing to the guarantor.

However, the collateral agreement may be challenged by the collateral provider on the grounds of significant disproportionality and, if successful, the collateral agreement may be held invalid and unenforceable by the court.

Moreover, within a period of one year from the starting date of the liquidation the creditors or the liquidator may challenge the collateral agreement concluded within three years preceding the filing of the liquidation claim if it constitutes gratuitous commitment burdening the debtor's assets.

In case the company goes into liquidation, creditors or the liquidator may file an action and request the court establishes the directors liable for not taking into consideration the creditors' interest and as a result caused the assets of the debtor company to decrease. The conclusion of a gratuitous or significantly disadvantageous collateral agreement (guarantee) may establish such liability.

2.3 Is lack of corporate power an issue?

Lack of corporate power may arise in case of state-owned companies, agencies or other public organs.

2.4 Are any governmental or other consents or filings, or other formalities (such as shareholder approval), required?

There is no governmental consent or filing requirement. The articles of association or other internal bylaws of the collateral provider may set forth a binding obligation regarding issuing guarantees or otherwise undertaking commitments.

2.5 Are net worth, solvency or similar limitations imposed on the amount of a guarantee?

There are no such restrictions. However, mandatory solvency requirements applicable to credit institutions may constitute a limit of issuance of bank guarantees.

2.6 Are there any exchange control or similar obstacles to enforcement of a guarantee?

There are no such obstacles.

3 Collateral Security

3.1 What types of collateral are available to secure lending obligations?

Collaterals over business shares

Charges over LLCs' quotas.

Security deposit over securities.

Charge over securities.

Collaterals over rights and receivables

Security deposit over bank accounts.

Charges over bank account receivables.

Charges over other receivables.

(Security) assignment of receivables.

Charge over IP rights and other rights eligible for registration in a public register.

Call options.

Collaterals over movables and immovable

Fixed charge over movable assets.

Asset pool charge (charge over assets not uniquely determined).

Real estate mortgage.

Call options.

Personal collaterals

Guarantees.

Suretyship.

3.2 Is it possible to give asset security by means of a general security agreement or is an agreement required in relation to each type of asset? Briefly, what is the procedure?

Usually separate collateral agreements are concluded with respect to each type of security. It is advisable to enter into separate agreements as the perfection (e.g. registration in public registers) and enforcement rules are different. Notwithstanding, the separate agreements may be incorporated in one public deed.

3.3 Can collateral security be taken over real property (land), plant, machinery and equipment? Briefly, what is the procedure?

Yes, security can be granted over such assets. A real property mortgage shall be established by a mortgage agreement and the registration with the competent land registry authority, the mere agreement is not sufficient. The parties may agree in the mortgage agreement that newly-built buildings or other permanent structures become subject to the mortgage without any further action.

Plant, machinery and equipment may be encumbranced by a mortgage agreement and registration with the relevant (public) registry. If the asset is registered with a specific register (e.g. vehicle or aircraft or ship) the charge shall be registered within. If there is no such specific registry, the mortgage created in the mortgage agreement is established by the registration into the Security Register held by the Hungarian Chamber of Civil Law Notaries.

3.4 Can collateral security be taken over receivables? Briefly, what is the procedure? Are debtors required to be notified of the security?

Yes, charge or security assignments may be established over receivables.

A charge over receivables is established by the mortgage agreement entered into by the security provider (holder of the receivable) and the secured creditor and the registration of the charge with the specific Security Registry held by the Hungarian Chamber of Civil Law Notaries. The notification of the debtor is not a perfection condition; however, it is advisable for the protection of the secured creditor's interests: as from such notification any amendment or termination on whatsoever ground of the agreement forming basis to the encumbered receivable enters into force only with the consent of the secured creditor. Until the debtor is notified of the charge, the debtor and the security provider are entitled to freely amend and/or terminate their agreement and thus deteriorate the charged receivable.

Receivables may be assigned by agreement of the security provider and the censured creditor. The notification and delivery instruction addressed to the debtor is necessary for the perfection of the assignment.

3.5 Can collateral security be taken over cash deposited in bank accounts? Briefly, what is the procedure?

Cash deposited in bank accounts may be charged as receivables or a security deposit may be established over such amounts.

Charge over a bank account is established by the agreement of the chargor and chargee and perfected by the registration of the bank account charge with the Security Registry held by the Hungarian Chamber of Civil Law Notaries Charge. There is no statutory obligation to notify the account holder's bank but it is advisable and customary. Charges over bank accounts may only be enforced in judicial enforcement procedures.

Security deposits over bank accounts are established by the agreement of the security provider (bank account holder), secured creditor and the bank. In case the secured creditor and the bank is the same, a mere bilateral charge agreement is sufficient. The security deposit agreement is perfected by the block of the bank account from the bank account holder who no longer has control over the account, only the secured creditor is entitled to instruct the bank to sweep the account in accordance with the stipulations of the security deposit agreement. In order to facilitate the business operation of the security provider, the parties may agree to a delayed perfection: blocking takes place only in the event of default. Security deposits may be enforced directly by the secured creditor without judicial enforcement actors (e.g., public notaries and bailiffs) being involved. In the event of default (or other cases set forth by the security deposit agreement) the secured creditor instructs the bank to debit the charged bank account (or the secured creditor bank itself sweeps the account).

A prompt collection right may also be granted with respect to the encumbered bank accounts. A prompt collection right does not grant a secured creditor position in a liquidation procedure compared to charges or security deposits which render their holder as a secured creditor if all requirements by law are met.

3.6 Can collateral security be taken over shares in companies incorporated in your jurisdiction? Are the shares in certificated form? Can such security validly be granted under a New York or English law governed document? Briefly, what is the procedure?

Security over business shares of companies limited by shares (share)

Security deposit may be established over shares. Unalienable shares (e.g. state-owned golden shares) cannot be burdened by charge or security deposit. The method of establishment depends on the form of shares.

Share certificates may be taken into security deposit by the agreement of the share holder and the secured creditor. In such case, the share certificates shall be handed over to the secured creditor or shall be deposited with a third party escrow agent. The handover of the shares perfects the security deposit, ascertaining that the shareholder has lost control over the share certificates and the creditor is the party having control over the encumbranced asset.

Dematerialised shares may be taken into security deposit by a tripartite agreement of the shareholder, the secured creditor and the security account holder. The account holders shall, under the agreement, block the dematerialised shares on the securities account or create a sub-account and transfer the encumbranced shares thereto. Such block or transfer is the perfection step depriving the shareholder-security provider from the control over the encumbranced dematerialised shares.

Shares may be charged or taken into security deposit under law other than Hungarian law provided for by the shares which are situated in the country of the governing law (the certificates in the country of the dematerialised shares are held in a securities account held by an account holder of the given jurisdiction).

Shares may be charged irrespective of being dematerialised of share certificates. Share certificates are charged by charge agreement entered into by the secured creditor and the shareholder. The share certificates stay with the shareholder. (In case they are handed over to the creditor the charge qualifies as security deposit regardless of the will of the parties.) Dematerialised shares are charged by a charge agreement (the securities account holder may also be a party thereto). The dematerialised shares will be held in a sub-securities account. The scope of control of the shareholder over the charged shares depends on the charge agreement.

Security over business shares of limited liability companies (quota)

Quotas may be charged by a charge agreement of the quotaholder and the secured creditor. The charge over quota shall be registered with the Companies' Registry. Quotas are not securities and a security deposit is not a type of encumbrance to which the quota may be subject to.

A quota charge agreement over the quota(s) of companies registered in Hungary shall be governed by Hungarian law.

3.7 Can security be taken over inventory? Briefly, what is the procedure?

The current Hungarian legal framework does not recognise floating charges. (It was an existing legal institution until March 15, 2014 and floating charges established prior to that date are still existing and registered with a special registry held by the Hungarian Chamber of Civil Law Notaries.) However, a charge may be established over a group of not uniquely defined assets, provided that the description of the group of assets is unambiguous (description, referring to type or quantity or any adequate determination of an inventory, e.g. balance sheet row numbers). Assets sold from the group are free of charge as from the transfer of the title. Newly-acquired assets falling into the group described in the charge agreement become charged as from their acquisition by the security provider. Such charge is established by a charge agreement of the security provider and the secured creditor and the charge is perfected by the registration into the Security Register held by the Hungarian Chamber of Civil law Notaries.

3.8 Can a company grant a security interest in order to secure its obligations (i) as a borrower under a credit facility, and (ii) as a guarantor of the obligations of other borrowers and/or guarantors of obligations under a credit facility (see below for questions relating to the giving of guarantees and financial assistance)?

Yes, a company may grant security interest both as a borrower and a guarantor for other companies' obligations.

3.9 What are the notarisation, registration, stamp duty and other fees (whether related to property value or otherwise) in relation to security over different types of assets?

Quota charges shall be registered with the Companies' Registry, the registration fee is approx. EUR 60. Registration fee of a real estate mortgage with the land registry is approx. EUR 40. Registration fee of one entry with the Security Register is approx. EUR 23 (payable per security interest).

The extent of the notary fee depends of the lengths of the collateral agreements, the number of counterparts and the value of the security interest.

Fees are payable at the time of filling of the registration documents.

3.10 Do the filing, notification or registration requirements in relation to security over different types of assets involve a significant amount of time or expense?

The registration with the Companies' Registry usually takes 2–3 weeks. registration with the Security Register can be effectuated immediately after the execution of the security documents. Land registry registration procedures usually last 2–3 weeks, but the statutory registration deadline is 30 days.

3.11 Are any regulatory or similar consents required with respect to the creation of security?

Security interests established over assets pertaining to regulated sectors or security interests providing collateral to regulated sector-related credit facilities may be subject to further rules set forth by the specific legal framework. Moreover, the deed of foundation or internal bylaws of the security provider company may also set forth consents or other requirement which need to be met for the creation of a valid and enforceable security interest.

3.12 If the borrowings to be secured are under a revolving credit facility, are there any special priority or other concerns?

There are no specific concerns regarding the collaterals with respect to the credit facility being a revolving one; however, special attention is to be paid to the wording of the security agreement thus ensuring that the security agreement provides collateral for all borrowings drawn down under the revolving CFA.

3.13 Are there particular documentary or execution requirements (notarisation, execution under power of attorney, counterparts, deeds)?

Real estate mortgage agreements shall be in a private deed countersigned by an attorney at law or in public deed, Real estate mortgage agreements lacking these formalities are not eligible for registration in the land registry albeit the obligation therein is valid. This is also applicable for any other security interest which needs registration with the land registry for perfection (typically call option on real estate).

Other security agreements may be incorporated in private deeds, but it is highly advised to incorporate all security agreements in a public deed since it allows direct enforceability. Security interests established in private deeds may only be enforced upon a court judgment which may take years to acquire.

4 Financial Assistance

4.1 Are there prohibitions or restrictions on the ability of a company to guarantee and/or give security to support borrowings incurred to finance or refinance the direct or indirect acquisition of: (a) shares of the company; (b) shares of any company which directly or indirectly owns shares in the company; or (c) shares in a sister subsidiary?

(a) Shares of the company

Financial assistance is restricted only in case of public companies limited by shares (companies limited by shares with shares listed on stock exchange). Such companies are entitled to provide financial assistance to any third person in respect of the acquisition of the given company if the following requirements are met:

(i) financial assistance is provided with arm's length terms;

(i) financial assistance is provided to the extent and on the account of the asset of the given company eligible for dividend payment; and

(iii) the general meeting of the shareholders of the company approved such financial assistance by at least ¾ majority based on the proposal of the board meeting filed also with the registration court. The proposal shall present the reason of the provision of financial assistance, risks, method and conditions of provision, consideration of the shares to be acquired, and benefits to be obtained by the company providing financial assistance.

(b) Shares of any company which directly or indirectly owns shares in the company

There are no restrictions in this respect.

(c) Shares in a sister subsidiary

There are no restrictions in this respect.

5 Syndicated Lending/Agency/Trustee/Transfers

5.1 Will your jurisdiction recognise the role of an agent or trustee and allow the agent or trustee (rather than each lender acting separately) to enforce the loan documentation and collateral security and to apply the proceeds from the collateral to the claims of all the lenders?

The legal institution known as "trust" in the English (or likewise) legal systems does not exist in Hungary, the Hungarian trustee is the sole owner of the trust and is obliged to act and manage the trust asset in favour of the beneficiary.

The notion of a (fiduciary) agent does not exist in Hungarian law. Notwithstanding, it is market practice to loan facility agreements setting forth such position, and agents act on behalf of secured creditors but no jurisprudence has been elaborated in this respect to date. Strict interpretation does not allow agents to act and proceed on behalf of other creditors solely on the basis of being appointed as agent in the loan facility agreement or the intercreditor agreement.

5.2 If an agent or trustee is not recognised in your jurisdiction, is an alternative mechanism available to achieve the effect referred to above which would allow one party to enforce claims on behalf of all the lenders so that individual lenders do not need to enforce their security separately?

The position of a security trustee is more or less covered by a recently introduced legal institution, the security agent (in Hungarian *zálogjogosulti bizományos*). The security agent may be appointed by the secured creditor(s). The appointment of the security agent is effective *vis-à-vis* third persons, including security providers as from the registration of the security agent as such into the relevant registry (land registry, Security Register or other relevant public register depending on the encumbranced asset). From its registration, the security agent is entitled to and bound by all and every right and obligation of the secured creditor and acts in its own name but on behalf of the secured creditor(s). It is therefore entitled to enforce the credit facility agreement and collateral agreements and proceed in accordance with the financing documents. It is to be noted that the security agent was introduced to the Hungarian legal framework in 2014 and no relevant and unified jurisprudence has been evolved.

In addition to that, the security agent is regulated only with respect to mortgage, charges and liens. Assignment and call options cannot be enforced by a security agent based on their quality of security agent. Specific authorisation may entitle the security agent to act on behalf of the secured creditors *vis-à-vis* debtors, but it is not allowed to proceed in a lawsuit in its own name on behalf of others.

5.3 Assume a loan is made to a company organised under the laws of your jurisdiction and guaranteed by a guarantor organised under the laws of your jurisdiction. If such loan is transferred by Lender A to Lender B, are there any special requirements necessary to make the loan and guarantee enforceable by Lender B?

Unless provided otherwise in the loan agreement, there is no specific requirements but notification of the debtor on the transfer. However, in case of portfolio transfers the consent of the National Bank of Hungary is required. If enforcement proceeding is to be started against the debtor, the legal succession shall first be declared prior to the commencement of the enforcement proceeding.

6 Withholding, Stamp and Other Taxes; Notarial and Other Costs

6.1 Are there any requirements to deduct or withhold tax from (a) interest payable on loans made to domestic or foreign lenders, or (b) the proceeds of a claim under a guarantee or the proceeds of enforcing security?

At present, there is no withhold tax or tax deduction in connection with interests payable on loans or proceeds of enforcing securities.

6.2 What tax incentives or other incentives are provided preferentially to foreign lenders? What taxes apply to foreign lenders with respect to their loans, mortgages or other security documents, either for the purposes of effectiveness or registration?

There are no tax incentives with regard to foreign lenders. In addition, loans, mortgages and other security documents are not taxable. It should be noted that the costs (e.g. stamp, notary fee) incurred in connection with the establishment of the security shall not be considered as tax (in this context please refer to question 3.9).

6.3 Will any income of a foreign lender become taxable in your jurisdiction solely because of a loan to or guarantee and/or grant of security from a company in your jurisdiction?

The income of the foreign lender will not become taxable solely on the grounds of granting a loan, guarantee or security. However, this does not affect the tax liability of the lender, if it shall be considered as a taxable person on the grounds of particular legislation (e.g. the Corporate Income Tax Act or Bank Tax).

6.4 Will there be any other significant costs which would be incurred by foreign lenders in the grant of such loan/guarantee/security, such as notarial fees, etc.?

Please refer to question 3.9.

6.5 Are there any adverse consequences to a company that is a borrower (such as under thin capitalisation principles) if some or all of the lenders are organised under the laws of a jurisdiction other than your own? Please disregard withholding tax concerns for purposes of this question.

No, there are not.

7 Judicial Enforcement

7.1 Will the courts in your jurisdiction recognise a governing law in a contract that is the law of another jurisdiction (a "foreign governing law")? Will courts in your jurisdiction enforce a contract that has a foreign governing law?

The Hungarian law recognises the freedom to choice over the applicable law; however, the conflict of law provisions stipulates the minimum standards: the choice shall be expressed and the existence and validity of the agreement on the governing law shall be determined by the law of the State which would govern the legal relationship.

There is no obstacle to enforce a contract under a foreign law if the contract meets the requirements of the governing law and the Hungarian courts have jurisdiction over the contract.

7.2 Will the courts in your jurisdiction recognise and enforce a judgment given against a company in New York courts or English courts (a "foreign judgment") without re-examination of the merits of the case?

We must make a clear distinction between judgments on the ground that the judgment was rendered by the court of an EU Member State or another State.

According to Regulation No. 1215/2012, a judgment given in a Member State shall be recognised in the other Member States without any special procedure. The enforcement may take various forms (please further refer to question 7.3 below); however, re-examination of the merits of the case is not required. We note that "BREXIT" may affect the judicial cooperation.

The situation is different in the case of a New York court judgment, because there is no international convention or reciprocity in respect of judicial enforcement between the Governments of Hungary and the United States. In this case the rules of Private International Law Act (conflict of law rules) shall be applicable as follows:

A judgment made by a foreign court shall be recognised if the jurisdiction of the foreign court is considered legitimate and the judgment is construed as final and non-appealable by the law of the State in which it was made, or equivalent.

The foreign judgment shall not be recognised if: **(i)** the decision may be contradictory to Hungarian public policy; **(ii)** the party against whom the decision was made did not attend the proceeding either in person or by proxy because the citation, petition, or other document on the basis of which the proceeding was initiated was not delivered at his place of residence or usual residence properly or in a timely fashion in order to allow adequate time to prepare his defence; **(iii)** proceedings arising from the same cause of action and between the same parties are commenced before Hungarian courts before the commencement of foreign proceedings (*pending at law*) or the Hungarian court has already made a final and non-appealable decision in an action arising from the same cause of action and between the same parties (*res judicata*); or **(iv)** the court of a foreign state, other than the State of the court that has already adopted a judgment in an action arising from the same cause of action and between the same parties, has made a final and non-appealable decision which met the requirements of recognition in Hungary.

7.3 Assuming a company is in payment default under a loan agreement or a guarantee agreement and has no legal defence to payment, approximately how long would it take for a foreign lender to (a) assuming the answer to question 7.1 is yes, file a suit against the company in a court in your jurisdiction, obtain a judgment, and enforce the judgment against the assets of the company, and (b) assuming the answer to question 7.2 is yes, enforce a foreign judgment in a court in your jurisdiction against the assets of the company?

(a) Court proceedings

An obvious reply cannot be provided, the length of the proceedings depend on the type of procedure and the circumstances of the individual case as well.

(b) Enforcement

EU judgment

Regulation No. 805/2004 introduced the European Enforcement Order. A judgment which has been certified as a European Enforcement Order in the Member State of origin shall be recognised and enforced in the other Member States without the need for a declaration of enforceability and without any possibility of opposing its recognition. A European Enforcement Order may only be issued if: **(i)** the claim is uncontested; **(ii)** the judgment is enforceable in the Member State of origin; **(iii)** the judgment does not conflict with Brussel I. Regulation; and **(iv)** the court proceedings in the Member State of origin meet the minimum requirements for uncontested claims procedures.

In the absence of a European Enforcement Order the rules of Regulation No. 1215/2012 shall prevail. According to the Regulation, a judgment given in a Member State which is enforceable in that Member State shall be enforceable in the other Member States without any declaration of enforceability being required. The procedure for the enforcement of judgments shall be governed by the law of the Member State addressed, under the same conditions as a judgment given in the Member State addressed. This procedure includes an additional step compared to the European Enforcement Order, where the court of the Member State addressed will issue a declaration of enforceability (without re-trial or re-examination).

Non-EU foreign judgment

Non-EU foreign judgment shall be enforced, if the judgment is in compliance with the provisions of Private International Law Act (please refer to question 7.2) and meets the requirements of the Judicial Enforcement Act. If the foreign judgment is in compliance with the requirements above, the court shall issue an enforcement certificate which confirms that it may be executed in accordance with Hungarian law the same way as a decision of a Hungarian court.

7.4 With respect to enforcing collateral security, are there any significant restrictions which may impact the timing and value of enforcement, such as (a) a requirement for a public auction, or (b) regulatory consents?

Judicial enforcement

Judicial enforcement is the primary way of enforcement in Hungary; however, the Judicial Enforcement Act and other relevant laws stipulate several legal instruments which may impact the timing and costs of enforcement.

Legal remedies: Debtors have several legal remedies in connection with the enforcement, which could lead to a long and expensive procedure. The debtor is entitled to: **(i)** propose the withdrawal of the enforceable document; **(ii)** submit demurrer of execution against the bailiff; or **(iii)** initiate litigation against the creditor. Unfortunately, these procedures are time-consuming and may result in additional costs as well.

Public auction: Unless otherwise provided by law, the bailiff shall organise a public auction which is the main method of recovery in judicial enforcement.

Regulatory consent: There is no such restriction in the Judicial Enforcement Act.

Out-of-court enforcement

Based on the Hungarian Civil Code, the lien holder is entitled to enforce its claims other than by judicial enforcement. The lien holder may exercise its rights through: **(i)** the sale of the pledged property by itself; **(ii)** the acquisition of the pledged property; or **(iii)** the enforcement of a pledged right or claim.

Out-of-court enforcement is less time consuming and the foreseeable costs are lower; however, if the lien holder infringes his obligations laid down in the Civil Code, the lienor, the designated lienor or any other person who has a legal interest therein may bring action requesting the court to suspend the exercise of the right to satisfaction, or to order the lien holder to exercise his right to satisfaction in accordance with the conditions stipulated by the court.

7.5 Do restrictions apply to foreign lenders in the event of (a) filing suit against a company in your jurisdiction, or (b) foreclosure on collateral security?

There are no general restrictions in respect of foreign lenders; however, the Hungarian courts may require lenders to pay security for costs in order to ensure the costs of the litigation. Foreign lenders with a registered seat in a Member State shall not be obliged to pay security for costs. It is also important that if the foreign lender does not have a registered seat in Hungary, or a proxy with residence or registered seat in Hungary, it shall be obliged to appoint a delivery agent.

7.6 Do the bankruptcy, reorganisation or similar laws in your jurisdiction provide for any kind of moratorium on enforcement of lender claims? If so, does the moratorium apply to the enforcement of collateral security?

Upon the request of the debtor the court may grant a temporary payment moratorium with immediate effect, provided that the bankruptcy petition has not been refused. If the court did not refuse the bankruptcy petition, it shall issue an order on the commencement of the bankruptcy proceeding which leads to a 120-day extension of the payment moratorium after the publication in the Company Gazette. The payment moratorium may be extended up to a maximum period of 240 days from the time of the commencement of the bankruptcy proceeding or exceptionally to 365 days. The payment moratorium allows the debtor to negotiate a bankruptcy settlement with its creditors while the payment obligations are temporarily suspended.

Under the duration of payment moratorium the enforcement of securities may not be ordered with the exception of security deposits that were established prior to the commencement of the bankruptcy proceeding.

7.7 Will the courts in your jurisdiction recognise and enforce an arbitral award given against the company without re-examination of the merits?

Having regard to the fact that Hungary is a contracting party to the New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards, the provisions of the Convention shall apply to the recognition and enforcement of arbitral awards. This means that an arbitral award made in the territory of another contracting state shall be recognised and enforced without re-examination of the merits of the case. Further requirements are that the arbitral award shall comply with Hungarian public policy.

8 Bankruptcy Proceedings

8.1 How does a bankruptcy proceeding in respect of a company affect the ability of a lender to enforce its rights as a secured party over the collateral security?

The Hungarian Bankruptcy Act governs two types of insolvency proceedings depending on the purpose of the procedure: bankruptcy proceedings; and liquidation proceedings.

Bankruptcy proceeding

As we mentioned above, the main purpose of the bankruptcy proceeding is to help the reorganisation of the debtor company by restructuring its debt in a settlement agreement. To that purpose, the enforcement of securities is suspended and the enforcement of such claims may not be ordered. Please note, if no settlement agreement can be concluded, the court must order the liquidation proceedings against the debtor company.

Liquidation proceeding

If the court declared the debtor insolvent and ordered liquidation proceedings, securities may be enforced only by the liquidator. This means that generally the secured lender shall not be entitled to enforce its rights over the securities directly; however, if the debtor provided a security deposit that was established prior to the commencement of the bankruptcy proceeding, the creditor shall be entitled to enforce this collateral.

8.2 Are there any preference periods, clawback rights or other preferential creditors' rights (e.g., tax debts, employees' claims) with respect to the security?

Bankruptcy proceeding

Transactions may be contested by the bankruptcy administrator, if the debtor has concluded a contract or made a legal statement in the absence of his approval. In this case, the bankruptcy administrator shall initiate proceedings for the recovery of any payments effected unlawfully or arising out of or in connection with any unlawful claim.

Liquidation proceeding

Transactions may be contested by the liquidator and the creditors in case of:

(i) contracts concluded by the insolvent company or other legal statements made by the insolvent company within five years preceding the date when the court received the petition for the commencement of the liquidation proceeding or thereafter, resulting in a decrease in the assets of the insolvent company, if intended to conceal the assets of the insolvent company or to defraud the creditors, and the other party had or should have had knowledge of such intent;

(ii) contracts concluded by the insolvent company or other legal statements made by the insolvent company within three years preceding the date when the court received the petition for the commencement of liquidation proceedings or thereafter, if the subject matter of the contract or the legal statement was the transfer of the assets of the insolvent company without any compensation or to undertake a commitment as an encumbrance to the insolvent company's assets without remuneration, or if the stipulated consideration constitutes unreasonable and extensive benefits to a third party;

(iii) contracts concluded by the insolvent company or other legal statements made by the insolvent company within 90 days preceding the date when the court received the petition for the commencement of liquidation proceeding or thereafter, if the subject matter of the contract or the legal statement was to give privileges to a creditor, such as the amendment of an existing contract to the benefit of a creditor, or to provide security to a creditor that does not have any; and

(iv) contracts concluded by the insolvent company or other legal statements made by the insolvent company within three years preceding the date when the court received the petition for the commencement of the liquidation proceeding or thereafter, if the subject matter of the contract or the legal statement was the transfer of ownership by way of guarantee, or the assignment of a right or claim by way of a guarantee or exercising an option right to buy, where the beneficiary exercised such acquired right by failing to settle toward the debtor, or did so improperly, and/or failed to pay the amount remaining after the secured claim is satisfied; if the right-holder did not have the acquisition of ownership, or the assignment of a right or claim by way of a guarantee registered in the collateral register, or his option right in the real estate register.

The liquidator – on behalf of the debtor – shall be entitled to reclaim, within the time limit referred to subparagraph (i)–(iv) above, any service the insolvent company has provided within a 60-day period preceding the date when the court received the petition for the commencement of the liquidation proceeding or thereafter, if it was provided to give privileges to any creditor and if such service is not usually provided under normal course of business.

The liquidator shall be entitled to terminate the contracts concluded by the debtor with immediate effect, or to rescind from the contract if neither of the parties rendered any services.

In addition to the above, any creditor or – on behalf of debtor – the liquidator may initiate action during the liquidation proceedings before the court against the former executives of the insolvent company on the ground that the executive failed to exercise their management functions in the interests of creditors within three years prior to the commencement of the liquidation proceeding.

8.3 Are there any entities that are excluded from bankruptcy proceedings and, if so, what is the applicable legislation?

The Hungarian Bankruptcy Act shall be applicable as regards the business associations; however, particular legislation may stipulate some exception from the general rule. Financial institutions, insurers, investment service providers, non-governmental organisations and local governments generally fall within the scope of the Hungarian Bankruptcy Act and particular provisions shall be applicable to their liquidation.

8.4 Are there any processes other than court proceedings that are available to a creditor to seize the assets of a company in an enforcement?

As a general rule, the Hungarian Bankruptcy Act stipulates that after the commencement of the liquidation proceeding securities may be enforced only by the liquidator, however there are a few exceptions:

(i) *Security deposit*: as we mentioned above, if the debtor provided a security deposit that was established prior to the commencement of the bankruptcy proceeding, the creditor shall be entitled to enforce this collateral directly.

(ii) *Set-off*: non-disputed claims can be set-off during the liquidation proceeding, if those have been registered by the liquidator and the claim has not been assigned following the commencement of the liquidation proceeding. Please note, the creditor – in the proceedings initiated by the insolvent company – may enforce his claim existing at the time of the commencement of liquidation proceeding against the debtor as a setoff claim, provided, however, that the beneficiary of the claim was the same creditor at the time of the commencement of liquidation proceedings as well.

(iii) *Option right*: the right holder is entitled to buy the assets by way of an unilateral statement after the commencement of the liquidation proceeding. Following the enforcement of option right, the right holder cannot exercise set-off against the debtor.

9 Jurisdiction and Waiver of Immunity

9.1 Is a party's submission to a foreign jurisdiction legally binding and enforceable under the laws of your jurisdiction?

Yes. According to the Private International Law Act, the parties are entitled to conclude a choice of court agreement that designates the courts of a State or one or more specific courts of a State for the purpose of deciding disputes which have arisen or may arise in connection with a particular action relating to property law.

9.2 Is a party's waiver of sovereign immunity legally binding and enforceable under the laws of your jurisdiction?

Yes; however, the Hungarian courts shall have no jurisdiction in: **(i)** proceedings pertaining to any right in real estate property situated abroad, including the rental or lease of such property; **(ii)** succession proceedings where the inheritance is located abroad and the testator is not a Hungarian citizen; **(iii)** actions filed for the destruction of official instruments or securities issued abroad; **(iv)** proceedings in connection with the granting and termination of industrial property rights abroad, including the contents thereof; **(v)** proceedings concerning the establishment and termination of a foreign-registered legal person, in proceedings concerning the validity of the contract or instrument of constitution underlying the registration of the legal person, and in proceedings concerning the review of the resolutions passed by the organs of legal persons; **(vi)** proceedings concerning the registration of rights, facts and data into a public register abroad; and **(vii)** actions concerning enforcement procedures abroad.

10 Licensing

10.1 What are the licensing and other eligibility requirements in your jurisdiction for lenders to a company in your jurisdiction, if any? Are these licensing and eligibility requirements different for a "foreign" lender (i.e. a lender that is not located in your jurisdiction)? In connection with any such requirements, is a distinction made under the laws of your jurisdiction between a lender that is a bank *versus* a lender that is a non-bank? If there are such requirements in your jurisdiction, what are the consequences for a lender that has not satisfied such requirements but has nonetheless made a loan to a company in your jurisdiction? What are the licensing and other eligibility requirements in your jurisdiction for an agent under a syndicated facility for lenders to a company in your jurisdiction?

It is a general rule that financial services (e.g. business like lending) may be carried out with the authorisation of the Hungarian National Bank (supervisory authority of the financial sector); however, the Hungarian legislation stipulates specific provisions in respect of foreign lenders as well.

A foreign lender may provide its financial services via branch office, at the same time it is important to note, that lenders with a registered seat in an EU Member State are entitled to provide cross-border services throughout the Community. It is also important that no licence is required if the lender has a registered seat in an EU Member State or OECD Member State which comply with the requirements of authorisation in Hungary.

The Hungarian legislation makes a clear distinction between lenders on the ground of its services. A lender that is a bank is entitled to provide each financial service stipulated by the relevant Hungarian legislation; on the other hand, a lender that is non-bank may provide limited financial services.

Please note that the supervisory authority is entitled to monitor the activity of the financial market and takes action against unauthorised financial providers. Within this framework, the supervisory authority may impose fines up to EUR 6,500,000.

11 Other Matters

11.1 Are there any other material considerations which should be taken into account by lenders when participating in financings in your jurisdiction?

There is no other material consideration to take in to account.

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BPSS Attorneys at Law

At BPSS Attorneys at Law we are committed to provide our clients with non-template-kind solutions of the highest level of expertise. BPSS guides its clients in the most complicated legal matters in Hungarian, English, German or French languages, including dispute resolution matters and various types of transactions. BPSS has established a strong presence in the Hungarian legal market of lending and finance, our partners having been involved in significant number of related transactions, both financing and work-out matters as well as in legal disputes held at ordinary and arbitration courts. BPSS's senior partner has been nominated as President of the Permanent Court of Arbitration attached to the Hungarian Chamber of Commerce and Industry as from January 1, 2018. One of our partners is listed in the roll of arbitrators in the Finance and Capital Market Section.

India

Anjan Dasgupta

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1 Overview

1.1 What are the main trends/significant developments in the lending markets in your jurisdiction?

Despite higher economic growth, the banking sector has been under tremendous stress due to sharp increase in non-performing assets ("**NPAs**"). Asset quality reviews conducted on banks have shown significant discrepancies in the reported levels of impairment and actual positions, leading to increasing levels of provisioning requirements. To address the issue of revitalising distressed assets and financial restructuring of large accounts, the Reserve Bank of India ("**RBI**") had introduced several restructuring schemes; however, none of the said schemes have yet achieved the desired results.

RBI Circular on Revised Restructuring Framework

The RBI recently vide its circular dated February 12, 2018 ("**RBI Circular**") has withdrawn most of the existing restructuring guidelines on stressed assets, which were issued by RBI previously, and tried to align the same with the current Bankruptcy Code regime.

As per the RBI Circular, resolution plans have to be implemented within a period of 180 (one hundred and eighty days) days from March 1, 2018 or the date of default (as the case may be) in respect of accounts with aggregate exposure of more than Rs. 20 billion. In case of failure to implement the resolution plan, the lenders are required to file an insolvency application under the Bankruptcy Code.

Banking Regulation (Amendment) Ordinance 2017

Pursuant to the Banking Regulation (Amendment) Ordinance 2017, RBI has issued two lists of total 40 (forty) large corporate defaulters, and directed the lenders to initiate insolvency proceeding against such defaulters, if resolution plan of such accounts are not implemented within the timelines specified by the RBI. We note that for most of these accounts corporate insolvency resolution process have now been initiated in the National Company Law Tribunal ("**NCLT**") under the Insolvency and Bankruptcy Code, 2016 ("**Bankruptcy Code**" or "**Code**").

Companies (Amendment) Act, 2017

Some provisions of the Companies Act, 2013 ("**Companies Act**") were amended pertaining to inter-corporate loans and corporate resolutions for borrowing but the same have not been notified yet.

Insolvency and Bankruptcy Code (Amendment) Act, 2017

The Indian Parliament passed the Bankruptcy Code, a comprehensive legislation dealing with the insolvency and bankruptcy resolution of companies, limited liability partnerships, partnership firms and individuals in a time bound manner. The Code aims to maximise asset value, revive business on a going concern basis while keeping the interest of all stakeholders.

The Code was recently amended *vide* the Insolvency and Bankruptcy Code (Amendment) Act, 2017 (effective from November 27, 2017), to state that defaulting promoters/investors (including their interested entities) would not be allowed to participate in the resolution bid process of the corporate debtor.

P2P Regulations

The RBI *vide* its master direction dated October 4, 2017 ("**P2P Directions**"), has regulated the peer-to-peer ("**P2P**") lending business in India. In accordance with the P2P Directions, a company which desires to carry on P2P business is compulsorily required to register themselves with the RBI as P2P Non-Banking Financial Company.

Enforcement of Real Estate (Regulations and Development) Act, 2016

A key recent development in the real estate financing sector is the enactment and notification of the Real Estate (Regulations and Development) Act, 2016 ("**RERA**"). RERA has been enacted with the aim to promote the real estate sector by ensuring transparency of information, accountability of real estate developers, completion of real estate projects in a time bound manner, protecting the investment of the investors, and establishing a specialised adjudicating authority. Under the RERA, contractual rights of the buyers/investors have been statutorily recognised. With the enforcement of the RERA, lenders in the real estate financing sector are now required to follow the relevant provisions of the RERA.

Amendment to the DRT Act and SARFAESI Act

The Enforcement of Security Interest and Recovery of Debts Laws and Miscellaneous Provisions (Amendment) Act, 2016, was also notified in August 2016. The amendment includes certain procedural changes to ensure stricter timelines for filing written statements, conclude proceedings, and filing written applications/statements in an electronic form. It also bringing debenture trustees within the ambit of the Recovery of Debts Due to Banks and Financial Institutions Act, 1993 ("**DRT Act**") and the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 ("**SARFAESI Act**"), allowing them to enforce security without court intervention and approach the tribunals under the DRT Act to recover unpaid debt. The Central Registry of Securitisation Asset Reconstruction and Security Interest of India ("**CERSAI**") was introduced and lenders are now required to mandatorily register the security created in their favour on the CERSAI within the timelines stipulated.

External Commercial Borrowings

The framework for external commercial borrowings ("**ECBs**") from overseas lenders also received a make-over with the introduction of fewer restrictions on end-uses, higher all-in cost ceilings, expansive listing of eligible lenders to include insurance companies, pension funds and sovereign wealth funds and permission for higher interest on long-term ECBs. To encourage investment in start-ups, the RBI has also permitted start-ups to raise up to USD 3 million in a financial year for a three-year tenure.

Amendment to the FPI Regulations

Foreign portfolio investors ("**FPIs**") have now been allowed to invest in defaulted bonds with a maturity of three years or more. FPIs have also now been allowed to invest in unlisted bonds subject to certain terms and conditions.

1.2 What are some significant lending transactions that have taken place in your jurisdiction in recent years?

The current banking and finance trends in India have seen significant lending by way of, *inter alia*, the following:

I. Corporate Bonds

Recently, numerous regulatory changes have been brought in, including the introduction of regulations to govern 'Masala Bonds' (Indian Rupee-denominated bonds issued to overseas investors), regulatory amendments to laws governing private and public placement of non-convertible debentures (listed and unlisted), amendments to laws pertaining to foreign currency borrowings and foreign currency convertible bonds. Some landmark issuances include India's first listed rupee denominated bonds by Pune Municipal Corporation and Hyderabad Municipal Corporation, and India's first listed offshore green rupee-denominated bonds by International Finance Corporation and the world's first listed 'Masala Bond' issuance by Housing Development Finance Corporation in July 2016. Other high-profile issuances included foreign currency convertible bond issuance by Videocon Industries, and listed non-convertible debenture issuances by Peninsula Land, Muthoot Finance Limited, and Indiabulls Housing Finance Limited.

II. Real Estate Financings

Real estate financing has gained momentum following the Central Government's aim to liberalise overseas investment in the Indian real estate sector, considering it is one of the largest employers in India. Real estate financing transactions include debt funding by banks, financial institutions and non-banking financial companies ("**NBFCs**") and equity financing by way of foreign direct investment (through mezzanine financing, structured equity instruments, etc.). The External Commercial Borrowings norms for affordable housing and enhancement of limits for listed non-convertible debentures has also helped to increase funding avenues for the real estate sector. Some significant debt funded real estate financing includes lease rental discounting loans by Deutsche Bank to, *inter alia*, Raheja Group, private equity investments by GIC Pte Ltd (Singapore), Blackstone Group, and Asian Development Bank's financial assistance to Bangalore Metro Rail.

III. Renewable Power Project Financings

There has been a considerable amount of financing in the renewable power (especially solar and wind power) sector. Numerous policy initiatives have increased the development of renewable power projects hence the increase in project financing for such projects.

Many banks and NBFCs, including financing arms of L&T, and government-owned banks and financial institutions such as State Bank of India, Power Finance Corporation Limited and Rural Electrification Corporation Limited have undertaken and continue to fund several renewable power projects across the country through unilateral and consortium financing.

IV. Restructurings and Stressed Asset Buyouts

Given the increase in stressed assets in the market, RBI has changed the regulations governing restructured debt financing and financing of companies in financial distress. Under these restructuring guidelines, some of the significant restructured financing deals include Essar Steel, Gammon India, Electrosteel Steels, Bhushan Steel, Jaypee and Monnet Ispat. Further, RBI has very recently, vide RBI Circular, withdrawn most of the existing restructuring guidelines on stressed assets, which were issued by RBI previously.

HSA Advocates has, in its capacity as lenders' legal counsel, advised in several banking and financing transactions under the abovementioned types of financings.

2 Guarantees

2.1 Can a company guarantee borrowings of one or more other members of its corporate group (see below for questions relating to fraudulent transfer/financial assistance)?

No company shall, directly or indirectly, give any security including a guarantee in connection with any loan taken by a director or any other person in whom the director is interested. However, a holding company can give guarantee or provide security in respect of loan availed:

- by its wholly-owned subsidiary company; or
- by its subsidiary company from any bank or financial institution, where such loan is to be used for the principal business activities of the company in whose favour guarantee or security is being provided.

However, the aforesaid restriction on giving of guarantee or security is not applicable to, amongst others, a government company, and a private company subject to the fulfilment of conditions stipulated in Companies Act. A private company can guarantee the borrowing of one or more members of its corporate group subject to the company providing a guarantee fulfilling the following conditions:

(a) no other body corporate has invested any money in share capital of such company;

(b) the borrowings of such company from banks, financial institution or any body corporate is less than twice of its paid-up share capital or 50 crore rupees, whichever is lower; and

(c) such a company has made no default in repayment of such borrowings subsisting at the time of making transactions under this section.

Recently, the Companies (Amendment) Act, 2017 ("**Companies Amendment Act**") has been enacted, wherein certain amendments have been proposed in relation to inter-corporate loans/guarantees/security. Though certain provisions of the Companies Amendment Act have been notified, the provisions pertaining to inter-corporate loans/guarantees/security are yet to see light of the day. Post such provisions becoming effective, a company can guarantee the borrowings of another entity or provide security (where any director of the guarantee issuing company is an interested party) provided prior consent of the members of the guarantee issuing company has been obtained *vide* a special resolution.

2.2 Are there enforceability or other concerns (such as director liability) if only a disproportionately small (or no) benefit to the guaranteeing/securing company can be shown?

In accordance with Section 127 of the Indian Contract Act, 1872, anything done, or any promise made, for the benefit of the principal debtor, may be a sufficient consideration to the guarantor for giving the guarantee.

2.3 Is lack of corporate power an issue?

The Companies Act stipulates that every company shall take consent of the directors present at the board meeting before giving any guarantee and providing security and in case any term loan is subsisting from public financial institutions, prior approval from such public financial institution shall be obtained (if any default in payment of interest or term loan is subsisting).

In addition to the above, prior approval of members by a special resolution passed at a general meeting of the company issuing such guarantee is required, in case such guarantee exceeds 60% of its paid-up share capital, free reserves plus amounts lying in the securities premium account or 100% of its free reserves plus amounts lying in the securities premium account, whichever is more ("**Limit**").

2.4 Are any governmental or other consents or filings, or other formalities (such as shareholder approval), required?

The following approvals, consents and filings are required in addition to compliance with conditions given under question 2.6 herein below:

(a) prior approval of members by a special resolution passed at a general meeting and filing of the same with the registrar of the companies (if the guarantee is beyond the Limit);

(b) prior approval from public financial institution in case of a subsisting loan (if any default in payment of interest or term loan is subsisting);

(c) to maintain a register which shall contain particulars of the guarantee given. The entries in the register (either manual or electronic) shall be authenticated by the company secretary of the company or by any other person authorised by the board for the purpose; and

(d) to disclose the details in the financial statement of the company.

2.5 Are net worth, solvency or similar limitations imposed on the amount of a guarantee?

No company:

(a) directly or indirectly, shall give any guarantee in connection with a loan to any other body corporate or person – exceeding the Limit – unless such guarantee is authorised by a special resolution passed in a general meeting of the shareholders of the company; or

(b) which is in default in the repayment of any deposits accepted before or after the commencement of the Companies Act or in payment of interest thereon, shall give any loan or any guarantee until such default is subsisting.

2.6 Are there any exchange control or similar obstacles to enforcement of a guarantee?

Yes, the Reserve Bank of India has stipulated controls on issuance and enforcement of a guarantee through various guidelines namely:

(a) Foreign Exchange Management (Permissible Capital Account Transaction) Regulations, 2000;

(b) Foreign Exchange Management (Guarantees) Regulation, 2000;

(c) Master Direction – External Commercial Borrowings, Trade Credit, Borrowing and Lending in Foreign Currency by Authorised Dealers and Persons other than Authorised Dealers ("**ECB Master Directions**"); and

(d) Foreign Exchange Management (Borrowing and Lending in Foreign Exchange) Regulations, 2000 ("**Borrowing and Lending Regulations**").

3 Collateral Security

3.1 What types of collateral are available to secure lending obligations?

A lending obligation may be secured by way of collateral security which may take the form of security over tangible and intangible property (whether movable and immovable both current and fixed), shares and other securities including convertible and non-convertible debt instruments, bank accounts, contractual rights (such as rights available to a borrower under its project documents), receivables and intellectual property (including goodwill, trademarks, copyrights). Any collateral security created shall be subject to applicable laws and the terms of the contractual arrangement between the lender and the borrower and any arrangement between the borrower and the counter parties to its project documents.

3.2 Is it possible to give asset security by means of a general security agreement or is an agreement required in relation to each type of asset? Briefly, what is the procedure?

It is possible to give asset security by way of a general security agreement; however, it is not prevalent in the market. Security over various types of collateral may be created as follows:

Security over immovable property, including leasehold rights over such properties, is required to be created by way of a mortgage. The law provides for creation of mortgage in several forms, of which simple mortgage, English mortgage and equitable mortgage are prevalent. Simple mortgage and English mortgage need to be executed in writing and should be compulsorily registered with the relevant sub-registrar of assurances and stamped as per applicable stamp laws. An equitable mortgage (also known as mortgage by deposit of title deeds) is created and perfected by depositing the title deeds of the immovable properties, with the lender/security trustee/agent. Parties generally decide on the form of mortgage, based on various considerations, including stamp duty implications in the state where the property is situated/where the security documents/title deeds are being executed/deposited. Some states have made registration of equitable mortgage mandatory. Security over movable property may be created by way of:

(a) A deed of pledge with a fixed or floating charge (depending on the contractual terms and commercial understanding of the parties) on shares and debentures or other securities. A pledge is perfected by actual or constructive delivery of the pledged assets to the lender and is often accompanied by a power of attorney executed by the pledger in favour of the pledgee, authorising the pledgee to, *inter alia*, transfer the pledged shares and exercise other rights and powers thereof, in the event of default.

(b) A hypothecation is a floating charge (without transfer of possession and as per the contractual terms and commercial understanding of the parties) on movables created pursuant to a deed of hypothecation and includes inventory and other trading stock. Charge by way of hypothecation is crystallised upon an event of default.

Companies are required to register charges/mortgage/pledge with the concerned registrar of companies as per the provisions of the Companies Act read with rules thereto, whereas banks and financial institutions are required to notify charges created in their favour to the CERSAI.

3.3 Can collateral security be taken over real property (land), plant, machinery and equipment? Briefly, what is the procedure?

Security can be created over movable and immovable properties (including leasehold rights) such as land, plant, machinery equipment. Simple mortgage, English mortgage and equitable mortgage are common forms of mortgage for taking security over immovable properties. Movable properties may be secured by means of a pledge or by hypothecation with a fixed or floating charge. The procedure has been briefly mentioned in question 3.2 above.

3.4 Can collateral security be taken over receivables? Briefly, what is the procedure? Are debtors required to be notified of the security?

Trade and other cash receivables (including receivables under insurance contracts) may be secured/charged in favour of a lender by a borrower by way of hypothecation, mortgage, or an assignment (depending on the terms of the lending transaction). Assignment is generally avoided due to stamp duty implications. Generally, notice of assignment of receivables in favour of the lender is required to be given to the debtors under the Factoring Regulation Act, 2011.

3.5 Can collateral security be taken over cash deposited in bank accounts? Briefly, what is the procedure?

Subject to the terms and conditions stipulated in the contract between the creditor and debtor, collateral security may be created over cash deposited in bank accounts as stated in question 3.4 above.

The general practice, in large lending transactions where security is envisaged over the borrower's cash deposits, is to create security over the cash deposits by a deed of hypothecation or create a charge over the accounts maintained with the account bank in which the borrower's cash deposits lie.

3.6 Can collateral security be taken over shares in companies incorporated in your jurisdiction? Are the shares in certificated form? Can such security validly be granted under a New York or English law governed document? Briefly, what is the procedure?

Collateral can be taken over shares by way of a pledge. The procedure for creation of a pledge is briefly stated in question 3.2 hereinabove. Shares may be in dematerialised or physical form. A pledge of shares entails constructive or actual delivery of the share certificates evidencing title thereto. A pledge over dematerialised shares may be created by following the process prescribed in the rules of the relevant depository together with the provisions of the Depositories Act, 1996 and the Securities and Exchange Board of India (Depositories and Participants) Regulations, 1996 (collectively "**Depositories Regulations**"). The pledgor's depository participant is required to notify the depository to block the pledged securities and prevent any transfer of the same until the charge is satisfied and the pledge is released by the pledgee by filing requisite forms and annexures as provided, *inter alia*, under the Depositories Regulations.

Pledge over shares can be validly created under English or New York law. However, for the pledge to be enforceable in India against the Indian company, it must be compliant with the provisions of Indian laws including the Code of Civil Procedure, 1908 ("**CPC**"), and the Depositories Regulations. However, general market practice does not include creating a pledge over shares of an Indian company, under foreign law.

Under Indian law, the execution of a foreign decree is governed by the provisions of Section 44A of the CPC unless it falls under any of the exceptions given under Section 13 of the CPC, which provides that a foreign judgment shall be conclusive as to any matter thereby directly adjudicated between the same parties or between parties under whom they or any of them claim litigating under the same title, except: (a) where the judgment has not been pronounced by a court of competent jurisdiction; (b) where it has not been given on the merits of the case; (c) where it appears on the face of the proceedings to be founded on an incorrect view of international law or a refusal to recognise the law of India in case where such law is applicable; (d) where the proceedings in which the judgment was obtained are opposed to natural justice, or the claim is founded on a breach of any law in force in India. Section 44A of the CPC provides that where a foreign judgment has been rendered by a superior court in a territory which the government of India ("**GOI**") has by notification recognised to be a "reciprocating territory", it may be enforced in India by proceedings in execution as if the judgment had been rendered by a relevant court in India.

A "reciprocating territory" is any country or territory outside India, which the GOI may, by notification in the official gazette, declare to be a reciprocating territory. The United Kingdom has been declared by the GOI to be a reciprocating territory for the purposes of Section 44A and a judgment by a high court or any superior court in the United Kingdom enforceable in Indian district courts provided it is brought in India within 3 (three) years from the date of the judgment. It is to be noted that the proper procedure for the creation and enforcement of a pledge as per Indian law will be required to be observed. It may be noted that Section 44A does not cover decrees in respect of taxes, fines, penalties or other charges of a similar nature.

The United States of America has not yet been declared a reciprocating territory, and any judgment by any courts therefrom may not be enforceable in India. Judgments of courts in the United States of America can be enforced only by filing a suit in an Indian court for a judgment based on the foreign judgment. The time limit to file such a law suit in India is within three years of the foreign judgment.

3.7 Can security be taken over inventory? Briefly, what is the procedure?

Security over inventory (movable property) is generally created by way of a deed of hypothecation in accordance with the procedure prescribed under question 3.2 above.

3.8 Can a company grant a security interest in order to secure its obligations (i) as a borrower under a credit facility, and (ii) as a guarantor of the obligations of other borrowers and/or guarantors of obligations under a credit facility (see below for questions relating to the giving of guarantees and financial assistance)?

Companies may grant security (i) in favour of their lender, subject to the provisions of the Companies Act, and (ii) as a guarantor, in favour of lenders of other borrowers and/or guarantors of obligations under credit facilities extended subject to the provisions of the Companies Act. For details please see our response to question 4.1. Companies are required to execute security documents by their key managerial personnel/directors and/or under a common seal if required and register the security with the concerned registrar of companies as per the provisions of the Companies Act. A company may also have to obtain the approval of its shareholders, consent/no objection of the income tax authorities and permission of the lessor (if required under the lease deed) before proceeding with the creation and perfection of a charge. Creation of a charge on immovable property or movable property not being stock-in-trade, requires the consent and confirmation of income-tax authorities to ensure that no proceedings are pending against the security provider or such assets under the Income Tax Act, 1961 ("**Income Tax Act**").

3.9 What are the notarisation, registration, stamp duty and other fees (whether related to property value or otherwise) in relation to security over different types of assets?

As stated in question 3.2 above, registered mortgage deed and mortgage by deposit of title deeds (in some states) is required to be registered with the concerned land registry. A deed of pledge or deed of hypothecation is not required to be registered, except with the concerned registrar of companies and with the CERSAI by the concerned lenders. Documents including power of attorney, declaration cum undertaking (affidavit), foreign documents and any other documents which may not be executed in the presence of a lender need to be notarised by a notary registered under the Notaries Act, 1952 and by paying minimal notary fees. Any security document including documents pertaining to mortgage, hypothecation and pledge attract stamp duty as per the rate prescribed by each State in India and may be fixed or *ad valorem*.

Stamp duty rates substantially vary from state to state and parties generally decide the place of execution of security documents based on location of the parties, ease of security enforcement and stamp duty implications. It is to be noted that if a document is stamped in one state but the original or copy of such document is brought into another state that has a higher stamp duty, the differential stamp duty applicable in the state into which the document has been brought, may need to be paid on such document. Registration and stamp duty requirements of all the above security documents have been provided under question 3.2 above.

3.10 Do the filing, notification or registration requirements in relation to security over different types of assets involve a significant amount of time or expense?

The law generally provides specific timelines within which a security document needs to be filed/registered with the registrar of companies, CERSAI or the land registry (in case of security over land) any other concerned regulatory authorities such as the Directorate General of Civil Aviation (in case of security over the aircrafts), the Registry of Ships in India (in case of security over the ships/vessels), the Trade Mark Registry (in case of security over the relevant intellectual property rights) and the Patent Office (in case of security over the patents), etc. The GOI, with an aim to forward its digital and green initiative, has begun to make e-filing mandatory for various corporate actions. Such filing, notifications or registration requirement does not involve significant amount of time and expenses.

3.11 Are any regulatory or similar consents required with respect to the creation of security?

Creation of security on property may require consents or approvals depending on the nature or use of the property. For example, in case of mortgage of a leasehold property, the mortgagor (also the lessee) may be required to take consent of the lessor. Similarly, in case of security on receivables arising out of a contract between borrower and a third party, consent of the third party may be required to be procured under the terms of such contract.

In addition to the above, the consent of income tax authorities is also required under Section 281(1)(ii) of the Income Tax Act, unless exempted therein.

3.12 If the borrowings to be secured are under a revolving credit facility, are there any special priority or other concerns?

A revolving credit facility is generally secured by hypothecation over current assets and movables (having a floating charge). There is no special priority for revolving credit facilities, subject to the contractual arrangement between the parties. Since a revolving credit facility may be withdrawn and re-drawn by the borrower any number of times (depending on the contractual terms), lenders need to ensure that the facility is adequately secured at all times. The lenders may also need to ensure regular monitoring of the secured assets through financial statements, physical inspection, stock statements and registers.

3.13 Are there particular documentary or execution requirements (notarisation, execution under power of attorney, counterparts, deeds)?

Kindly refer to our response to question 3.9.

4 Financial Assistance

4.1 Are there prohibitions or restrictions on the ability of a company to guarantee and/or give security to support borrowings incurred to finance or refinance the direct or indirect acquisition of: (a) shares of the company; (b) shares of any company which directly or indirectly owns shares in the company; or (c) shares in a sister subsidiary?

(a) Shares of the company

Section 67(1) of the Companies Act restricts a company limited by shares from directly or indirectly purchasing its own shares, without effecting a reduction in its share capital. Section 67(2) of the Companies Act restricts public limited companies and their subsidiaries from providing security, guarantees or any kind of financial assistance for the purchase of, or subscription by, any person of any shares in the company or its holding company, subject to exceptions provided under Section 67(3) of the Companies Act.

(b) Shares of any company which directly or indirectly owns shares in the company

In addition to our response under (a), Section 186 of the Companies Act allows a company to provide security or guarantee for a loan to a body corporate without its shareholders' approval, provided such loan does not exceed 60% of its total paid-up share capital, free reserves and securities premium account or 100% of its free reserves and securities premium account, whichever is more. However, companies need to ensure compliance with Section 185 of the Companies Act in relation to loans to directors, etc., if applicable. Further, financing of any acquisition of a holding company's shares is also restricted under Section 67(2) of the Companies Act.

(c) Shares in a sister subsidiary

As provided under (b) herein above, subject to compliance of Section 185 of the Act, Section 186 of the Companies Act lays down the law to be observed while giving security/guarantee by a company for a loan obtained by anybody corporate, for the aforesaid purposes, subject to the conditions laid down thereunder.

In addition to (a), (b) and (c) hereinabove, it is pertinent to note that as per the Banking Regulation Act, Indian banks are not allowed to provide financial assistance to companies for buy-back of their own securities. The RBI also places certain restrictions on Indian lenders funding companies' purchase of securities or investments in other corporates in concurrence with the Companies Act.

5 Syndicated Lending/Agency/Trustee/Transfers

5.1 Will your jurisdiction recognise the role of an agent or trustee and allow the agent or trustee (rather than each lender acting separately) to enforce the loan documentation and collateral security and to apply the proceeds from the collateral to the claims of all the lenders?

While trusts are governed by the Indian Trusts Act, 1882, the concept of agency is governed by Section 182 of the Indian Contract Act, 1872. In large consortium or multiple banking transactions, it is standard practice to appoint a trustee or an agent (lenders' agent or trustee) and create security in favour of such trustee or agent to enable it to enforce the security/loan documentation on behalf of the lender(s). The agent or trustee must be given adequate powers vide the trustee or agent appointment agreement to enable it to enforce the security on behalf of the lender(s) and apply the proceeds therefrom towards the claims of all the lender(s), in accordance with the trustee agreement or the *inter se* agreement ("**ISA**") between the lenders.

While the trustee or the agent has the technical or legal ownership of the assets, the lenders remain the ultimate beneficiaries. However, certain lending transactions such as issuance of secured debentures, make the appointment of a debenture trustee mandatory under the Companies Act.

5.2 If an agent or trustee is not recognised in your jurisdiction, is an alternative mechanism available to achieve the effect referred to above which would allow one party to enforce claims on behalf of all the lenders so that individual lenders do not need to enforce their security separately?

The mechanism of "trust" and "agent" is a well-recognised concept in India and may be carried out as provided in question 5.1 above.

Alternatively, lenders may also appoint any one of the lenders (usually the largest lender of the consortium) as a lead lender/lender's agent to hold the security on behalf of all the lenders and distribute the proceeds thereof among the lenders, in the ranking provided under the contractual terms.

5.3 Assume a loan is made to a company organised under the laws of your jurisdiction and guaranteed by a guarantor organised under the laws of your jurisdiction. If such loan is transferred by Lender A to Lender B, are there any special requirements necessary to make the loan and guarantee enforceable by Lender B?

Debt may be transferred by novation whereby all the rights, benefits and obligations under the loan documents are novated in favour of the new lender, or by way of an assignment where the existing lender assigns the whole or part of its rights under a loan in favour of the new lender. In case of a transfer of rights and obligations on the same commercial terms, Lender A may not need to procure consent of the borrower before transferring its loan to Lender B (subject to the contractual terms). However, if the commercial terms of Lender B differ from Lender A, the lenders will have to take consent of the borrower before proceeding with such transfer. Further, Lender A will also be required to release and return the guarantee executed in its favour so that a fresh guarantee may be executed in favour of Lender B. This process would involve additional costs (especially stamp duty on the guarantee and other accession/ novation documents). It may also be noted that as per the Master Circular – Loans and Advances – Statutory and Other Restrictions, issued by the RBI from time to time, the transferee bank must obtain necessary credit information of the borrower from the transferor bank before taking over an account/loan.

6 Withholding, Stamp and Other Taxes; Notarial and Other Costs

6.1 Are there any requirements to deduct or withhold tax from (a) interest payable on loans made to domestic or foreign lenders, or (b) the proceeds of a claim under a guarantee or the proceeds of enforcing security?

Withholding tax at the rate of 10% is applicable in case of payment of interest to loans from domestic lenders. Withholding tax is required to be deducted or withheld by a borrower in case the interest is to be paid to a foreign lender, as per the provisions of Section 194LC of the Income Tax Act. The present rate of withholding tax ranges from 5% to 20% under Section 194LC of the Income Tax Act (depending on the category of borrower). Withholding tax is determined by the finance acts and/or double taxation treaties with other countries and entities may avail the benefit of a lower tax rate if available thereunder. Withholding tax will also have to be deducted from the proceeds of a claim under a guarantee or from the enforcement of a security.

6.2 What tax incentives or other incentives are provided preferentially to foreign lenders? What taxes apply to foreign lenders with respect to their loans, mortgages or other security documents, either for the purposes of effectiveness or registration?

Tax and other incentives to foreign lenders will depend upon the nature of the lending transaction, the income from such transaction, the type of lender, as well as the type of borrowing entity and the country of origin. As stated in question 6.1 hereinabove, tax incentives and benefits, if any, may be availed of under any double taxation treaties executed with other countries. Taxes applicable to foreign lenders have been provided under question 6.1.

6.3 Will any income of a foreign lender become taxable in your jurisdiction solely because of a loan to or guarantee and/or grant of security from a company in your jurisdiction?

In addition to our response under question 6.1 hereinabove, it may be noted that mere grant of security from a domestic entity will not subject the foreign lender to tax implications.

6.4 Will there be any other significant costs which would be incurred by foreign lenders in the grant of such loan/guarantee/security, such as notarial fees, etc.?

Expenses pertaining to creation and perfection of security (generally borne by the borrower), include stamp duty and registration charges. Affidavits, powers of attorney and declarations (in the form of affidavits) need to be notarised for evidentiary value. However, notarial fees and registration fees (before the registrar of companies) are nominal. Stamp duty charges vary from state to state.

6.5 Are there any adverse consequences to a company that is a borrower (such as under thin capitalisation principles) if some or all of the lenders are organised under the laws of a jurisdiction other than your own? Please disregard withholding tax concerns for purposes of this question.

Foreign loans or credit facilities to an Indian borrower (external commercial borrowings or ECBs), are governed by the Foreign Exchange Management Act, 1999 ("**FEMA**") and rules and regulations made thereunder and also by the ECB Master Directions. As per the ECB Master Directions, a foreign equity lender is required to hold at least 25% of the equity of the domestic borrower to be an eligible foreign lender. Separately, the FEMA lays down certain restrictions on the remittance outside India, of enforcement proceeds of assets in India. Although the ECB Master Directions allow for remittances of principal, interest and other charges to foreign lenders, the ECB Master Directions lay down ceilings on the interest, fees, repayment and prepayment methods, and the amounts that can be raised vide ECBs, which need to be adhered to. Therefore, this may pose certain restrictions on the domestic borrower in terms of the amount of loans that it may avail, additional reporting requirements and end-use restrictions, etc.

The Income Tax Act does not recognise thin capitalisation principles.

7 Judicial Enforcement

7.1 Will the courts in your jurisdiction recognise a governing law in a contract that is the law of another jurisdiction (a "foreign governing law")? Will courts in your jurisdiction enforce a contract that has a foreign governing law?

In addition to our response given under question 3.6 above, a party's submission to a foreign jurisdiction is permitted under Indian law. Choice of law by parties is governed by the rules of Private International Law/Conflict of Laws ("**PIL Rules**"), which generally permit a contract to be governed by the legal system chosen by the parties to the contract. The choice of law must be express and should not be contrary to public policy. Indian courts may not oust the choice of a foreign law unless the parties show "good and sufficient reasons" or such choice results in "perpetuating injustice".

The courts in India recognise foreign governing law documents. To determine whether a foreign law has a substantial connection to the contract, courts generally examine the place of residence or business of the parties, the place where the relationship of the parties was centred, the place where the contract was made or performed, or the nature and subject matter of the contract. However, if the cause of action of a dispute arises in India or if the subject matter has no real bearing to the foreign jurisdiction and both parties being domestic entities have chosen the foreign jurisdiction with the intention of circumventing Indian laws, then Indian courts would have the jurisdiction over the contract/transaction under question and the choice of law may not be upheld by the courts. Generally, courts in India, subject to certain conditions, recognise and enforce a judgment obtained from a competent court in relation to enforcement of a contract that has a foreign governing law. Please refer to our response given under question 3.6.

7.2 Will the courts in your jurisdiction recognise and enforce a judgment given against a company in New York courts or English courts (a "foreign judgment") without re-examination of the merits of the case?

Please refer to our response to question 3.6.

7.3 Assuming a company is in payment default under a loan agreement or a guarantee agreement and has no legal defence to payment, approximately how long would it take for a foreign lender to (a) assuming the answer to question 7.1 is yes, file a suit against the company in a court in your jurisdiction, obtain a judgment, and enforce the judgment against the assets of the company, and (b) assuming the answer to question 7.2 is yes, enforce a foreign judgment in a court in your jurisdiction against the assets of the company?

In an event of a payment default under a guarantee or payment default by a borrower, foreign lenders may invoke the guarantee or enforce security by filing a suit against the guarantor/security provider before the concerned courts as per the provisions of the CPC.

(a) Proceedings as per the provisions of the CPC may take anywhere from three to five years depending on the specifics of the case and procedural delays.

(b) A foreign judgment (assuming it is of a reciprocating territory) will need to be filed before the concerned domestic courts and the procedure under Section 44A read, *inter alia*, with Section 13 of the CPC will need to be followed. Please refer to our response given under question 3.6.

7.4 With respect to enforcing collateral security, are there any significant restrictions which may impact the timing and value of enforcement, such as (a) a requirement for a public auction, or (b) regulatory consents?

Collateral security can be enforced in several ways depending upon the type of security. A creditor (whether a bank, financial institution or other creditor), in whose favour a security whether by way mortgage, charge or hypothecation has been created, may enforce its security by various methods available under law. In India, various legislative measures have been adopted from time to time to facilitate the recovery of dues by banks, financial institutions and other creditors. Debt recovery tribunal ("**DRTs**") and debt recovery appellate tribunals ("**DRATs**") have been established under the DRT Act, to smoothen the process of recovery of dues from partnerships and individuals. For recovery of dues from corporate debtors, one may now to approach the concerned NCLT as per the provisions of the Bankruptcy Code. The Code also gives a borrower the right to provide a proposal for restructuring itself, failing which the borrower is required to be liquidated as per the timelines set forth under the Code. The Code also gives priority to secured creditors and workmen's dues over government dues.

The Central Government has also notified the Companies (Transfer of Pending Proceedings) Rules, 2016, (as amended from time to time) wherein all proceedings (except voluntary winding up of the company where notice of the resolution by advertisement has been given under sub-section (1) of section 485 of the Companies Act, but the company has not been dissolved before the 1st day of April, 2017) relating to winding up and otherwise stand transferred to the NCLT as per the dates given under the said notification.

The SARFAESI Act gives banks and financial institutions power to enforce security without the intervention of courts. Banks, financial institutions and asset reconstruction companies have also been given special powers to not only take possession of a borrower's secured assets but also to dispose of such assets through public auction or private sale to recover their dues. The SARFAESI Act also provides banks and financial institutions with the power to approach the concerned Chief Metropolitan Magistrate, if the borrower fails to hand over possession of the secured assets. Further, on August 8, 2016, the Ministry of Finance, GOI notified 196 (one hundred and ninety-six) NBFC registered with the RBI as "financial institutions" under the SARFAESI Act, facilitating security enforcement by systemically important NBFCs. Changes have also been made to the SARFAESI Act and the DRT Act to include a debenture trustee (appointed for secured debt securities listed in accordance with applicable regulations issued by the Securities and Exchange Board of India) as a secured creditor.

Such changes have been carried out to ensure that lenders who are not specifically included under the SARFAESI Act or the DRT Act (such as funds, foreign portfolio investors and other investors in the corporate debt market) benefit from the provisions of these acts when acting through a debenture trustee in respect of listed debt securities.

Even though a lot more power has been given to lenders in recent years to enforce security and procure their dues, borrowers continue to use various tactics to delay the process of enforcement. Further, Rule 8 and 9 of the Security Interest (Enforcement) Rules, 2002 ("**Rules**") require a lender to provide a 30-day notice to the borrower, before undertaking the sale of any secured immovable property. The Supreme Court has also, on several occasions, held that unless 30 days' clear notice is given to the borrower, sale or transfer of secured property, by public sale cannot be effected under the SARFAESI Act. The Supreme Court has also held that if a sale which has been notified to the borrower falls through, the lender cannot effect the sale or transfer of such asset on a subsequent date without giving a fresh notice of sale to the borrower. It may be noted that Rule 8(8) of the Rules also provides for sale on private terms settled between the parties in writing.

It is also pertinent to note that Section 67 of the Transfer of Property Act, 1882 prohibits a mortgagee of "a railway, canal or other work in which the public are interested", from taking enforcement actions against such assets. In the event of default, the mortgagee can only recover earnings generated from such mortgaged assets.

7.5 Do restrictions apply to foreign lenders in the event of (a) filing suit against a company in your jurisdiction, or (b) foreclosure on collateral security?

Foreign lenders can enforce their rights over assets secured for their benefit, subject to the guidelines prescribed by the RBI. However, they do not enjoy the same rights available to domestic secured creditors under the SARFAESI Act. Regulated foreign banks, bilateral or multilateral financial institutions and other eligible ECB lenders still need to undergo traditional court proceedings by filing a civil suit to recover their dues. Except the Asian Development Bank and International Finance Corporation, no other bank or financial institution or secured creditor has recourse to SARFAESI Act, for recovery of their dues. Foreign lenders also do not have the right to approach DRTs or DRATs established under the DRT Act for recovery of dues from partnerships and individuals. However, foreign lenders may now approach the NCLT as per the provisions of the Bankruptcy Code to institute necessary resolution or winding up proceedings.

In respect of foreclosure of collateral, on any enforcement/invocation of charge over an immovable asset or over movables, and subsequent sale, such assets may be sold only to a resident Indian as per applicable regulations issued under FEMA. Further, the sale proceeds may be remitted overseas to the ECB lender, subject to withholding tax. In case of invocation of a pledge, one needs to ensure that the transfer is made in accordance with the extant RBI and FEMA regulations governing the issuance and transfer of securities to and by foreign lenders.

7.6 Do the bankruptcy, reorganisation or similar laws in your jurisdiction provide for any kind of moratorium on enforcement of lender claims? If so, does the moratorium apply to the enforcement of collateral security?

An insolvency process for corporate debtors is initiated under the Bankruptcy Code. The Bankruptcy Code envisages a two-step action to resolve a potentially insolvent or bankrupt entity. The first step is the insolvency resolution process, during which creditors assess whether the debtor's business is viable to continue the process of revival. Liquidation is then undertaken in the event the process of resolution fails. A financial or operational creditor may approach the NCLT or DRT (for partnerships and individuals) for initiating the insolvency resolution process against a debtor for any unpaid debts. The NCLT provides for a moratorium for the period of the resolution process. During this moratorium period no judicial proceedings for recovery (including an action by lenders for security enforcement under the SARFAESI Act), enforcement of security interest, sale or transfer of assets, or termination of essential contracts may take place against the debtor. A resolution professional is appointed to oversee the resolution process and operates under the directions of the committee of creditors which considers revival and rescue proposals for the debtor. The resolution plan must be decided within 180 days from the date of admission of the application for resolution (subject to a one-time extension of 90 days after the expiry of 180 days).

7.7 Will the courts in your jurisdiction recognise and enforce an arbitral award given against the company without re-examination of the merits?

The law relating to domestic and international arbitration and all matters connected therewith and incidental thereto is set out in the Arbitration and Conciliation Act, 1996 ("**Arbitration Act**"). Enforcement of domestic arbitral awards are governed by the provisions of Sections 34 to 36 of the Arbitration Act, whereas foreign arbitral awards are subject to conditions set out under Sections 44 to 60. An arbitral award given against the company shall be enforced by the courts in accordance with the provisions of the CPC, without going into the merits of the award and subject to any challenge to the arbitral award, the same will be enforceable as a decree and in such a situation, the principles of res judicata would apply and the arbitral award shall be final and binding on the parties and persons claiming under them respectively.

8 Bankruptcy Proceedings

8.1 How does a bankruptcy proceeding in respect of a company affect the ability of a lender to enforce its rights as a secured party over the collateral security?

Laws governing bankruptcy and winding-up proceedings of companies, has been considerably overhauled in the last one year, especially pursuant to the enactment of Bankruptcy Code. However, pending winding up proceedings will continue to be governed by the provisions of the Companies Act and any winding up proceedings instituted after the enactment and notification of the Bankruptcy Code shall be governed by the Bankruptcy Code. On December 7, 2016, the Ministry of Corporate Affairs issued a notification stating that all pending winding-up petitions filed under Section 433(e) of the Companies Act, 1956, before the concerned high courts, pending admission and which have been not been served on the respondent as required under Rule 26 of the Companies (Court) Rules, 1959 shall stand transferred to the NCLT. Under the Companies Act a secured creditor had a right to stand outside the winding up/liquidation proceedings and independently enforce the security subject to the condition that the sale proceeds are distributed in accordance with the provisions of Section 326 of the Companies Act thereto.

When a secured creditor enforces its security under the SARFAESI Act in respect of a company in liquidation, he is entitled to retain the sale proceeds of the secured assets after depositing workmen's dues with the liquidator. As per the Bankruptcy Code, a secured creditor can realise its security by standing outside a debtor's winding up/ liquidation proceedings and can appropriate the sale proceeds towards its dues. However, during the moratorium process as given under question 7.6 above, no enforcement procedures may be initiated (including an action by lenders for security enforcement under SARFAESI Act) against the assets of the company under liquidation. Where the security enforcement yields an amount exceeding the debts due to the creditor, the secured creditor shall account to the liquidator for such surplus. The Bankruptcy Code has considerably changed the priority of distribution of liquidation proceeds. The costs of insolvency resolution (including any interim finance), followed by secured debt together with workmen dues for the preceding two years, rank highest in priority of distribution payments. Central and state government dues stand below the claims of secured creditors, workmen dues, employee dues and other unsecured financial creditors.

8.2 Are there any preference periods, clawback rights or other preferential creditors' rights (e.g., tax debts, employees' claims) with respect to the security?

As stated above under question 8.1, the Bankruptcy Code has considerably changed the priority of distribution of payments to workers, employees, secured creditors, etc. The Bankruptcy Code mandates that workmen's dues for two years and employees' dues for one year, preceding the liquidation commencement date, and government dues including taxes, etc. for two years preceding the liquidation commencement date, fall within the category of preferential payment and are entitled to priority as per the distribution mechanism provided under Section 53 of the Bankruptcy Code.

As concerns clawback rights, certain provisions of the Bankruptcy Code, including Sections 45 to 49, provide the liquidator or creditor to make an application for avoidance of undervalued transactions which a borrower may have undertaken to keep the assets beyond the reach of any claimant, provided the conditions specified under the relevant Sections are fulfilled. A liquidator or resolution professional also has the power to apply for the avoidance of extortionate credit transactions involving the receipt of financial or operational debt by the borrower, in the two years preceding the commencement of insolvency proceedings in compliance with Section 50 of the Bankruptcy Code.

8.3 Are there any entities that are excluded from bankruptcy proceedings and, if so, what is the applicable legislation?

Any company registered under the Companies Act, 1956 or Companies Act, 2013 can be the subject of bankruptcy proceedings. The Code has expanded the scope beyond companies to cover limited liability partnerships, partnership firms and individuals. The GOI has also proposed the Financial Resolution and Deposit Insurance Bill, 2017, to, *inter alia*, carry out the resolution of certain categories of distressed financial service providers and to provide deposit insurance to consumers of certain categories of financial services. As of today, financial service providers are excluded from bankruptcy proceedings under the Code.

8.4 Are there any processes other than court proceedings that are available to a creditor to seize the assets of a company in an enforcement?

Lenders may try and restructure the borrower's debts through the restructuring of the loan accounts of the company (which may include provisions for additional collaterals, etc.) in accordance with the prevailing restructuring guidelines issued by RBI. Such restructuring may also include change in ownership of the company by the new investors, provided the new investor is not disqualified under Section 29A of the Bankruptcy Code.

Banks and financial institutions including asset reconstruction companies have the power to take possession of a company's secured assets without the intervention of the courts, by following the procedure laid down under the SARFAESI Act Secured creditors having registered mortgage as a security on the borrower's immovable property, also have the right to enforce such security without the intervention of courts, pursuant to Section 69 of the Transfer of Property Act, 1882.

9 Jurisdiction and Waiver of Immunity

9.1 Is a party's submission to a foreign jurisdiction legally binding and enforceable under the laws of your jurisdiction?

Please refer to our response to questions 3.6 and 7.1.

9.2 Is a party's waiver of sovereign immunity legally binding and enforceable under the laws of your jurisdiction?

A party's right to waive its immunity is recognised by Indian courts where the subject matter is commercial in nature.

10 Licensing

10.1 What are the licensing and other eligibility requirements in your jurisdiction for lenders to a company in your jurisdiction, if any? Are these licensing and eligibility requirements different for a "foreign" lender (i.e. a lender that is not located in your jurisdiction)? In connection with any such requirements, is a distinction made under the laws of your jurisdiction between a lender that is a bank *versus* a lender that is a non-bank? If there are such requirements in your jurisdiction, what are the consequences for a lender that has not satisfied such requirements but has nonetheless made a loan to a company in your jurisdiction? What are the licensing and other eligibility requirements in your jurisdiction for an agent under a syndicated facility for lenders to a company in your jurisdiction?

Loans by domestic lenders are primarily provided by banking companies, financial institutions and NBFCs. Banking companies are governed by the Banking Regulation Act and the Reserve Bank of India Act, 1934 ("**RBI Act**"). The Indian banking sector includes nationalised banks (private sector banks that were nationalised by the GOI in 1969 and 1979), private sector banks that were granted licences post-liberalisation, old private sector banks incorporated as banking companies and foreign banks. In February 2013, the RBI released guidelines for private sector entities looking to apply for banking licences and has most recently also issued banking licences to several private sector banks. Foreign and domestic banks are required to obtain a licence from the RBI under the Banking Regulation Act to establish branches and subsidiaries in India and provide banking services in India. Financial institutions are generally regulated by the respective statutes under which they have been incorporated as well as by the RBI Act. Loans (foreign currency loans and rupee loans) by foreign lenders (without establishing branches and/or subsidiaries in India) are governed by the ECB Master Directions and the Borrowing and Lending Regulations (collectively, "**ECB Regulations**") enacted by the RBI, pursuant to the powers granted to it under the FEMA. While the ECB Master Directions set out the broad framework in respect of lending by foreign lenders to domestic borrowers in foreign currency as well as in Indian rupees. An eligible foreign lender does not need to obtain prior permission of the RBI if it meets the various conditions pertaining to all-in-cost, interest rate, average maturity, etc. specified under the ECB Master Directions. Eligible foreign lenders include international banks, capital markets, multilateral financial institutions, export credit agencies, foreign equity holders, etc. If a foreign lender does not fall under the category of an eligible lender, prior RBI approval is required. No other licensing is required. The domestic borrower is required to observe certain procedural formalities with the concerned authorised dealer bank and RBI to ensure the clear monitoring of inflow and outflow of funds. NBFCs are required to obtain a certificate of registration from the RBI under the RBI Act and are also required to maintain a minimum net worth and fulfil certain other financial parameters to be recognised as an NBFC as per the RBI Act. Companies, individuals, societies and trusts are categorised as moneylenders under the respective State's moneylending acts and are required to obtain a money lending licence to operate as a moneylender in the relevant state.

Extending ECBs without complying with the ECB Regulations or the terms and conditions on which approval has been granted by the RBI can result in the imposition of large penalties under FEMA, as well as civil imprisonment in serious cases. Similarly, banking companies, financial institutions and NBFCs undertaking any activities without obtaining requisite licences/approvals will also be subject to penalties as well as suspension or cancellation of their licences. A syndicate agent is generally appointed in large lending transactions with various kinds of loans where risk is shared among the lenders.

The syndicate agent is generally the largest lender. However, it can be any of the syndicate lenders. The main responsibilities of a syndicate agent is to formulate the syndicate documentation, arrange for financiers or underwrite the loans, negotiate the terms and conditions of the loans, etc. The fees usually include underwriting fees, agency fees, participation fees, management fees, etc. The syndicate bank will necessarily require licences mandated by the RBI, depending on whether it is a banking company or a financial institution or an NBFC. In case the syndicate agent is an investment bank, appropriate licences from the Securities and Exchange Board of India will also have to be obtained depending on the kind of financing that is being underwritten/arranged for by the bank.

11 Other Matters

11.1 Are there any other material considerations which should be taken into account by lenders when participating in financings in your jurisdiction?

Foreign lenders need to carefully examine and understand the nuances of Indian laws, including the CPC, FEMA, the Depositories Regulations, the Bankruptcy Code etc. with particular reference to conditions pertaining to creation of pledge or transfer of shares and securities of an Indian company, creation of corporate and personal guarantees, royalty payments, technical know-how fees, eligibility of borrowers as well as the lenders under the ECB Regulations. Hedging of foreign exchange risk is also an important factor which a lender needs to address while proceeding with lending in India, in addition to ensuring that requisite approvals and licences are obtained before a loan is extended to a borrower.

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Indonesia

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1 Overview

1.1 What are the main trends/significant developments in the lending markets in your jurisdiction?

To support the development of technology-based financial industry in Indonesia, in 29 December 2016, the Financial Services Authority ("**OJK**") issued OJK Regulation No. 77/POJK.01/2016 regarding Technology-Based Fund-Lending Services ("**POJK 77/2016**").

The Financial Technology-Based Money Lending Services or Fintech Peer-to-Peer Lending ("**Fintech P2P**") platforms are meant to facilitate the provision of cash funds on an expeditious, easy and efficient basis especially for micro, small, and medium scale business operators ("**UMKM**") to boost their competitiveness.

POJK 77/2016 sets out a range of comprehensive guidelines for the organisation of P2P Lending Services. It defines P2P lending services as financial services which are provided via online systems and which facilitate meetings between lenders and borrowers for the purpose of entering into loan agreements in the Indonesian Rupiah currency.

1.2 What are some significant lending transactions that have taken place in your jurisdiction in recent years?

As the largest issuer of bonds, the Government of Indonesia regularly taps the local market to finance the state budget. The Indonesian Government bond forms vary from conventional and retail government bonds to government sukuk in several tenors. Municipal bonds are issued by the province or district government for financing public utilities projects.

Although both government and corporate bonds are listed on the Indonesia Stock Exchange ("**IDX**"), they are mostly traded Over-the-Counter ("**OTC**"). Bank Indonesia ("**BI**") also issues short-term bank certificates known as Certificates of the Central Bank.

The Republic of Indonesia (the "**Republic**") returned to the global Sukuk markets through its issuance of US$ 1.0 billion five-year and US$ 2.0 billion 10-year Reg S/144A Trust Certificates due in 2022 and 2027, respectively (the "**Wakala Sukuk**"). The Wakala Sukuk is issued via Perusahaan Penerbit SBSN Indonesia lII ("**PPSl-lll**"), a legal entity established by the Republic solely for the purpose of issuing Shari'a compliant securities in foreign currencies in the international markets, and will be listed on the Singapore Stock Exchange and NASDAQ Dubai. The settlement date is 29 March 2017. The Wakala Sukuk tranches were priced on 22 March 2017 at par to yield 3.40% and 4.15%, respectively, and each tranche has been assigned a rating of Baa3 by Moody's Investors Service and BBB- by Fitch Ratings. It is the largest ever non-GCC US Dollar Sukuk transaction, and the largest ever US Dollar Sukuk issued by the Republic. The Sukuk are structured based on the Shari'a principle of Wakala. The Sukuk assets under this Wakala Sukuk issuance consist of (i) state-owned assets including land and buildings (51%), and (ii) project assets which are under construction or to be constructed (49%).

The other notable transaction is the financing of the US$ 8 billion Tangguh LNG Train 3 Expansion project. The project was funded by a consortium of international and domestic banks with a debt value of US$ 3.74 billion. The international lenders which were involved in the financing are Mizuho Bank, Bank of China, China Construction Bank, BNP Paribas, Korea Development Bank, Asian Development Bank, and the Japan Bank for International Cooperation. Domestic lenders involved in the financing are Bank Mandiri, Bank Rakyat Indonesia, Bank Negara Indonesia, and Indonesia Infrastructure Finance, with a total loan of US$ 100 million. It is said that this is the first time Indonesian financial institutions involved in the financing of an international LNG project. The project is expected to have up to 75% of its annual LNG production sold to the Indonesian state electricity company, PT PLN (Persero) to support Indonesia's growing energy demand.

2 Guarantees

2.1 Can a company guarantee borrowings of one or more other members of its corporate group (see below for questions relating to fraudulent transfer/financial assistance)?

Yes, a company guarantee is commonly acceptable in financing practice.

2.2 Are there enforceability or other concerns (such as director liability) if only a disproportionately small (or no) benefit to the guaranteeing/securing company can be shown?

Under Indonesian law, the validity of a legal act performed by an Indonesian company may be contested for want of a corporate benefit. Furthermore, under Indonesian law, there is uncertainty as to whether the issuance of a guarantee or a third party security or a stipulation in an agreement for the benefit of third parties by a company in order to secure the fulfilment of obligations of a third party is or can be regarded to be in the furtherance of the objects of that company (the

"*Ultra Vires* Doctrine"), and consequently, whether such guarantee or third-party security may be voidable or unenforceable under the laws of the Republic of Indonesia. In determining whether the issuance of a guarantee and third party security is in furtherance of the objects of a company, it is important to take into account the provisions of the articles of association of that company and whether that company derives certain commercial benefit from the transaction in respect of which the guarantee and third-party security is issued.

Based on the *Ultra Vires* Doctrine, validity or enforceability can in principle only be challenged by that company itself, i.e. arguably through (a) the shareholders of that company, (b) the board of directors of that company, (c) the board of commissioners of that company, or (d) by a receiver in the event of bankruptcy. By obtaining the written consent of all of the shareholders, board of directors and board of commissioners of the relevant company authorising that company to enter into a guarantee and third-party security for the benefit of the company for whose benefit it creates such guarantee or third-party security and confirming that such transaction is in the interests of that company, those parties should not be able to successfully challenge the validity or enforceability of that guarantee on the basis of the *Ultra Vires* Doctrine.

2.3 Is lack of corporate power an issue?

Yes, the Indonesian Company Law and the articles of association of an Indonesian company normally stipulate certain requirements to obtain a corporate power (approval) from the organs of the company, i.e. board of commissioners' approval and/or shareholders' approval. Lack of corporate approval would legally affect the validity of the corporate guarantee and cause the board of directors to be held liable against any loss in relation to such provision of corporate guarantee/security.

2.4 Are any governmental or other consents or filings, or other formalities (such as shareholder approval), required?

Please refer to our explanation in question 2.3 above.

2.5 Are net worth, solvency or similar limitations imposed on the amount of a guarantee?

On the amount of guarantee, it is not specifically stipulated in the regulations. Please note, however, that Indonesian Company Law stipulates that the board of directors must request shareholders' approval to encumber the assets of the company having a value that exceeds 50% of the net assets in 1 (one) transaction or more, whether or not related to each other. Thus, it could somehow be interpreted that a guarantee needs to also consider the assets of the company.

2.6 Are there any exchange control or similar obstacles to enforcement of a guarantee?

There are no exchange control obstacles for the enforcement of a guarantee. The enforcement of a guarantee will be done through a court order. Please note, however, that the Indonesian court system recognises three levels of courts, namely the district court, court of appeal and Supreme Court. This means that if a borrower still challenges a decision from the judges of a district court and files an appeal to the court of appeal, the guarantee cannot be enforced by the lender pending the decision of the judges of court of appeal. This process would continue up to the Supreme Court, which can certainly take years for enforcement.

3 Collateral Security

3.1 What types of collateral are available to secure lending obligations?

To secure the lending obligations, in general, we can classify the common types of security as follows:

- Immovable assets – i.e. land, buildings, fixtures and vessels with gross weight of 20 cubic metres or more and aircraft – form of security granted: **mortgage**.
- Movable assets – i.e. machinery, inventory, raw material and vehicles – form of security: **fiduciary transfer**.
- Intangible assets – i.e. shares, intellectual property rights, etc. – form of security: **pledge**.

3.2 Is it possible to give asset security by means of a general security agreement or is an agreement required in relation to each type of asset? Briefly, what is the procedure?

A special agreement is required to create security over each type of assets. In general, the procedure for each type of security is as follows:

- Mortgage:

  A mortgage deed must be signed before the Land Officer with jurisdiction over the land to be mortgaged. This deed must be in Bahasa Indonesia (the official language of Indonesia) and in the prescribed official form. The signed mortgage deed must be then registered at the relevant land offices. The mortgage is established at the moment it is entered in the land book located at the relevant land offices.
- Fiduciary security:

  A fiduciary security deed must be signed before the notary. This deed must be in Bahasa Indonesia (the official language of Indonesia) and in the prescribed official form. Based on this deed, the transferor (borrower) transfers its legal title to the transferred assets to the transferee (lender) for the period during which the debt remains outstanding. The fiduciary security is effective when the fiduciary security is recorded in the Fiduciary Register Book (*Buku Daftar Fidusia*) at the fiduciary registration office.
- Pledge:

  A pledge agreement can be executed in a notarial deed or executed privately, setting out the pledge's particulars. A pledge of shares is effective when the pledge is recorded in the shareholders' register of the relevant company.

3.3 Can collateral security be taken over real property (land), plant, machinery and equipment? Briefly, what is the procedure?

Please refer to questions 3.1 and 3.2.

3.4 Can collateral security be taken over receivables? Briefly, what is the procedure? Are debtors required to be notified of the security?

Yes, the proper form of security over receivables is fiduciary transfer. Please refer to question 3.2 above.

3.5 Can collateral security be taken over cash deposited in bank accounts? Briefly, what is the procedure?

Yes, the most common form of security over a cash deposit is a pledge over the bank account. However, the fiduciary registration office has expressed the view that a bank account cannot be the subject of an Indonesian security interest and the enforceability of a pledge over a bank account is yet to be tested in court. Although its enforceability is doubtful, it is common practice to secure cash deposits with a pledge over a bank account.

3.6 Can collateral security be taken over shares in companies incorporated in your jurisdiction? Are the shares in certificated form? Can such security validly be granted under a New York or English law governed document? Briefly, what is the procedure?

Yes, collateral security over shares in companies incorporated in Indonesia can be taken. A pledge of Indonesian shares can be enforced provided the governing law is Indonesian law. See the procedure discussed above.

3.7 Can security be taken over inventory? Briefly, what is the procedure?

Security over the movable property can be taken by way of fiduciary transfer.

The Fiduciary Security must be made by a notarial deed and in the Indonesian language. The debt so secured can be in the form of:

- existing debts;
- future debts already agreed upon in a certain amount; or
- debts the amount of which can be determined at the time of execution based on the principal agreement.

The goods encumbered by a Fiduciary Security must be registered, including goods located outside Indonesian territory.

The fiduciary transferee shall apply for the registration of the Fiduciary Security and attach to the application a registration statement with the stipulated data. Upon registration on the date of receipt of the registration application, the applicant will obtain a Fiduciary Security Certificate stating the date of the application. The Fiduciary Security is created on the date of registration it in the Fiduciary Register Book (*Buku Daftar Fidusia*). The fiduciary security certificate has force of execution equal to a final court verdict.

3.8 Can a company grant a security interest in order to secure its obligations (i) as a borrower under a credit facility, and (ii) as a guarantor of the obligations of other borrowers and/or guarantors of obligations under a credit facility (see below for questions relating to the giving of guarantees and financial assistance)?

Yes, it can.

3.9 What are the notarisation, registration, stamp duty and other fees (whether related to property value or otherwise) in relation to security over different types of assets?

Registration fees for mortgages are normally based on the value of the secured amount under the mortgage (the lender has a choice whether to use the actual value of the assets or the principal amount of the loan), and can be costly. There is also a registration fee for fiduciary transfers. However, the amount is nominal. Notary fees concerning fiduciary transfers and pledges of shares vary and are at the notary's discretion. Stamp duty of IDR 6,000 (approximately US$ 0.50) is payable on any agreement signed by the parties.

3.10 Do the filing, notification or registration requirements in relation to security over different types of assets involve a significant amount of time or expense?

Please refer to question 3.9 above, particularly on the registration fee for mortgages. With regard to the estimated time for filing and registering a mortgage or Fiduciary Security, it would approximately take one month, while for the shares pledge it can be done once the pledge agreement has been executed.

3.11 Are any regulatory or similar consents required with respect to the creation of security?

Normally, creditor consent is required (unless the relevant security provider does not have any debt). A shareholder approval is also required in the situation as we have described in our response to question 2.5 above.

3.12 If the borrowings to be secured are under a revolving credit facility, are there any special priority or other concerns?

If it is a revolving credit facility and the initial loan has been repaid, the security needs to be re-created every time the facility is given. However, we understand, in practice, some creditors have different views. They are of the view that no re-creation of security is required since the initial security covers the entire facility.

3.13 Are there particular documentary or execution requirements (notarisation, execution under power of attorney, counterparts, deeds)?

Yes, please refer to question 3.9 above.

4 Financial Assistance

4.1 Are there prohibitions or restrictions on the ability of a company to guarantee and/or give security to support borrowings incurred to finance or refinance the direct or indirect acquisition of: (a) shares of the company; (b) shares of any company which directly or indirectly owns shares in the company; or (c) shares in a sister subsidiary?

Financial assistance is not an issue: there are no such prohibitions or restrictions other than those that may be set out in the Articles of Association of the company concerned. In addition, a company guaranteeing and/or giving security to support borrowings incurred to finance or refinance the direct or indirect acquisition of such shares may be deemed *ultra vires* unless there is direct commercial benefit. See also question 2.5 above.

5 Syndicated Lending/Agency/Trustee/Transfers

5.1 Will your jurisdiction recognise the role of an agent or trustee and allow the agent or trustee (rather than each lender acting separately) to enforce the loan documentation and collateral security and to apply the proceeds from the collateral to the claims of all the lenders?

Indonesia indeed recognises the role of an agent for the above purpose. They are known as a "security agent". The security agent is appointed by the lenders in a separate agreement. This agreement, among others, stipulates the period of appointment, rights and obligations of the security agent, termination, etc.

5.2 If an agent or trustee is not recognised in your jurisdiction, is an alternative mechanism available to achieve the effect referred to above which would allow one party to enforce claims on behalf of all the lenders so that individual lenders do not need to enforce their security separately?

This is not applicable.

5.3 Assume a loan is made to a company organised under the laws of your jurisdiction and guaranteed by a guarantor organised under the laws of your jurisdiction. If such loan is transferred by Lender A to Lender B, are there any special requirements necessary to make the loan and guarantee enforceable by Lender B?

Yes, Lender A may use a "cessie mechanism", commonly known as an "assignment of claim receivables", and assign its rights to Lender B by executing the "Cessie Deed". Regarding the guarantee, all related guarantee deeds must be re-executed in favour of Lender B.

6 Withholding, Stamp and Other Taxes; Notarial and Other Costs

6.1 Are there any requirements to deduct or withhold tax from (a) interest payable on loans made to domestic or foreign lenders, or (b) the proceeds of a claim under a guarantee or the proceeds of enforcing security?

Yes, there are requirements to deduct or withhold tax from interest payable on loans made to domestic or foreign lenders, as stipulated in Income Tax Law. For cross-border loans, the withholding tax rate can usually be reduced if the lender resides in a jurisdiction which has a tax treaty with Indonesia.

6.2 What tax incentives or other incentives are provided preferentially to foreign lenders? What taxes apply to foreign lenders with respect to their loans, mortgages or other security documents, either for the purposes of effectiveness or registration?

No tax incentives would be given to a foreign creditor. However, foreign creditors may enjoy a certain tax rate to the extent its country has a treaty with Indonesia.

6.3 Will any income of a foreign lender become taxable in your jurisdiction solely because of a loan to or guarantee and/or grant of security from a company in your jurisdiction?

No, unless, under the "force of attraction" rule, such loan or guarantee or grant generates income for the foreign lender attributable to its Indonesian business, if any.

6.4 Will there be any other significant costs which would be incurred by foreign lenders in the grant of such loan/guarantee/security, such as notarial fees, etc.?

Please refer to question 3.9 above, particularly on the registration fee for mortgages.

6.5 Are there any adverse consequences to a company that is a borrower (such as under thin capitalisation principles) if some or all of the lenders are organised under the laws of a jurisdiction other than your own? Please disregard withholding tax concerns for purposes of this question.

No, but recurring administrative requirements relating to the reporting of payment of interest and principal apply, and foreign loans received by certain categories of Indonesian borrowers require prior governmental approval.

7 Judicial Enforcement

7.1 Will the courts in your jurisdiction recognise a governing law in a contract that is the law of another jurisdiction (a "foreign governing law")? Will courts in your jurisdiction enforce a contract that has a foreign governing law?

Indonesian law recognises a choice of foreign law as the governing law of a loan agreement except to the extent that: (i) a loan term or a provision of that law is clearly incompatible with Indonesian public policy; and (ii) the Indonesian court must give effect to mandatory rules of the law of another jurisdiction with which the situation has a close connection.

Theoretically, courts in Indonesia can enforce a contract that has a foreign governing law. In practice, however, there have been cases where Indonesian courts have refused to give effect to choice of foreign law clauses for other specified or unspecified reasons. A foreign choice of law is not permitted for security agreements or guarantees, and these agreements must be governed by Indonesian law.

7.2 Will the courts in your jurisdiction recognise and enforce a judgment given against a company in New York courts or English courts (a "foreign judgment") without re-examination of the merits of the case?

Indonesian courts will not recognise judgments of foreign courts. Accordingly, it will be necessary for any matter in which a judgment has been obtained in a foreign court to be re-litigated in the Indonesian courts in order to enforce in Indonesia the cause of action giving rise to the foreign judgment, and such Indonesian courts may attribute such importance to the foreign judgment as they may deem appropriate.

7.3 Assuming a company is in payment default under a loan agreement or a guarantee agreement and has no legal defence to payment, approximately how long would it take for a foreign lender to (a) assuming the answer to question 7.1 is yes, file a suit against the company in a court in your jurisdiction, obtain a judgment, and enforce the judgment against the assets of the company, and (b) assuming the answer to question 7.2 is yes, enforce a foreign judgment in a court in your jurisdiction against the assets of the company?

(a) It would take approximately six months to obtain a judgment in the district court. However, if the counter party (defendant) appeals to the higher courts (court of appeal and supreme courts), it may take years.

(b) Foreign court judgments cannot be enforced in Indonesia.

7.4 With respect to enforcing collateral security, are there any significant restrictions which may impact the timing and value of enforcement, such as (a) a requirement for a public auction, or (b) regulatory consents?

On default, a security interest can be enforced through a public auction or private sale.

Public sale or auction

In theory, a public auction can be conducted without a court judgment or order if the owner of the assets is co-operative. In practice, however, a court order is required.

In the case of listed shares, however, the Indonesian Civil Code clearly specifies that an auction held by two brokers can be conducted in the market. In this case, no court order is required so long as a power of attorney to dispose of the shares has been given (usually at the time the pledge is created).

Private sale

A private sale is permitted if this means that a higher sale price can be achieved for the parties. Private sale requires consent from the owner of the assets, which is normally included in the relevant security documents.

For mortgage and fiduciary transfer, private sale can only be conducted:

- After the expiry of one month from written notification of the intended sale to interested parties and publication of this notice in at least two daily newspapers with circulation in the area where the asset is located.
- Where no third party has voiced an objection against the private sale. The law is unclear as to who these third parties may be, although it is safe to assume that they include, at least, the borrower's other creditors.

7.5 Do restrictions apply to foreign lenders in the event of (a) filing suit against a company in your jurisdiction, or (b) foreclosure on collateral security?

The above enforcement method as explained in question 7.4 also applies to foreign lenders.

7.6 Do the bankruptcy, reorganisation or similar laws in your jurisdiction provide for any kind of moratorium on enforcement of lender claims? If so, does the moratorium apply to the enforcement of collateral security?

Yes, it is known as Suspension of Payments (moratorium). The procedure is started by the debtor or its creditor petitioning the Commercial Court for a suspension of payments. The Commercial Court must then grant a provisional moratorium, and appoint a supervisory judge and an administrator or receiver to assist the debtor in managing its estate. The debtor will be entitled to manage and dispose of its assets jointly with the administrator. During this suspension period, the debtor does not have to make payments to its unsecured creditors and secured creditors cannot enforce their security without the court's consent. The purpose of a suspension of payments is to enable the debtor to propose a composition plan.

Creditors holding a mortgage, a pledge, a fiduciary security or any other *in rem* security right may enforce its right against the secured assets as if there were no bankruptcy. However, the aforesaid right is limited by the so-called "stay period". A stay is a restriction on the right of secured creditors and third parties to exercise their right. This stay applies for a time period of at most 90 (ninety) days as of the date of the bankruptcy judgment. The stay does not apply to claims of creditors whose rights are secured by cash deposits and the rights of creditors to set-off debts. By law, the 90-day stay will expire on an earlier date in case of an early termination of the bankruptcy or upon the commencement of the state of insolvency.

7.7 Will the courts in your jurisdiction recognise and enforce an arbitral award given against the company without re-examination of the merits?

A foreign or international arbitral award can be recognised and enforced in Indonesia as Indonesia has ratified the 1958 New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards through Presidential Decision No. 34 of 1981. The procedures for recognition and enforcement of foreign arbitral awards are further regulated by Law No. 30 of 1999 on Arbitration and Alternative Dispute Resolutions. However, before the enforcement, the award needs to be registered at the District Court of Central Jakarta. Please note, however, that the Chairman of the District Court of Central Jakarta may refuse to issue the writ of execution if it views that the award violates public order. The decision rejecting the enforcement can be appealed at the Supreme Court and must be decided by the Supreme Court within 90 (ninety) days as of the registration of the appeal. A decision approving the enforcement of the award cannot be appealed.

8 Bankruptcy Proceedings

8.1 How does a bankruptcy proceeding in respect of a company affect the ability of a lender to enforce its rights as a secured party over the collateral security?

The mortgage, the pledge and the fiduciary transfer are "*in rem rights*" which are "*absolute*" and "*exclusive*", and create preferential rights to the holder of the security even in bankruptcy. Bankruptcy of the mortgagor, the pledgor and the fiduciary transferor does not, in principle, affect the security right of the mortgagee, pledgee and transferee in that the assets in question are not regarded as being part of the bankruptcy assets. However, the creditors should note the "stay" period as we have elaborated in response to question 7.6, which restricts the ability of the creditors to enforce its rights.

8.2 Are there any preference periods, clawback rights or other preferential creditors' rights (e.g., tax debts, employees' claims) with respect to the security?

Yes, there are.

On the preference period with respect to the security, we believe that there should be no preference period, except that: once the bankruptcy estate is declared in the state of insolvency, the secured creditors must exercise their privileged right over the collateral within 2 (two) months as of the point the bankruptcy estate is declared to be in the state of insolvency. Otherwise, the appointed receiver is required to request the delivery of the collateral to be sold by the receiver. If the receiver has enforced the collateral, the proceeds that will be distributed to the secured creditors need first to be deducted by not only the amount of the mandatory preferred claims (which will also apply if the secured creditors enforced the collateral by themselves), but also the bankruptcy costs.

On the clawback rights, under Articles 41 and 42 of the Indonesian Bankruptcy Law, for the interest of the bankruptcy assets, only the receiver could request the nullification of a preferential transfer transaction conducted by the debtor before its bankruptcy, if such transaction was considered detrimental to the creditors ("**Bankruptcy Preferential Transfer**"). To nullify a Bankruptcy Preferential Transfer, the receiver must prove the following requirements:

(i) the preferential transfer was performed by the debtor before it was declared bankrupt;

(ii) the debtor was not obligated by contract (existing obligation) or by law to perform the preferential transfer;

(iii) the preferential transfer prejudiced the creditors' interests; and

(iv) the debtor and such third party had or should have had knowledge that the preferential transfer would prejudice the creditors' interests.

If the preferential transfer transaction was conducted within a period of 1 (one) year before the company's bankruptcy, provided that the transaction was not mandatory for the debtor and unless it could be proven otherwise, both the debtor and the third party with whom the said act was performed were deemed to know that such transaction was detrimental to the creditors when such transaction belongs to one of the following three categories:

(i) a transaction in which the consideration that the debtor received was substantially less than the estimated value of the consideration given;

(ii) a payment or granting of security for debts which are not yet due; or

(iii) a transaction entered into by the debtor with a certain relative or related parties.

There is no provision under the Bankruptcy Law which stipulates a specific period when the Bankruptcy Preferential Transfer claim can be made. However, request for the nullification of a Bankruptcy Preferential Transfer shall be made by the receiver. The claim can be made only if the debtor has a receiver.

If the underlying security documents are nullified due to the Bankruptcy Preferential Transfer, then the security will also become invalid.

On other preferential creditors' rights, there are several kinds of creditors, generally regulated in the Indonesian Civil Code ("**ICC**"), Indonesian Bankruptcy Law, and Law No. 6 of 1983 which was lastly amended by Law No. 16 of 2009 regarding the General Provision of Taxation ("**Tax Law**"), which have preferential rights with respect to the *in rem* security as follows:

A. Specific expenses stipulated by the Tax Law:
- legal expenses arising solely from a court order to auction movable and/or immovable goods;
- expenses incurred for securing the goods; and
- legal expenses, arising solely from the auction and settlement of inheritance.

B. Preferred creditors ranked above the secured creditors.

Tax claims and court charges which specifically result from the disposal of a movable or immovable asset (these must be paid from the proceeds of the sale of the assets over all other priority debts, and even over a pledge or mortgage) and the legal charges, exclusively caused by sale and saving of the estate (these will have priority over pledges and mortgages).

C. The receiver's fee.

8.3 Are there any entities that are excluded from bankruptcy proceedings and, if so, what is the applicable legislation?

No, there are no entities which are excluded from bankruptcy proceedings.

8.4 Are there any processes other than court proceedings that are available to a creditor to seize the assets of a company in an enforcement?

No, there are no processes other than the court proceedings which are available to a creditor to seize the assets of the company in enforcement.

9 Jurisdiction and Waiver of Immunity

9.1 Is a party's submission to a foreign jurisdiction legally binding and enforceable under the laws of your jurisdiction?

Yes, a submission to a foreign jurisdiction should be binding and enforceable.

9.2 Is a party's waiver of sovereign immunity legally binding and enforceable under the laws of your jurisdiction?

Sovereign immunity has not been explicitly legislated in Indonesia. The Republic of Indonesia has subscribed to the doctrine of restrictive sovereign immunity by its entry into the Convention on the Settlement of Investment Disputes between States and Nationals of other States of 1965. However, if a party is a state-owned company and enters into a commercial contract, it can be argued that such state-owned company has waived its entitlement (if any) to sovereign immunity.

In practice, the Government of Indonesia ("**GOI**") does not use sovereign immunity as the basis of defence in a dispute which relates to its obligation under a commercial agreement.

Nevertheless, the GOI specifically does not waive any immunity in respect of:

- actions brought against the Republic arising out of or based upon U.S. federal or state securities laws;
- attachments under Indonesian law;
- present or future "premises of the mission" as defined in the Vienna Convention on Diplomatic Relations signed in 1961;
- "consular premises" as defined in the Vienna Convention on Consular Relations signed in 1963;
- any other property or assets used solely or mainly for Government or public purposes in the Republic or elsewhere; and
- military property or military assets or property or assets of the Republic related thereto.

The GOI is subject to suit in competent courts in Indonesia. However, Law No. 1 of 2004 on State Treasury prohibits the seizure or attachment of property or assets owned by the GOI.

10 Licensing

10.1 What are the licensing and other eligibility requirements in your jurisdiction for lenders to a company in your jurisdiction, if any? Are these licensing and eligibility requirements different for a "foreign" lender (i.e. a lender that is not located in your jurisdiction)? In connection with any such requirements, is a distinction made under the laws of your jurisdiction between a lender that is a bank *versus* a lender that is a non-bank? If there are such requirements in your jurisdiction, what are the consequences for a lender that has not satisfied such requirements but has nonetheless made a loan to a company in your jurisdiction? What are the licensing and other eligibility requirements in your jurisdiction for an agent under a syndicated facility for lenders to a company in your jurisdiction?

There are not necessarily any eligibility requirements for a lender to be a bank. Lenders to a company in Indonesia do not need to be licensed in Indonesia as long as the loan is not given in a manner that causes the lenders to be engaged in the banking business in Indonesia. There is no distinction between a lender that is a bank and a non-bank. Similarly with lenders, there is no specific licence for an agent in Indonesia. However, we normally assume that the lenders and agents have proper licences under its jurisdiction.

11 Other Matters

11.1 Are there any other material considerations which should be taken into account by lenders when participating in financings in your jurisdiction?

Lenders should also take into account the fulfilment by the borrower of several requirements including Bank Indonesia Regulation No. 16/21/PBI/2014 as amended by Bank Indonesia Regulation No. 18/4/PBI/2016 concerning the Implementation of Prudential Principles for the Management of Offshore Loans of Non-Bank Corporations ("**NBCs**") ("**Regulation 16**"). Regulation 16, which came into force as of 1 January 2015, aims to mitigate various risks inherent to private external debt, specifically for non-bank corporations. In principle, Regulation 16 requires NBCs with offshore loans in foreign currency (except for trade credit) to implement prudential principles by satisfying certain obligations to meet prescribed hedging ratios, liquidity ratios, and credit ratings, as follows:

- Hedging Requirement. Each NBC must effectuate a minimum hedging ratio of 25% of the combined negative spread between its Foreign Exchange Assets and its Foreign Exchange Liabilities which will be due (i) within three months after the end of the relevant quarter, and (ii) between the fourth and the sixth month after the end of the relevant quarter. The hedging ratio must be realised through a derivative transaction in the form of forward, swap and/or option. During the first year after effectiveness (until 31 December 2015), a reduced minimum hedging ratio of 20% applied.
- Liquidity Ratio. The NBC must meet a minimum liquidity ratio of 70%, calculated by dividing the total value of Foreign Exchange Assets that is available up to three months after the end of the last quarter by the amount of Foreign Exchange Liabilities that are due up to three months after the end of the most recent quarter. Receivables derived from forwards, swaps, and/or options which will be closed up to three months after the end of the most recent quarter may be included in the calculation. During the first year after effectiveness (until 31 December 2015), a reduced minimum liquidity ratio of 50% applied.
- Credit Rating. The NBC must have a credit rating (an issuer credit rating and/or a debt credit rating, as the case may be, depending on the type and term of the term of the offshore foreign currency debt) of at least BB- (or equivalent) issued by an authorised Rating Agency (including, amongst others, Fitch Ratings, Moody's Investor Service and Standard and Poor's). The rating may not be older than two years. The rating must be a long-term debt rating if the NBC wishes to issue long-term bonds. The credit rating requirement is not applicable to offshore debt in foreign exchange ("**FX Offshore Loan**") obtained, among others, (i) for the purposes of refinancing (i.e. without increase of principal), or (ii) from international institutional credit providers (bilateral or multilateral) in relation to infrastructure projects (including infrastructure in the fields of transportation, roads, irrigation, drinking water, sanitation, telecommunication and informatics, electricity, and oil and gas). Institutions that are specifically mentioned in Regulation 16 are, among others, the International Finance Corporation ("**IFC**"), Japan Bank for International Cooperation ("**JBIC**"), Japan International Cooperation Agency ("**JICA**"), Asian Development Bank ("**ADB**") and Islamic Development Bank ("**IDB**"). The Credit Rating requirement would be applicable on the FX Offshore Loan that is signed or issued as of 1 January 2016.

The enactment of the BI Regulation No. 18/4/PBI/2016 dated 22 April 2016 has expanded the coverage of exemption on credit rating requirement so that multifinance companies would not be subjected to the credit rating requirement provided that certain requirements on financial soundness level and gearing ratio have been met. In addition to multifinance companies, the Indonesia Eximbank (*Lembaga Pembiayaan Ekspor Indonesia*) has also been exempted from the credit rating requirement.

It should also be noted that, according to the Regulation 16, as of 1 January 2017, hedging transactions for the purpose of fulfilling the hedging requirement must be conducted with banks in Indonesia. Receivables from hedging transactions which are not conducted with banks in Indonesia will not be considered as Foreign Exchange Assets, and will not be considered as fulfilment of the hedging and liquidity ratio requirements.

Furthermore, Bank Indonesia Regulation No. 17/3/PBI/2015 concerning Mandatory Use of the Rupiah in the Territory of Indonesia ("**Regulation No. 17**"), which is effective for cash transactions as of 31 March 2015, and for non-cash transactions, 1 July 2015 stipulates that individuals or corporations must use the Rupiah in all cash and non-cash transactions in Indonesia. Transactions extend to the use of cheques, giro slips, credit cards, debit cards, ATM cards, and electronic money, which include:

(a) payment transactions;

(b) other settlement of obligations that must be fulfilled on money terms; and/or

(c) other financial transactions.

There are some specific exemptions to this mandatory use of the Rupiah that are stipulated in Regulation No. 17 (including its exemptions and formality to obtain those exemptions).

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Mr. Gunadi returned to ABNR after a few months post with a major Indonesian power company as its senior legal manager. He has been listed by The Asia Pacific Legal 500 2016 as a recommended lawyer in Projects & Energy and Intellectual Property.

A B N R
COUNSELLORS AT LAW

Ali Budiardjo, Nugroho, Reksodiputro, usually abbreviated to ABNR, was established in Jakarta in 1967 as a partnership of legal consultants in Indonesian business law. The firm is one of Indonesia's largest independent full-service law firms. The commitment we make to clients is to provide broad-based, personalised service from top-quality teams of lawyers with international experience that includes groundbreaking deals and projects. ABNR's reputation has been recognised around the world by independent industry surveys and law firm guides. ABNR was selected, based on its high level of integrity and professionalism, to be the sole Indonesian member of the world's largest law firm association Lex Mundi and of the prestigious Pacific Rim Advisory Council ("**PRAC**").

Ireland

Conor Houlihan

Dillon Eustace

Richard Lacken

1 Overview

1.1 What are the main trends/significant developments in the lending markets in your jurisdiction?

Alternative finance continues to be a developing sphere in the Irish lending market. Alternative lenders are very active; in particular, in the Irish real estate finance space. Crowdfunding is an area of increasing interest. Although not currently regulated in Ireland, the European Commission has proposed a pan-European regulatory regime for crowdfunding in its 2018 work programme and is due to bring a proposal for an EU framework on crowd and peer-to-peer finance for discussion in March 2018. Beyond the foregoing, domestic and cross-border loan and financing activity levels are high – especially in some sectors, like aviation, where Ireland has particular dominance and expertise.

There have been notable legal/regulatory developments too – for example, the establishment of the Central Credit Register, a new centralised system for collecting personal and credit information on loans.

The impact of Brexit on Ireland, while yet unknown, could present significant opportunities for the Irish lending market. This is so particularly given Ireland's common law system and its geographic location, being close to Britain and mainland Europe, which make it an attractive destination for international banks, currently operating out of the UK, which want to maintain an EU presence post-Brexit.

1.2 What are some significant lending transactions that have taken place in your jurisdiction in recent years?

As already noted, transaction activity levels have been healthy across a range of asset-classes. Real estate finance has been particularly strong with the full spectrum lenders (traditional banks, debt funds, etc.) and transaction types (e.g. commercial/residential, development/investment, etc.). One landmark transaction, in which Dillon Eustace acted for the purchaser/borrower, was the financing of the newly planned EXO building, which – when constructed – will be Dublin's tallest office building. Transaction numbers in the loan sales space – which has been a major focus for the past number of years – were lower in 2017 but 2018 looks set to be a very busy year. One noteworthy transaction in 2017 was Proteus RMBS DAC, which is a securitisation of the residential mortgage portfolio of Danske Bank in Ireland in which Dillon Eustace acted for the significant investor. The transaction is significant because of its size (€1.8 billion approx.), the context (i.e. securitisation used to fund the purchase/sale of a portfolio of tracker mortgages originated by Danske Bank) and the fact that this is one of the largest post-crisis securitisations in Ireland.

2 Guarantees

2.1 Can a company guarantee borrowings of one or more other members of its corporate group (see below for questions relating to fraudulent transfer/financial assistance)?

Yes; however, this is subject to the corporate benefit rule (discussed at question 2.2 below) and to certain provisions of the Companies Act 2014 (as amended) (the "**Act**") relating to the provision of financial assistance (discussed at question 4.1 below).

2.2 Are there enforceability or other concerns (such as director liability) if only a disproportionately small (or no) benefit to the guaranteeing/securing company can be shown?

Although not specifically addressed in the Act, it is generally accepted that Irish companies must derive some form of corporate benefit from transactions which they enter into. Accordingly, prior to authorising the provision of a guarantee/security to a third party, directors should consider, and document such considerations of, the commercial benefit that will accrue to the company as a result of providing such security. Directors who authorise a transaction which does not benefit the company may be liable for breach of their statutory and fiduciary duties. In the context of a guarantee of the borrowings of another corporate group member, it is often possible to establish sufficient corporate benefit if the provision of the guarantee/security would benefit the group as a whole. For example, a holding company which guarantees the obligations of its subsidiary could feasibly expect to benefit from the success of that subsidiary through increased dividends.

2.3 Is lack of corporate power an issue?

Generally no, as the doctrine of *ultra vires* has been abolished by the Act and accordingly an Irish company limited by shares has the same unlimited capacity as an individual. However, the Act introduced a new type of private company – a Designated Activity Company ("**DAC**") – which must (similar to a public limited company) have an objects clause which sets out the specific powers of the company. If it is not specifically stated in the objects clause of such a company that it has the power to issue a guarantee or grant security, then any such action by the company could be subject to challenge by a shareholder of that company. While this in itself should not impact the validity or enforceability of the guarantee/security, there is a risk that the third party lender may become indirectly involved in a dispute between a company and its shareholders. In addition to this, any liquidator appointed to a company, which has granted security in breach of its objects clause may, in certain circumstances, have clawback rights under the Act which could potentially result in the security being set aside (see question 8.2 below).

2.4 Are any governmental or other consents or filings, or other formalities (such as shareholder approval), required?

Generally no, subject to the provisions of the Act relating to financial assistance and transactions with directors. However, if the company is regulated or subject to the supervision of the Central Bank of Ireland (the "**CBI**") or some other regulatory authority, additional consents may be required. For example, an Irish regulated fund cannot give "guarantees" to support the obligations of a third party (which may include another sub-fund within the same umbrella fund structure). While, the term "guarantees" when used in this context is not defined, it is generally accepted that this term includes any security provided to support the obligations of a third party. In terms of formalities, a guarantee must be in writing and must be executed as a deed. Execution as a deed is important for a number of reasons, for example, to remove any concerns about the adequacy of the consideration passing to the guarantor.

2.5 Are net worth, solvency or similar limitations imposed on the amount of a guarantee?

No; however, in certain circumstances a guarantee may be set aside as an unfair preference or due to the insolvency of the company (see question 8.2 below).

2.6 Are there any exchange control or similar obstacles to enforcement of a guarantee?

Generally, no (subject to the application of anti-money laundering, anti-terrorism, anti-corruption and human rights laws and regulations, and any restrictions on financial transfers arising from any United Nations, EU and Irish sanctions).

3 Collateral Security

3.1 What types of collateral are available to secure lending obligations?

In principle, all assets of an Irish company are available to secure lending, subject to any contractual restrictions to which a company might be bound. The most common forms of security taken by a lender are:

i. **Mortgage:** there are essentially two types of mortgage – a legal mortgage and an equitable mortgage. A legal mortgage involves the transfer of legal title to an asset by a debtor, by way of security, upon the express or implied condition that legal title will be transferred back to the debtor upon the discharge of its obligation. An equitable mortgage on the other hand involves the transfer of the beneficial interest in the asset to the mortgagee with legal title remaining with the debtor and as such creates an equitable security interest only. Mortgages are commonly taken over shares, aircraft and ships.

ii. **Charge:** this represents an agreement between a creditor (chargee) and a debtor (chargor) to appropriate and look to an asset and its proceeds to discharge indebtedness. The principle difference between a mortgage and a charge is that a charge need not involve the transfer of ownership in the asset. A charge may be fixed (i.e. security attaches to a specific asset) or floating (i.e. security floats over the asset leaving the chargor free to deal with it until, upon the happening of certain defined events, the charge crystallises into a fixed charge) in nature. A fixed charge can be created by a company or an individual whereas a floating charge can only be created by a company. It is also worth noting that a floating charge ranks behind certain preferential creditors such as the Irish Revenue Commissioners ("**Revenue**") and employees of the chargor in respect of unpaid wages, etc.

iii. **Assignment:** this is akin to a mortgage in that it transfers the legal or beneficial ownership in an asset to the creditor upon the understanding that ownership will be assigned back to the debtor upon discharge of the secured obligation owing to the creditor. Assignments are most commonly utilised in the context of intangible assets such as receivables, book debts and other choses in action. Assignments to a creditor are sometimes referred to as security assignments to distinguish them from absolute assignments where the ownership is being assigned by way of sale for value. In order to be a valid and effective legal assignment, as opposed to an equitable assignment, there must be absolute assignment (although it can be stated to be by way of security), it must be in writing under hand of the assignor, and express notice in writing must be given to the third party from whom the assignor would have been entitled to receive or claim the right which is assigned.

iv. **Others:** to include a pledge, lien, chattel mortgage, bill of sale and retention of title.

3.2 Is it possible to give asset security by means of a general security agreement or is an agreement required in relation to each type of asset? Briefly, what is the procedure?

Security over all, or substantially all, of a company's assets usually takes the form of an "all-assets" debenture, which is a single security document entered into by a company in favour of the secured party(-ies) to create security (e.g. a combination of mortgages, assignments and/or fixed and floating charges) over the borrower's assets. The debenture will usually include: (i) a fixed charge over specific assets which are identifiable and can be controlled by the lender (e.g. buildings, restricted accounts, intellectual property assets); (ii) a floating charge over fluctuating and less identifiable assets (e.g. inventory); (iii) an assignment of any interest in receivables, contracts, insurance policies and bank accounts; and (iv) a mortgage and/or charges over real estate and shares.

3.3 Can collateral security be taken over real property (land), plant, machinery and equipment? Briefly, what is the procedure?

Yes. Security over real property, plant, machinery and equipment is most commonly taken by way of fixed charge. Where security is created over real estate which is registered in the Property Registration Authority of Ireland ("**PRAI**"), an additional prescribed form is also required to validly create the security.

3.4 Can collateral security be taken over receivables? Briefly, what is the procedure? Are debtors required to be notified of the security?

Security over receivables most commonly takes the form of a legal assignment and is permitted so long as the underlying contract creating the receivable does not contain a prohibition on assignment. In order to be a valid legal assignment certain requirements (as outlined in question 3.1 above) must be adhered to, including the provision of written notice to the third party from whom the assignor would have been entitled to receive or claim the assigned right (the "**Underlying Debtor**"). An assignment not meeting these criteria is deemed to be an equitable assignment. One of the disadvantages of an equitable assignment is that the rights of the assignee will be subject to any equity (such as rights of set-off) already vested in the Underlying Debtor. In addition, should the Underlying Debtor pay off a debt due to the assignor and claim a good discharge of this debt, in circumstances where no notice of the assignment was given to the Underlying Debtor, then the assignee would solely reliant on the assignor passing this payment on.

3.5 Can collateral security be taken over cash deposited in bank accounts? Briefly, what is the procedure?

Yes. This can take the form of a security assignment, fixed charge or floating charge. Taking a fixed charge over a "blocked" account would generally be considered the most effective form of security a lender could take. A blocked account is one where the chargor is prohibited from withdrawing, transferring or otherwise dealing with the account without the prior consent of the chargee. Given that commercial borrowers generally need ready access to their bank accounts for normal trading purposes, it is more usual that the chargee will accept a floating charge over the trading bank account which allows the chargor to retain control over the cash until such time as a trigger event (e.g. an event of default under the loan documents) causes the floating charge to crystallise.

For a security assignment, a notice of assignment must be served on the account-holding bank informing them that the account has been assigned in order to create a legal security interest. In some instances, the secured party(-ies) and the account holding bank may agree an account control agreement or similar document regarding the operation of the assigned account.

A notification in relation to book debts should also be filed with Revenue, under s.1001(3) of the Taxes Consolidation Act 1997 within 21 days of the creation of charge to put it on notice of the creation of the charge and to protect the chargee's interests should the chargor default on certain tax obligations in the future.

3.6 Can collateral security be taken over shares in companies incorporated in your jurisdiction? Are the shares in certificated form? Can such security validly be granted under a New York or English law governed document? Briefly, what is the procedure?

Yes. Security can be taken over shares issued by an Irish company. There are two main types of security over shares: a legal mortgage; and an equitable mortgage. An equitable mortgage – which does not transfer legal ownership and as such does not require the lender to be registered in the company's share register as owner of the shares – is the most common. This is effected by delivery of share certificates and signed but undated share transfer forms, irrevocable proxies and various other deliverables which authorise the lender to complete the undated stock transfer form and any formalities required to become legal holder of the shares if the security becomes enforceable. Prior to the security becoming enforceable all voting rights, dividends and any communication about the shares will remain with the chargor. It is common for a lender to also take a fixed charge over shares issued by an Irish company. This is commonly taken alongside an equitable mortgage.

Shares may be issued in certificated or uncertificated form; however, ordinarily in the case of a private limited company, shares will be issued in certificated form. A public limited company whose shares are listed on the Stock Exchange will issue shares in uncertificated form (which will be held in a clearing system).

While Irish law does not strictly require that share security be granted under an Irish law governed document, it is almost always the case that Irish law-governed security is taken over shares in an Irish incorporated company, given that Irish law is likely to govern the validity and perfection requirements of the security.

3.7 Can security be taken over inventory? Briefly, what is the procedure?

Yes, this typically takes the form of a floating charge given that the chargor trading company needs to retain sufficient freedom to deal with inventory in the ordinary course of business.

3.8 Can a company grant a security interest in order to secure its obligations (i) as a borrower under a credit facility, and (ii) as a guarantor of the obligations of other borrowers and/or guarantors of obligations under a credit facility (see below for questions relating to the giving of guarantees and financial assistance)?

Yes, subject to certain provisions of the Act relating to transactions with directors and the prohibition on the provision of financial assistance (discussed at question 4.1 below), the corporate benefit rule (discussed at question 2.2 above) and solvency considerations (see question 8.2 below).

3.9 What are the notarisation, registration, stamp duty and other fees (whether related to property value or otherwise) in relation to security over different types of assets?

Subject to certain exceptions set out in the Act, particulars of charges created by an Irish company over its assets must be registered at Companies Registration Office ("**CRO**") within 21 days of its creation. The foregoing does not apply to security over certain financial assets, such as cash and shares. Particulars of any charges created by an Irish Collective Asset-management Vehicle ("**ICAV**") must be filed in the form prescribed (form CH1) with the CBI within 21 days of the creation of the security. Failure to do so will render the charge void against any liquidator or creditor of the company/ICAV. A filing fee of €40 is payable per each C1. No filing fees are incurred in respect of a form CH1. As mentioned in question 3.5 above, where security comprises a fixed charge over book debts, a notification should be made to Revenue within 21 days of the creation of the charge. No fee is incurred in respect of such notification.

Security over real property must be registered at the PRAI and security over certain other assets, such as IP, ships and aircraft, needs to be registered at applicable registries. There are no notarisation requirements for security documents under Irish law.

See section 6 regarding stamp duty.

3.10 Do the filing, notification or registration requirements in relation to security over different types of assets involve a significant amount of time or expense?

Generally no, as prescribed forms are provided in most instances and filing fees are nominal. However, the filing requirements (for example of the CRO and PRAI) are very prescriptive and any errors in the forms can cause delays, extra expense and in worst case may render the security void, necessitate an application to court for an order rectifying the particulars or require the parties to put new security in place.

3.11 Are any regulatory or similar consents required with respect to the creation of security?

Generally no, assuming the underlying contracts do not require any such third party consents. See also question 2.4 above in relation to regulated entities. Regulated entities may be restricted from creating security over certain assets.

3.12 If the borrowings to be secured are under a revolving credit facility, are there any special priority or other concerns?

Generally no, provided the security is properly perfected at the time it was granted and the underlying security documents stipulate any repayment under the facility does not serve to extinguish the security, which should be expressed to secure all amounts owing from time to time.

3.13 Are there particular documentary or execution requirements (notarisation, execution under power of attorney, counterparts, deeds)?

In general, Irish law security documents are executed as deeds to remove any concerns about the adequacy of the consideration. Other guidelines should be considered, such as Law Society practice notes and recent case law in relation to virtual completion and signing, for example the decision in the English case of *R (on the application of Mercury Tax Ltd) v Revenue and Customs Commissioners [2008] EWHC 2721*. It is generally accepted in Ireland that a previously executed signature page from one document may not be transferred to another document, even where the documents in question are simply updated versions of the same document.

4 Financial Assistance

4.1 Are there prohibitions or restrictions on the ability of a company to guarantee and/or give security to support borrowings incurred to finance or refinance the direct or indirect acquisition of: (a) shares of the company; (b) shares of any company which directly or indirectly owns shares in the company; or (c) shares in a sister subsidiary?

(a) Shares of the company

Yes, s.82(2) of the Act creates a general prohibition on the provision by a company (either directly or indirectly) of financial assistance – whether in the form of loans, guarantees, the provision of security or otherwise – for the purpose of the acquisition of its own shares or the shares in its holding company. There are exceptions and s.82(5) allows the financial assistance where the company's principal purpose in giving the assistance is not for the purpose of the acquisition or where it is incidental in relation to some larger purpose and the assistance is given in good faith. S.82(6) also provides a list of exemptions to the prohibition which includes the carrying out of a "Summary Approval Procedure" which allows an otherwise prohibited transaction to proceed.

(b) Shares of any company which directly or indirectly owns shares in the company

Yes, s.82 of the Act applies in respect of the acquisition by a company of shares in its holding company.

(c) Shares in a sister subsidiary

No – this is not applicable.

5 Syndicated Lending/Agency/Trustee/Transfers

5.1 Will your jurisdiction recognise the role of an agent or trustee and allow the agent or trustee (rather than each lender acting separately) to enforce the loan documentation and collateral security and to apply the proceeds from the collateral to the claims of all the lenders?

Yes. Syndicated lending arrangements involving the appointment of a security agent to hold any security on trust for the benefit of all lenders and any other parties entitled to benefit from the security are common in the Irish lending market. However, it is worth noting that under Irish law it is usually the receiver appointed by the lender/security agent over the secured assets who realises same on behalf of the secured parties. The Irish security document will usually provide for the appointment of a receiver and will usually provide that the receiver is the agent of the borrower rather than the lender(s)/security agent – this is noteworthy as it means that the lender/security agent is protected against any potential claims arising from the actions of the receiver as part of the enforcement.

5.2 If an agent or trustee is not recognised in your jurisdiction, is an alternative mechanism available to achieve the effect referred to above which would allow one party to enforce claims on behalf of all the lenders so that individual lenders do not need to enforce their security separately?

This is not applicable.

5.3 Assume a loan is made to a company organised under the laws of your jurisdiction and guaranteed by a guarantor organised under the laws of your jurisdiction. If such loan is transferred by Lender A to Lender B, are there any special requirements necessary to make the loan and guarantee enforceable by Lender B?

Secured debts can be assigned, transferred or novated under Irish law. As the security provider must be provided with notice of the assignment, it is not unusual for the security provider to be a party to the transfer or novation.

6 Withholding, Stamp and Other Taxes; Notarial and Other Costs

6.1 Are there any requirements to deduct or withhold tax from (a) interest payable on loans made to domestic or foreign lenders, or (b) the proceeds of a claim under a guarantee or the proceeds of enforcing security?

(a) Interest payable on loans made by domestic or foreign lenders

A company making a payment of yearly interest from an Irish source is required to withhold Irish income tax from that interest at a rate of 20%.

For these purposes, yearly interest is taken to be interest on a debt, the duration of which is at least one year, or is capable of lasting for a year or more. Interest will have an Irish source if it is paid by an Irish company or branch or the debt is secured on Irish land or buildings.

Notwithstanding the above, there are extensive exemptions under Irish tax legislation from the obligation to withhold tax where interest is paid to domestic or foreign lenders such that, in many circumstances, Irish withholding tax does not apply (assuming relevant conditions are met).

(b) Proceeds of a claim under a guarantee or the proceeds of enforcing security

From relevant case law in the area, it is not clear as to whether a payment made under a guarantee should constitute an interest payment (i.e. the guarantor being deemed to step into the shoes of the borrower) or, alternatively, whether it should to be considered a payment derived from a separate and distinct legal obligation. If the former, the analysis at (a) above should apply. Conversely, if the latter applies (such that the payment is not considered interest), Irish withholding tax should generally not apply.

With regard to the proceeds of enforcing security, to the extent that the security being disposed of is Irish lands or buildings or shares deriving their value from Irish land or buildings, there is a requirement for the purchaser to withhold tax at the rate of 15% from the proceeds. This withholding tax can be avoided if (i) the proceeds from the sale do not exceed €500,000 (€1,000,000, in the case of the disposal of residential property), or (ii) assuming certain conditions are met, the vendor applies for and obtains a CGT Clearance Certificate from Revenue and the vendor provides this certificate to the purchaser.

Where security is enforced, tax must be paid by the vendor on any gains arising in priority to any secured liability.

6.2 What tax incentives or other incentives are provided preferentially to foreign lenders? What taxes apply to foreign lenders with respect to their loans, mortgages or other security documents, either for the purposes of effectiveness or registration?

There are no tax incentives provided preferentially to foreign lenders and no taxes generally apply to their loans, mortgages and security documents for the purposes of effectiveness or registration.

No Irish stamp duty arises on the origination or novation of a loan. However, in very limited circumstances, stamp duty might arise on the acquisition of a loan by way of assignment.

6.3 Will any income of a foreign lender become taxable in your jurisdiction solely because of a loan to or guarantee and/or grant of security from a company in your jurisdiction?

Pursuant to general Irish tax rules, unless otherwise exempt, any foreign lender in receipt of Irish source interest income would be liable to Irish income tax. Notwithstanding this, Irish domestic tax legislation provides for exemptions from such income tax where the lenders are resident in EU Member States or in a territory that has signed a double taxation agreement with Ireland. In addition, an exemption may be available under a double taxation agreement itself.

Based on current Revenue guidance, a gain arising on the disposal by a foreign lender of a loan secured on Irish land or buildings may be subject to Irish capital gains tax. In addition, there may be a requirement for the purchase to withhold tax at the rate of 15% on the proceeds (please refer to question 6.1 above and the discussion there regarding withholding tax on the proceeds of enforcing security). This is a highly technical area and, where applicable, specialist advice should be sought.

6.4 Will there be any other significant costs which would be incurred by foreign lenders in the grant of such loan/guarantee/security, such as notarial fees, etc.?

No; see question 3.9 above.

6.5 Are there any adverse consequences to a company that is a borrower (such as under thin capitalisation principles) if some or all of the lenders are organised under the laws of a jurisdiction other than your own? Please disregard withholding tax concerns for purposes of this question.

Irish tax legislation does not specifically provide for thin capitalisation or similar rules. However, in certain cases, interest paid to a foreign lender which owns 75% or more of the shares in the relevant Irish borrower, could be regarded as a distribution and, therefore, would not be tax deductible for the borrower. Notwithstanding this, there are various circumstances where these rules are disapplied including where the lender is resident an EU Member State or pursuant to the provisions of a double taxation agreement.

7 Judicial Enforcement

7.1 Will the courts in your jurisdiction recognise a governing law in a contract that is the law of another jurisdiction (a "foreign governing law")? Will courts in your jurisdiction enforce a contract that has a foreign governing law?

Generally, the Irish courts respect and recognise the governing law chosen by parties to a contract. In this regard, Rome I Regulation (Regulation (EC) No. 593/2008 ("**Rome I**")) governs the position with respect to contracts relating to civil and commercial matters involving EU Member State parties and provides that, subject to certain limitations, a contract will governed by the law chosen by the parties. The choice of law in contract disputes falling outside Rome

I will be determined by common law, unless there is a specific law or convention which deals with the particular contract in question. Again, the common law generally recognises and enforces the choice of governing law provided for in the contract, subject to certain qualifications such as where there are public policy issues.

The Irish courts can enforce a contract that has a foreign governing law. However, the party seeking to rely on the foreign law will need to provide evidence to the court to prove to the satisfaction of the court what the foreign law is. Generally, the Irish court will not research the foreign law.

7.2 Will the courts in your jurisdiction recognise and enforce a judgment given against a company in New York courts or English courts (a "foreign judgment") without re-examination of the merits of the case?

Generally, yes. The recognition and enforcement of foreign judgments in Ireland is determined by international conventions and treaties. In this regard and broadly speaking, there are three categories of jurisdiction being: (i) judgments from states within the EU; (ii) judgments from states which are party to the Lugano Convention; and (iii) all states not within the EU or not a party to the Lugano Convention. Irrespective of which category of jurisdiction a judgment falls within, an application can be made to the Irish courts to have the foreign judgment recognised in Ireland without re-litigating the facts of the case.

As New York falls within category (iii), an application can be made to have the foreign judgment recognised in Ireland. In order for the judgment to be deemed enforceable in Ireland, the Irish courts will have to determine, amongst others, that: (i) the court in which the judgment is made had competent jurisdiction; (ii) the judgment is for a definite sum of money; (iii) the judgment is final and conclusive; and (iv) it is not contrary to public policy in Ireland.

As England is still an EU Member State, a judgment made in England can currently be enforced in Ireland without any declaration of enforceability being required pursuant to Regulation (EU) No. 1215/2012 ("**Brussels I**"). In this regard, judgments made in England are effectively treated like a judgment made by a court in Ireland. The position will have to be reviewed post-Brexit.

7.3 Assuming a company is in payment default under a loan agreement or a guarantee agreement and has no legal defence to payment, approximately how long would it take for a foreign lender to (a) assuming the answer to question 7.1 is yes, file a suit against the company in a court in your jurisdiction, obtain a judgment, and enforce the judgment against the assets of the company, and (b) assuming the answer to question 7.2 is yes, enforce a foreign judgment in a court in your jurisdiction against the assets of the company?

The timing for obtaining a judgment on foot of a debt outstanding pursuant to a loan agreement or guarantee will firstly depend on the monetary amount for which the creditor is seeking judgment as the court system is divided into a number of courts with each having different monetary jurisdiction. Each of the courts also has their own distinct rules but each has a special procedure available to creditors to recover a debt or liquidated demand. Furthermore, obtaining judgment will depend on whether the debtor enters an appearance to the proceedings or not. In very broad terms, where debt proceedings are brought against an Irish company for a debt owing to a foreign lender of over €75,000 and the Irish company does not enter an appearance to the proceedings, judgment may be obtained within 6–9 months of the proceedings issuing.

Enforcement of the judgment will depend on the assets which the Irish company has and there are a number of methods of enforcement. In relation to immoveable property/land, a foreign lender can register the judgment as a judgment mortgage over any property/land owned by the Irish company in Ireland following which it may be in a position to appoint a receiver over the property/land. In relation to moveable property, an enforcement order can be obtained pursuant to which such assets of the Irish company may be seized. Furthermore, if it is believed that the Irish company is insolvent, a foreign lender who has obtained judgment can issue a statutory demand to the company calling on it to discharge the amount due pursuant to the judgment within 21 days failing which a petition can be brought to have the company wound up and have all assets liquidated to attempt to satisfy all creditors of the Irish company. The Irish courts will generally only order the winding up of the Irish company if it is satisfied that the Irish company is insolvent. It may take 2–3 months following the expiry of the 21-day demand letter for a liquidator to be appointed over the Irish company.

In terms of the time period for enforcing a foreign judgment, this will, as mentioned under question 7.2 above, depend on the jurisdiction in which the judgment has been made. Where the judgment has been given in an EU Member State, Brussels I applies and the judgment against the Irish company is essentially enforceable as if it were a judgment made by an Irish court meaning that the enforcement procedures, as described above, can be invoked.

In relation to judgments made by non-EU Member States, an application has to be made to the Irish courts before the judgment can be enforceable. Where the judgment has been given in a state which is a party to the Lugano Convention (being EU Member States, Iceland, Norway, and Switzerland), an application is made to have the foreign judgment declared enforceable in Ireland. It may take 1–2 months to have the foreign judgment declared enforceable following which it can be enforced against an Irish company as set out above. In relation to judgments from non-EU and non-Lugano Convention states, an application can be made to have the foreign judgment recognised in Ireland. However, unlike a judgment from a state which is a party to the Lugano convention, the application to have the judgment recognised is made on notice to the Irish company which brings with it practical issues such as serving the proceedings. Furthermore, the debtor, being on notice of the application, may attend and oppose the application to have the judgment recognised. Therefore, whilst the application may get a first return date within 1–3 months from the date of issuing proceedings, the application may not proceed on the first return date if it is opposed as the debtor will be given the opportunity to challenge the application and the foreign judgment holder could be significantly delayed in having the judgment recognised depending on the extent of the challenge. Once the judgment has been declared enforceable or is recognised by the Irish courts, it can be enforced as set out above.

7.4 With respect to enforcing collateral security, are there any significant restrictions which may impact the timing and value of enforcement, such as (a) a requirement for a public auction, or (b) regulatory consents?

Generally no, the circumstances in which a lender can enforce its security under Irish law are largely dependent on the terms of the underlying security documents. The most common method of enforcement against a corporate lender is the appointment of a receiver or for the charge-holder to become mortgagee in possession of the charged property. S.439 of the Act provides that in selling property of a company, a receiver must exercise all reasonable care to obtain the best price reasonably obtainable for the property as at the time of sale. This may involve recourse to expert opinions and valuations of company property which, depending on the circumstances, could lead to a recommendation that a public auction is necessary in order to achieve the best available price for the respective property. This would have a consequent effect on the timing of any enforcement. The timing of enforcement could also be impacted by the appointment of an examiner (see question 7.6 below).

7.5 Do restrictions apply to foreign lenders in the event of (a) filing suit against a company in your jurisdiction, or (b) foreclosure on collateral security?

No, foreign lenders are subject to the same statutory limitation periods within which a claim must be brought and the same rules of court as those imposed on Irish lenders seeking to file suit against a company and enforce security through the courts.

7.6 Do the bankruptcy, reorganisation or similar laws in your jurisdiction provide for any kind of moratorium on enforcement of lender claims? If so, does the moratorium apply to the enforcement of collateral security?

Yes, Irish companies may enter examinership, which is a court-enforced moratorium on creditor action which allows a brief period during which a company can be restructured. This process usually results in creditor balances being reduced, while intangible assets of the company are protected, investment is obtained and the company can continue to trade. The examiner is typically appointed for 70 days (but this may be extended to 100 days or in exceptional cases, longer) during which time the lender will not be permitted to take any enforcement action against the security provider, save in respect of a security financial collateral arrangement as defined in the Financial Collateral Arrangement Regulations. Pursuant to the Insolvency Regulation, this moratorium is also ineffective in relation to rights *in rem* of creditors or third parties by way of security in assets situated outside of Ireland and does not affect the right of creditors to exercise their right of set-off against the claims of a debtor.

In addition to the above, there are certain other laws and codes that apply in the consumer lending sector (including enforcement of such loans), many of which must be adhered to by foreign lenders lending into Ireland.

7.7 Will the courts in your jurisdiction recognise and enforce an arbitral award given against the company without re-examination of the merits?

Generally, yes – subject to certain conditions being satisfied. Ireland ratified the New York Arbitration Convention under s.24 of the Arbitration Act 2010. The Convention provides for the recognition and enforcement of domestic and international arbitral awards. Pursuant to s.23 of the Arbitration Act 2010, an award made by an arbitral tribunal under an arbitration agreement shall be enforceable in this jurisdiction either by action or leave of the High Court. For enforcement of foreign arbitral awards, the award must be in writing and be signed by the arbitrator or arbitrators. In arbitral proceedings with more than one arbitrator, the signatures of the majority of the tribunal will suffice, so long as the reason for any omitted signature is set out. The award should also state its date and the place of arbitration.

8 Bankruptcy Proceedings

8.1 How does a bankruptcy proceeding in respect of a company affect the ability of a lender to enforce its rights as a secured party over the collateral security?

The capacity of a lender to enforce its rights as a secured party over collateral security is not affected by liquidation proceedings entered into by a company. Should the enforcement of a security fail to discharge the total debt owed to the lender, the balance may be claimed in the liquidation process. However, the rights of a secured lender will be affected where the company has entered examinership proceedings, as discussed above.

8.2 Are there any preference periods, clawback rights or other preferential creditors' rights (e.g., tax debts, employees' claims) with respect to the security?

Yes. Pursuant to s.597 of the Act, a floating charge will be invalidated where it has been created within 12 months of the company entering into insolvency proceedings unless it is proven that the company was solvent immediately after the creation of the charge. This period will be extended to two years where the floating charge has been created in favour of a connected person.

The Act also provides for certain clawback rights where a fraudulent or unfair transfer of company property has occurred. For example, pursuant to s.604 of the Act, any transfer of company property to a creditor will be invalidated where such transfer was made with the view to securing a preference over other creditors in the company and was made within six months of the insolvency of the company (period will be extended to two years where the transfer was made to a connected person).

With regard to preferential creditors, the expenses relating to an examinership or liquidation, together with certain taxes, rates and employee claims have priority over floating charge security holders.

8.3 Are there any entities that are excluded from bankruptcy proceedings and, if so, what is the applicable legislation?

All trading Irish companies are subject to insolvency proceedings under the Act.

8.4 Are there any processes other than court proceedings that are available to a creditor to seize the assets of a company in an enforcement?

Secured creditors may exercise set-off rights and appoint receivers without recourse to court proceedings. Unsecured creditors cannot seize secured assets of a company without a court order authorising such; however, unsecured creditors may be able to repossess goods/assets which have not been paid for in full by the company in question and which are subject to a valid retention of title clause.

9 Jurisdiction and Waiver of Immunity

9.1 Is a party's submission to a foreign jurisdiction legally binding and enforceable under the laws of your jurisdiction?

Yes, it is.

9.2 Is a party's waiver of sovereign immunity legally binding and enforceable under the laws of your jurisdiction?

Yes, Ireland accepts the recognised principles of international law as the rule of conduct in its relations with other States and accordingly, in principle, an Irish court will recognise a party's waiver of sovereign immunity.

10 Licensing

10.1 What are the licensing and other eligibility requirements in your jurisdiction for lenders to a company in your jurisdiction, if any? Are these licensing and eligibility requirements different for a "foreign" lender (i.e. a lender that is not located in your jurisdiction)? In connection with any such requirements, is a distinction made under the laws of your jurisdiction between a lender that is a bank *versus* a lender that is a non-bank? If there are such requirements in your jurisdiction, what are the consequences for a lender that has not satisfied such requirements but has nonetheless made a loan to a company in your jurisdiction? What are the licensing and other eligibility requirements in your jurisdiction for an agent under a syndicated facility for lenders to a company in your jurisdiction?

In general, commercial lending is not a regulated activity in Ireland and, unless the lender is a bank, there is generally no requirement to obtain a licence. The regulatory regime in Ireland relating to lending generally focuses on consumer lending. However, this does not operate as a blanket exemption for commercial lenders from all reporting and regulatory requirements. For example:

- the Credit Reporting Act 2013 requires that, from 31 March 2018, lenders – both regulated and unregulated – are obliged to collect and report to the CBI certain information relating to credit advanced to non-consumer borrowers, which includes companies, limited liability partnerships, etc.; and
- the Consumer Protection (Regulation of Credit Servicing) Act 2015 provides that unregulated lenders which purchase consumer loans or loans to small- or medium-sized enterprises ("**SMEs**") from a lender which was regulated by the CBI (or its equivalent in another EU country) must appoint a credit servicing firm who is regulated by the CBI to service the loans.

Irish anti-money laundering laws and, in some cases, CBI statistical reporting requirements would typically also apply to lenders.

In addition, many lenders may find that they fall within the scope of regulation by virtue of other activities carried out by them, for example taking deposits. Any lender in Ireland which provides banking services, which includes the taking of deposits, is required, on application to the CBI, to obtain a licence from the European Central Bank. Carrying on a banking business in Ireland without a licence is a criminal offence. Banks licensed in another EU Member State may also be required to passport into Ireland in order to carry on a lending activity in Ireland that would otherwise be unregulated.

There are no specific licensing requirements that apply to a security agent under a syndicated facility. However, such an agent would be subject to regulation if it carries on any regulated activities, for example accepting deposits.

As regards the position of a foreign lender, if lending to persons in Ireland, they would generally be subject to the same conduct of business rules as an Irish lender, and are also required to hold the appropriate licence/authorisation if carrying on a regulated activity (albeit their regulatory status in their home country may have a bearing on the latter, e.g. passporting rights if carrying on passportable activities).

11 Other Matters

11.1 Are there any other material considerations which should be taken into account by lenders when participating in financings in your jurisdiction?

As mentioned above, the regulatory regime in Ireland relating to lending largely focuses on lending to natural persons at present and there is various legislation, regulation and codes of which lenders would need to be cognisant if originating loans to such persons (or acquiring loans originated to such persons or to SMEs).

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The authors would like to acknowledge the assistance of their colleague Elaine Cummins in the preparation of this chapter. Elaine acts on a wide range of banking transactions for both financial institutions and corporates, both domestic and foreign, on an extensive range of banking law matters.

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DILLON EUSTACE

The Dillon Eustace banking team advises domestic and international financial institutions and corporates, for both transactional work and banking regulatory matters.

Transactional expertise includes advising both lenders and borrowers on credit facilities (including term, revolving and composite facilities and whether on a syndicated, club or bi-lateral basis) as well as on associated security, credit support and enforcement issues.

In addition to secured property lending, we work on debt financings for investment funds and pension funds and acquisition finance for M&A transactions.

Our regulatory practice includes advising on the establishment of banks and branches of EU and non-EU credit institutions in Ireland and on their acquisition and sale. We also advise on e-banking, consumer credit and banking regulation and licensing generally.

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1 Overview

1.1 What are the main trends/significant developments in the lending markets in your jurisdiction?

With a view to increasing the competitiveness of the Italian lending market during the credit crunch, a number of laws have been introduced by the Italian legislator in recent years. In particular:

- new players have been given access to the lending market by including them among the entities licensed to lend directly to Italian entities (for further details see Section 10);
- non-listed companies have been given access to bond financings; and
- the tax regime has been rendered more favourable by extending the application of certain tax benefits (i.e. the exemption from withholding tax over interest and the substitutive tax regime).

Furthermore, new and more flexible types of *in rem* security interests have been introduced into the Italian legal system:

- the non-possessory pledge over movable assets (for further details see question 3.7); and
- the security transfer of real property (*patto marciano*) (for further details see question 3.3).

1.2 What are some significant lending transactions that have taken place in your jurisdiction in recent years?

A EUR10bn new revolving credit facility granted by a pool of banks including Mediobanca, as documentation agent, to Enel S.p.A. and its Dutch subsidiary Enel Finance International N.V. to replace the previous EUR9.4bn credit line renegotiated in February 2015.

A EUR3.4bn senior facilities agreement consisting of a EUR3bn amortising term loan and a EUR400m revolving credit facility granted to Wind Tre as part of the Italian mobile communications company's EUR10bn refinancing of debt at lower costs and to optimise its financial structure. The jumbo refinancing also comprised a EUR7.3bn issuance of high yield senior secured notes, in a combination of euro-denominated fixed and floating rate notes and dollar-denominated fixed rate notes, issued pursuant to Rule 144A and Regulation S under the Securities Act. The issuance represents the largest single issuance of euros by a single borrower and the floating rate notes are one of the largest such tranche ever issued.

A EUR330m refinancing of a bridge loan granted by a pool of banks (advised by Allen & Overy) comprising Banca IMI, BNP Paribas and Mediobanca to Italian listed company Cementir S.p.A. The refinancing is part of the financing contract stipulated in October 2016 to fund the cement producer's acquisitions of Compagnie des Ciments Belges (CCB) and the business division of Sacci as well as to refinance existing credit facilities and meet the group's working capital requirements.

A loan facility granted by a pool of banks (advised by Allen & Overy) comprising Mediobanca, as coordinator and facility agent, and including BNL BNP Paribas Group and UniCredit, to GVS S.p.A., a leading Italian microfiltration company, in connection with its acquisition of American company Kuss Filtration Inc from the private equity firm Industrial Opportunity Partners.

2 Guarantees

2.1 Can a company guarantee borrowings of one or more other members of its corporate group (see below for questions relating to fraudulent transfer/financial assistance)?

An Italian company can guarantee borrowings of one or more other members of its corporate group subject to certain limits. See questions 2.2, 2.5 and Section 4 for further details.

2.2 Are there enforceability or other concerns (such as director liability) if only a disproportionately small (or no) benefit to the guaranteeing/securing company can be shown?

In order for an Italian company to grant a guarantee or security there must be a corporate benefit. Whilst corporate benefit for a downstream guarantee or security is usually self-evident, the validity and effectiveness of an upstream or cross-stream guarantee or security granted by an Italian company depends on the existence of an actual benefit as direct or indirect "consideration" for entering into the guarantee or security.

Undervalue guarantees or security may be a breach of the directors' duties to act in the interests of the company, which can sometimes render them personally liable. The "business judgment" rule is strict and the risk of director liability can be high. Common directorships (conflicts of interest) increase risk – arrange for independent boards, if possible. Guarantees by companies whose directors have an interest in the guaranteed or secured company have increased risk.

Italian law does not, except for certain limited and specific purposes (such as antitrust law), recognise the concept of the "group" or "group interest" and, therefore, the group interest in a transaction is not a sufficient ground to exclude the application of the *ultra vires doctrine*.

Articles 2497 *et seq*. of the Italian civil code set out the general rules applying to any entity which, by virtue of a controlling or similar relationship (not necessarily granted by a majority stake), exercises the activity of direction and coordination (*attività di direzione e coordinamento*) over the companies in its group. In particular, article 2497 provides that if the holding company, in the exercise of the activity of direction and coordination, breaches the principles of the correct corporate and entrepreneurial management in order to pursue its own interest (or the interest of a third party) it is directly liable *vis-à-vis* the shareholders of the subsidiary for compromising the profitability of the subsidiary, as well as towards the subsidiary's creditors for having put at risk the integrity of the share capital of the subsidiary. In the case of bankruptcy of the subsidiary, the action pertaining to the creditors against the holding company may be exercised by the insolvency receiver of the bankrupt subsidiary.

2.3 Is lack of corporate power an issue?

According to articles 2384 and 2475-*bis* of the Italian civil code, lack of corporate power deriving from the by-laws or a corporate resolution of a joint stock company or limited liability company, as well as the existence of a director's personal or a third party's interest in a transaction, cannot be raised against a counterparty unless it proves that the counterparty has acted for the purpose of damaging the company.

2.4 Are any governmental or other consents or filings, or other formalities (such as shareholder approval), required?

The granting of a guarantee must be permitted under the by-laws of the company. Management bodies' and shareholders' resolutions may be required, in accordance with the by-laws.

The granting of guarantees *vis-à-vis* the public is considered a form of lending and, as a consequence, it is an activity that can be carried out exclusively by entities licensed to carry out lending activities in Italy. For further details see Section 10.

2.5 Are net worth, solvency or similar limitations imposed on the amount of a guarantee?

The most relevant limits on the amount of a guarantee that can be issued are:

- limits arising from financial assistance provisions. For further details see Section 4;
- limits arising from corporate benefit rules. For further details see question 2.2 above; and
- pursuant to article 1938 of the Italian civil code, the guarantor may only guarantee future obligations if an overall maximum guaranteed amount is set.

2.6 Are there any exchange control or similar obstacles to enforcement of a guarantee?

Under Italian law there are no exchange control or similar restrictions to the enforcement of a guarantee.

3 Collateral Security

3.1 What types of collateral are available to secure lending obligations?

The form of collateral mainly used in Italian financing transactions are the following:

- Mortgage over real property, ships or aircrafts.
- Security transfer of real property (*patto marciano*).
- Special privilege over certain movable assets.
- Pledge over a private company's shares.
- Pledge over marketable securities.
- Pledge or assignment by way of security of receivables.
- Pledge over bank accounts.
- Pledge over intellectual property.
- Pledge over goods.
- Non-possessory pledge over movable assets (subject to the implementation of the relevant register).

3.2 Is it possible to give asset security by means of a general security agreement or is an agreement required in relation to each type of asset? Briefly, what is the procedure?

Italian law does not provide for a universal corporate security interest covering all existing and future assets generically. But most common assets can be the subject of separate security.

3.3 Can collateral security be taken over real property (land), plant, machinery and equipment? Briefly, what is the procedure?

Real property mortgage

The mortgage deed must be signed before an Italian notary and the mortgaged property must be specified in detail. After-acquired property, including unplanned buildings, must be mortgaged when acquired. The deed should be registered in the local land registry to be enforceable against third parties (renewable after 20 years). Priority ranks from the date and time of registration. There is no advance priority reservation.

Security transfer of immovable property (*patto marciano*)

A loan granted to an entrepreneur by a bank, or another entity authorised to grant loans to the public in Italy, may be secured by transferring to the creditor (or to a company in the creditor's group authorised to purchase, hold, manage and transfer rights *in rem* in immovable properties), the ownership of a property or of another immovable right of the entrepreneur or of a third party. The transfer is subject to the condition precedent of the debtor defaulting.

Special privilege over certain movable assets

The special privilege deed must be signed before an Italian notary and can only be granted by the debtor to secure facilities with an overall maturity longer than 18 months granted to it by Italian or other EU banks.

The special privilege may cover: (a) existing and future equipment, concessions and produced goods of the enterprise; (b) raw materials, semi-manufactured goods, stock, finished goods, fruit, livestock and goods; (c) goods purchased with the loan in respect of which the special privilege is intended to be granted; and (d) present or future receivables arising from the sale of the assets and goods listed in (a) to (c).

For validity against creditors, the special privilege must be registered in the special register kept at the competent local court.

3.4 Can collateral security be taken over receivables? Briefly, what is the procedure? Are debtors required to be notified of the security?

Present and future receivables arising under an existing contract can be pledged or assigned.

Special rules apply to receivables against public authorities.

The deed of assignment of receivables arising out of rental leases having a remaining term exceeding three years must be executed in front of an Italian notary and registered.

Receivables arising under future contracts must be pledged/assigned upon their coming into existence. See Section 2 for the implications.

The deed of pledge must be in written form.

Formalities for rendering the pledge/assignment enforceable against third party creditors of the pledgor/assignor (including a receiver in the pledgor/assignor's insolvency) are either a notice of the assignment to, or an express acknowledgment by, the obligor, in each case bearing a date certain at law (*data certa*) pursuant to Italian law.

3.5 Can collateral security be taken over cash deposited in bank accounts? Briefly, what is the procedure?

A pledge can be granted over cash deposited in bank accounts. For the perfection formalities see question 3.4. New formalities must be put in place every time the account balance changes. There is a risk – also for claw-back purposes – that the pledge purported to be created over each increase in the balance of the relevant account may not exist until the above formalities are carried out and that each pledge should be considered a new and different pledge for all intents and purposes. See Section 2 for the implications. Any utilisation of the money standing to the credit of a pledge account will likely amount to a release of the relevant sum from the security interest.

3.6 Can collateral security be taken over shares in companies incorporated in your jurisdiction? Are the shares in certificated form? Can such security validly be granted under a New York or English law governed document? Briefly, what is the procedure?

<u>Pledge over shares of a *società per azioni*</u>

The deed of pledge can be non-notarial but must bear a certain date. The pledge must be: (i) registered on the certificates representing the shares – whether by endorsement (*girata*) performed by the pledgor or by annotation performed by a director of the issuing company; and (ii) annotated in the shareholders' book of the company for enforceability against, respectively, the creditors and the issuing company. The creditor (directly or through a depository) must take possession of the pledged share certificates.

The pledge can cover distributions, new issues of shares and exchanges. The creditor can (and typically does) authorise the debtor to exercise voting rights and collect distributions until the occurrence of a default. Where the creditor has voting rights, consider consolidation, loss of group tax relief, etc.

The market seems to tolerate the practice of granting security on Italian shares by a foreign law governed document; however, for the principle of *lex rei sitae*, the pledged shares must be transferred to the country of applicable law. Please also take into account the perfection formalities required.

<u>Pledge over quotas of a *società a responsabilità limitata*</u>

The quotas are not represented by certificates. The deed of pledge must be in notarial form and should be registered with the companies register in order for the pledge to be enforceable against third parties. Significant tax implications arise in connection with such registration (for further details see question 6.4).

The pledge must be annotated in the quotaholders' book of the company in order to be enforceable against the issuing company.

3.7 Can security be taken over inventory? Briefly, what is the procedure?

<u>Pledge over goods with dispossession</u>

The deed of pledge can be non-notarial but must bear a certain date. This can cover present movable and unregistered assets of the company. Future assets must be separately pledged under new security. See Section 2 for the implications. A right of substitution of the pledged assets may be provided, subject to the value of the replacing goods not exceeding the value of the replaced ones. As from the date of perfection of the pledge, the goods are not available to the pledgor without the cooperation of the secured creditor. The goods must at all times be identifiable.

Special rules apply if the assets are deposited with a *magazzino generale*.

<u>Non-possessory pledge over movable assets</u>

At the present date it is not possible to create such a pledge since the relevant electronic register set up by the Italian tax Authority (*Agenzia delle Entrate*) has not been created. Once this is available, the non-possessory pledge may be established:

- to secure financings, whether present or future, granted in order to run the business. A maximum secured amount must be set;
- over unregistered movable assets (including receivables and other immaterial assets), whether existing or future and whether determined or determinable, also by making reference to one or more categories of products or to an overall value; and/or
- by entry on the aforesaid electronic register. From the date of registration, the pledge acquires its ranking and is enforceable against third parties and in insolvency proceedings. The entry lasts for ten years and is renewable before expiry.

The pledged assets can be transformed or sold. The pledge is automatically transferred onto the product resulting from the transformation, the consideration deriving from the sale or the substitute asset purchased with that consideration, as applicable, without giving rise to the creation of new security.

3.8 Can a company grant a security interest in order to secure its obligations (i) as a borrower under a credit facility, and (ii) as a guarantor of the obligations of other borrowers and/or guarantors of obligations under a credit facility (see below for questions relating to the giving of guarantees and financial assistance)?

Yes. For limitations see questions 2.2, 2.5 and Section 4.

3.9 What are the notarisation, registration, stamp duty and other fees (whether related to property value or otherwise) in relation to security over different types of assets?

Excluding taxes (in this respect see Section 6), the fees that could arise in relation to securities relate to the following:

- Notarisation may be necessary for the validity and enforceability of a security agreement (e.g. real property mortgages) or to certify the date of the security agreement.
- Stamp duties apply to security agreements which are subject to registration. Stamp duties are based on the number of pages of a security document and are generally not material.

3.10 Do the filing, notification or registration requirements in relation to security over different types of assets involve a significant amount of time or expense?

Yes, depending on the type of security. However, certain security must be registered in Italy for perfection purposes. In such cases, Italian registration taxes will apply.

3.11 Are any regulatory or similar consents required with respect to the creation of security?

In general, no consent is required. However, the consent to the assignment of receivables against public authorities may be required.

3.12 If the borrowings to be secured are under a revolving credit facility, are there any special priority or other concerns?

No, there are not.

3.13 Are there particular documentary or execution requirements (notarisation, execution under power of attorney, counterparts, deeds)?

Certain security documents must be executed in notarial form. For notarial security documents the parties should provide evidence of their signatory powers.

4 Financial Assistance

4.1 Are there prohibitions or restrictions on the ability of a company to guarantee and/or give security to support borrowings incurred to finance or refinance the direct or indirect acquisition of: (a) shares of the company; (b) shares of any company which directly or indirectly owns shares in the company; or (c) shares in a sister subsidiary?

(a) Shares of the company

An Italian company, whether an S.p.A. or S.r.l., is prohibited from providing financial assistance (i.e. granting a loan or providing a guarantee or security) to any entity for financing or refinancing the direct or indirect acquisition or subscription of its own shares. Whitewash for S.p.A. is allowed under certain conditions.

Various structures have been implemented in order to mitigate the impact of the financial assistance prohibition. The most frequently used structure involves the merger of the target company into the acquisition vehicle after closing. However, any risk of voidness must be assessed on a case-by-case basis by looking at the transaction as a whole.

(b) Shares of any company which directly or indirectly owns shares in the company

The same rules described in sub paragraph (a) above apply.

(c) Shares in a sister subsidiary

In principle, there are no restrictions with respect to security or guarantees granted over shares in a sister subsidiary (subject, in any case, to the corporate benefit analysis). However, any risk of voidness must be assessed on a case-by-case basis by looking at the transaction as a whole.

5 Syndicated Lending/Agency/Trustee/Transfers

5.1 Will your jurisdiction recognise the role of an agent or trustee and allow the agent or trustee (rather than each lender acting separately) to enforce the loan documentation and collateral security and to apply the proceeds from the collateral to the claims of all the lenders?

Security must be granted to, and perfected in favour of, each creditor individually. Trusteeship and parallel debt arrangements are generally not recognised in Italy. In syndicated loans secured creditors appoint an agent on the basis of a mandate (*mandato con rappresentanza*). The agent is entitled to exercise the secured creditors' rights and to enforce the security on the basis of the intercreditor arrangements. However, each secured creditor should intervene in the judicial enforcement.

5.2 If an agent or trustee is not recognised in your jurisdiction, is an alternative mechanism available to achieve the effect referred to above which would allow one party to enforce claims on behalf of all the lenders so that individual lenders do not need to enforce their security separately?

See question 5.1.

5.3 Assume a loan is made to a company organised under the laws of your jurisdiction and guaranteed by a guarantor organised under the laws of your jurisdiction. If such loan is transferred by Lender A to Lender B, are there any special requirements necessary to make the loan and guarantee enforceable by Lender B?

Perfection requirements change depending on whether the transfer made by Lender A to Lender B is by transfer of contract (*cessione di contratto*) or assignment of receivables (*cessione del credito*).

A transfer of contract requires the consent of all parties, including the assigned debtor and guarantor. This can be provided ahead of the assignment, by including an express consent in the relevant loan agreement or guarantee, as applicable.

An assignment of receivables:

- does not require the consent of the assigned debtor and guarantor, unless the loan agreement or the guarantee, as applicable, expressly prohibits the assignment of the receivables arising therefrom; and
- must be notified to the debtor and the guarantor, as applicable, or accepted by it.

In order for the assignment to be enforceable against third parties, the notice or acceptance must bear a date certain at law pursuant to Italian law.

If the loan is secured, perfection formalities will need to be carried out in order to render the transfer of such security interest enforceable against third parties. However, if the assignment of the loan is carried out pursuant to article 58 of Legislative Decree No. 385/1993 (the "Italian Banking Act") or to an Italian securitisation vehicle pursuant to Law No. 130/1999 (the "Italian Securitisation Law"), no perfection formalities need to be carried out.

Should the receivables be governed by a law other than Italian law, the provisions of Article 14 of Council Regulation (EC) No. 593/2008 of 17 June 2008 on the Law Applicable to Contractual Obligations (the "Rome I Regulation") will apply, pursuant to which such law will govern the assignability of the receivables and the rights and obligations between the assignee and the assigned debtors (including the enforceability of the assignment against the assigned debtors).

6 Withholding, Stamp and Other Taxes; Notarial and Other Costs

6.1 Are there any requirements to deduct or withhold tax from (a) interest payable on loans made to domestic or foreign lenders, or (b) the proceeds of a claim under a guarantee or the proceeds of enforcing security?

As a general rule, no withholding tax is chargeable on interest payable on loans made to resident lenders. A withholding tax (generally at the rate of 26%) is chargeable on interest payable to a non-Italian resident lender (unless it is lending through an Italian branch to which the loan is effectively connected). The withholding tax can be reduced under the provisions of the double tax treaty applicable between Italy and the country of residence of the beneficial owner of the interest.

Moreover, no withholding tax applies to interest paid by Italian entrepreneurs on medium/long term loans if extended, *inter alia*, by credit institutions established in EU and institutional investors subject to regulatory supervision established in countries that allow an adequate exchange of information with Italy.

In case of proceeds of a claim under a guarantee or proceeds of enforcing security, in accordance with one interpretation of Italian tax law, any such payment would be equal to the payment under the loan and therefore may be subject to the same withholding tax.

6.2 What tax incentives or other incentives are provided preferentially to foreign lenders? What taxes apply to foreign lenders with respect to their loans, mortgages or other security documents, either for the purposes of effectiveness or registration?

Substantial registration taxes, depending on the nature of the security and the features of the facility agreement, may apply. In certain cases a substitutive tax regime (the **Substitutive Tax**) may be applicable in order to reduce the indirect taxes ordinarily applicable to the loan and the security package (e.g. registration and mortgage taxes).

The Substitutive Tax (generally at the rate of 0.25%) applies, upon the option of the parties, if the loan: (i) is granted, *inter alia*, by Italian banks (including Italian permanent establishments of EU and non-EU banks), EU banks, Italian securitisation companies and EU collective investment funds; (ii) is entered into within the territory of Italy; and (iii) has a duration exceeding 18 months.

Where Substitutive Tax does not apply, the securities are subject to indirect taxes varying from EUR 200 (where the guarantor is securing its own obligations) to 0.5% (where third parties' obligations are being secured) while mortgage tax is generally levied at a 2% rate on real estate mortgages.

Registration taxes may not be payable if the security agreement is executed outside Italy (unless specific events, occur, e.g. case of use, explicit reference or voluntary registration). However, certain security must be registered in Italy for perfection purposes, e.g. real estate mortgages, special privileges (certain movables), pledges of quotas of an S.r.l., pledges of intellectual property and mortgages of ships and aircraft. In particular, the granting of a pledge over quotas of an S.r.l. attracts registration tax equal to 0.5% of the amount of the secured obligations where third parties' obligations are being secured.

6.3 Will any income of a foreign lender become taxable in your jurisdiction solely because of a loan to or guarantee and/or grant of security from a company in your jurisdiction?

Generally, a foreign lender grating a loan to an Italian resident entity does not meet the concept of permanent establishment and therefore the lender remains a taxpayer not resident in Italy for fiscal purposes.

Please see question 6.1 above for the withholding tax treatment of interest paid by an Italian resident entity to foreign lenders.

6.4 Will there be any other significant costs which would be incurred by foreign lenders in the grant of such loan/guarantee/security, such as notarial fees, etc.?

Notarisation may be necessary for the validity of certain security agreements (e.g. real property mortgages) or to certify the date of the security agreement. Notarial fees can be material, especially in case of real property mortgages, although they are generally negotiable with the public notary.

6.5 Are there any adverse consequences to a company that is a borrower (such as under thin capitalisation principles) if some or all of the lenders are organised under the laws of a jurisdiction other than your own? Please disregard withholding tax concerns for purposes of this question.

Starting from 2016, no specific adverse consequences are provided by the Italian law in case of loans extended by foreign lenders (until 2015 a specific black list costs regime was applicable).

7 Judicial Enforcement

7.1 Will the courts in your jurisdiction recognise a governing law in a contract that is the law of another jurisdiction (a "foreign governing law")? Will courts in your jurisdiction enforce a contract that has a foreign governing law?

According to article 3 of Rome I Regulation on the law applicable to contractual obligations, the parties to an agreement are generally free to choose the law governing the agreement.

However, pursuant to article 3.3 of Rome I Regulation, if a contract is in breach of Italian public policy (*ordine pubblico*) or mandatory rules (*norme di applicazione necessaria*), Italian Courts will not enforce such agreement.

7.2 Will the courts in your jurisdiction recognise and enforce a judgment given against a company in New York courts or English courts (a "foreign judgment") without re-examination of the merits of the case?

European Countries

In particular, article 36 of EU Regulation No. 1215/2012 (the "Recast Brussels Regulation") provides that a judgment issued by the Court of a Member State shall be recognised in the other Member States "without any special procedure being required". While England is still part of the European Union, the Recast Brussels Regulation continues to apply.

Non European Countries (E.g. New York)

The acknowledgment and enforcement of decisions issued by courts belonging to jurisdictions outside of the European Union is generally governed by Law No. 218 of 31 May 1995. The enforcement of a foreign decision in the Italian territory requires the filing of a petition before the Court of Appeal of the place where the enforcement shall then take place. Such proceedings usually last six months to one year, and the order authorising the enforcement of the foreign decision in Italy fully entitles the creditor to seek enforcement over the debtor's assets.

7.3 Assuming a company is in payment default under a loan agreement or a guarantee agreement and has no legal defence to payment, approximately how long would it take for a foreign lender to (a) assuming the answer to question 7.1 is yes, file a suit against the company in a court in your jurisdiction, obtain a judgment, and enforce the judgment against the assets of the company, and (b) assuming the answer to question 7.2 is yes, enforce a foreign judgment in a court in your jurisdiction against the assets of the company?

The average length of first instance proceedings in Italy is approximately four years. Although a judgment issued at the end of first instance proceedings is normally enforceable, it would take approximately 10 years to obtain a final and binding judgment (due to appeals, the complexity of the case at stake or a court with a busy docket).

The Recast Brussels Regulation, in the absence of any contestation raised by the defendant, should theoretically speed up the proceedings aimed at the recognition and enforcement of a judgment granted in a Member State. On the contrary, the so-called acknowledgment proceedings of a judgment granted in a non-European country usually last one year to one year and half, depending on the agenda of the Court and issues relating to the complexity of the case at stake.

Enforcement proceedings last approximately three to four years and the duration is largely linked to the specific type of assets foreclosed by the creditor.

7.4 With respect to enforcing collateral security, are there any significant restrictions which may impact the timing and value of enforcement, such as (a) a requirement for a public auction, or (b) regulatory consents?

The enforcement of collateral security normally depends on the nature of the secured assets as well as on the ranking of the security itself. In particular, a security interest may be enforced:

- by means of a forced sale of the charged assets;
- for certain assets by means of a private sale, if so agreed by the parties in the original security agreement or at any time thereafter (pre- or post-default);
- through a public notary, a lawyer or an accountant, in certain stages of the enforcement proceeding; or
- in the case of marketable securities with an available market value, by an authorised broker on the market.

Financial collateral created under Legislative Decree No. 170/2004 (the "Financial Collateral Decree", which has implemented the financial collateral directive in Italy) may be enforced by appropriation or private sale.

7.5 Do restrictions apply to foreign lenders in the event of (a) filing suit against a company in your jurisdiction, or (b) foreclosure on collateral security?

Generally, no restrictions apply for foreign lenders.

7.6 Do the bankruptcy, reorganisation or similar laws in your jurisdiction provide for any kind of moratorium on enforcement of lender claims? If so, does the moratorium apply to the enforcement of collateral security?

The bankruptcy of the debtor, as well as its submission to reorganisation proceedings (i.e. *concordato preventivo*, *accordi di ristrutturazione*, *pre-concordato* and *concordato preventivo con continuità aziendale*), affect the secured creditor's right to enforce the security. Upon the commencement of such proceedings, and subject to certain exceptions (see question 8.1), all the enforcement actions made by creditors are stayed and creditors must file a claim within a defined period.

7.7 Will the courts in your jurisdiction recognise and enforce an arbitral award given against the company without re-examination of the merits?

Italy is party to the 1958 New York Convention, which establishes the conditions under which arbitral awards can be recognised and enforced within the contracting states.

An Italian Court will declare the effectiveness of arbitral awards *inaudita altera parte* provided that: (i) the litigation falls within the scope of the arbitration agreement pursuant to Italian law; and (ii) the contents of the arbitral award comply with Italian public policy. The counterparty is entitled to challenge such decision before the competent Court of Appeal within 30 days from its notification.

8 Bankruptcy Proceedings

8.1 How does a bankruptcy proceeding in respect of a company affect the ability of a lender to enforce its rights as a secured party over the collateral security?

Upon the declaration of bankruptcy, enforcement and preservation actions (*azioni esecutive e cautelari*) on a debtor's assets are stayed, with very few exceptions (such as: (i) enforcement actions on mortgaged assets according to mortgage credit rules (*credito fondiario*) as set out in Italian Banking Act; (ii) in very limited cases and under certain circumstances, creditors secured by a lien (*pegno*) or a privilege (*privilegio*); and (iii) enforcement of financial collateral arrangements pursuant to the Financial Collateral Decree).

8.2 Are there any preference periods, clawback rights or other preferential creditors' rights (e.g., tax debts, employees' claims) with respect to the security?

Some acts, transactions and security interests may be subject to bankruptcy claw-back actions if such acts have been perfected during the so-called suspect period (from six months to one year depending on the circumstances), with very few exceptions. In particular, payments of debts which are due and payable may be clawed-back if made in the six-month period preceding the declaration of bankruptcy.

Acts through which the debtor disposes of its assets may, under some conditions, be declared ineffective as a result of an ordinary claw-back action.

Gratuitous acts (*atti a titolo gratuito*) and prepayments (*pagamenti anticipati*) are *ex lege* ineffective if such acts have been made during the two-year period preceding the declaration of bankruptcy. In particular, prepayments can be revoked during such two-year period irrespective of whether the recipient was aware of the state of insolvency of the debtor.

Certain claims – expressly identified by operation of law (such as Italian tax and national social security contributions, employee arrears of wages or salary, etc.) – are preferred in the distribution of proceeds arising from the liquidation of the bankrupt's estate.

8.3 Are there any entities that are excluded from bankruptcy proceedings and, if so, what is the applicable legislation?

Companies carrying out commercial activity can be subject to the bankruptcy proceedings. Moreover, a company may be declared bankrupt when its size exceeds certain thresholds related to annual balance sheet assets, annual gross proceeds or indebtedness.

Italian companies which do not meet the above-mentioned thresholds (and physical persons in a situation of over-indebtedness) are subject to smaller bankruptcy proceedings (so-called *procedura da sovraindebitamento*).

In addition, special insolvency proceedings are applicable to large corporations (*grandi imprese*), public entities (*enti pubblici*) and regulated entities such as banks and insurance companies.

8.4 Are there any processes other than court proceedings that are available to a creditor to seize the assets of a company in an enforcement?

Pursuant to the Financial Collateral Decree, the beneficiary of financial collateral may, under certain conditions, satisfy its claims by way of appropriation or private sale without the involvement of the court, even whilst a bankruptcy proceeding is pending.

For certain types of security, such as pledges over shares, the parties may also agree – in the original security agreement or at any time thereafter – that the enforcement can take place by means of a private sale.

9 Jurisdiction and Waiver of Immunity

9.1 Is a party's submission to a foreign jurisdiction legally binding and enforceable under the laws of your jurisdiction?

An Italian Court will generally decline jurisdiction if the parties have submitted a dispute (either present or future) to the jurisdiction of a foreign court, subject to compliance with certain mandatory principles of law.

9.2 Is a party's waiver of sovereign immunity legally binding and enforceable under the laws of your jurisdiction?

Italian companies are generally not subject to sovereign immunity. In principle, waiver of sovereign immunity is not prohibited under Italian law. However, the possibility for governmental or other public agencies and relevant personnel to waive their sovereign immunity should be assessed on a case-by-case basis.

10 Licensing

10.1 What are the licensing and other eligibility requirements in your jurisdiction for lenders to a company in your jurisdiction, if any? Are these licensing and eligibility requirements different for a "foreign" lender (i.e. a lender that is not located in your jurisdiction)? In connection with any such requirements, is a distinction made under the laws of your jurisdiction between a lender that is a bank *versus* a lender that is a non-bank? If there are such requirements in your jurisdiction, what are the consequences for a lender that has not satisfied such requirements but has nonetheless made a loan to a company in your jurisdiction? What are the licensing and other eligibility requirements in your jurisdiction for an agent under a syndicated facility for lenders to a company in your jurisdiction?

Lending activity in Italy, to the extent it is conducted on a professional basis and is addressed to the general public, is regulated by the provisions set out under the Italian Banking Act and its implementing regulations. Pursuant to these, the only entities authorised to carry out lending activities in Italy are the following:

- licensed banks, which include:
  - Italian banks;
  - EU passported banks; and
  - non-EU banks licensed in Italy;
- financial institutions enrolled in a special register held by the Bank of Italy pursuant to Article 106 of the Italian Banking Act;
- EU-based financial companies that are controlled by a bank incorporated in the same EU country;
- securitisation special purpose vehicles incorporated pursuant to the Italian Securitisation Law;
- Italian insurance companies; and
- following certain relatively recent amendments introduced into the Italian legal system, Italian alternative close-ended investment funds and, subject to particular conditions and requirements, EU alternative close-ended investment funds.

Banks which are not established in an EU Member State may only engage in lending into Italy if they are explicitly authorised to do so (and granted a licence to this effect) by the Bank of Italy.

Lending activity (described in the relevant regulations as "the granting of finance in whatever form") includes the traditional direct granting of loans as well as other activities (including issues of guarantees, leasing, factoring and the purchase of receivables for consideration) which amount to lending.

The violation of the prohibition described above may lead to a variety of penalties and sanctions, depending on the actual circumstances of the relevant case and which, in addition to severe monetary penalties, may in certain cases also involve criminal charges.

A specific set of exemptions is provided for intragroup financings, where such financings are made in favour of parent companies, subsidiaries and affiliates and, more generally, to companies belonging to the same group, but with certain further restrictions if the lending is in the form of purchase of receivables.

11 Other Matters

11.1 Are there any other material considerations which should be taken into account by lenders when participating in financings in your jurisdiction?

Under Italian law the granting of financings is subject to certain mandatory rules relating to:

- Usury: in Italian law financing transactions, the applicable rate of interest (plus applicable fees and expenses) cannot exceed a certain threshold (which varies depending on the type of financing transaction) determined by the Bank of Italy on a quarterly basis.
- Compounding of interest: this is generally prohibited in financing transactions, save for certain limited cases.
- Transparency: financing transactions entered into by banks and financial intermediaries where the terms and conditions are unilaterally imposed by such entities and are not subject to individual negotiation with the client are subject to certain mandatory rules enacted by the Bank of Italy which are aimed at simplifying the understanding of the legal and economic terms of the financing transaction by the client.

Acknowledgment

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ALLEN & OVERY

Allen & Overy is a full-service global elite law firm headquartered in London. Our commitment to help our clients deliver their global strategies has seen us build a truly global network now spanning 44 offices in 31 countries. We have also developed strong ties with more than 450 relationship firms in 118 countries where we do not have a presence. In this way we are able to deliver high quality advice in 99% of the world's economies.

For 20 years, Allen & Overy has been one of Italy's premier legal practices, offering domestic and cross-border legal services to the world's leading corporations and financial institutions. Based in Milan and Rome, our lawyers have an in-depth knowledge of the local market and its related dynamics and players, and are able to combine that with our international reach and sector expertise.

Ivory Coast

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1 Overview

1.1 What are the main trends/significant developments in the lending markets in your jurisdiction?

Lending market activity is showing strong growth in Côte d'Ivoire as local banks and international financial institutions, either separately or together, are becoming involved in many extension or development projects by private borrowers, mainly being mid-size or large companies.

With the increase of the public and private partnership sector, financial institutions are showing great interest in providing assistance to government entities as well.

The main challenge for borrowers within the lending sector is the negotiation of a low interest rate and an overall global interest rate for financings.

1.2 What are some significant lending transactions that have taken place in your jurisdiction in recent years?

Important secured financings have taken place over recent years within the construction sector, including the construction of hotels – notably the Radisson Blu Hotel of Abidjan at about €40,000,000 – or the housing project to be completed in a suburb not far from Abidjan (Anyama) at €78,000,000.

2 Guarantees

2.1 Can a company guarantee borrowings of one or more other members of its corporate group (see below for questions relating to fraudulent transfer/financial assistance)?

Subject to compliance with the OHADA rules on securities and commercial companies, a limited company may guarantee the obligations of one or more other members of its corporate group. Further details are provided in the answers below.

2.2 Are there enforceability or other concerns (such as director liability) if only a disproportionately small (or no) benefit to the guaranteeing/securing company can be shown?

The OHADA rules on securities allow a third party to grant a security for another party without being the beneficiary of the loan. However, regarding important financial transactions, some restrictions apply in order to avoid a financial strain on the guarantor, a hidden value transfer or even money laundering.

Indeed, a guarantee or security interest granted by a limited company should not exceed the financial capabilities of the guarantor. As such, it is the lender's duty to ensure the financial capabilities of the guarantor when requesting such guarantee and the obligation of the guarantor to provide Board and/or shareholder approval of the transaction and the security package to mitigate the directors' liability risk and protect the minority shareholders' interests.

When it comes to a group of companies, the benefit of the company granting the security within a financial transaction concluded by another entity of the group must also be looked at to avoid unlawful value transfer and too much of a burden on that company. However, when a parent company which fully owns a subsidiary grants a security, there is no risk of unlawful value transfer because it is considered a full beneficiary of the loan. The only restriction would be to look at the fiscal implications of the financing when the subsidiary is in a different jurisdiction.

2.3 Is lack of corporate power an issue?

Only the legal representative of the company or any other person expressly designated can execute a finance transaction and grant securities attached to it. This legal representative must obtain the approval of the Board and/or the shareholders.

This should be a condition precedent before the finance documents are signed.

2.4 Are any governmental or other consents or filings, or other formalities (such as shareholder approval), required?

No governmental approvals are required in order for a private entity to provide guarantees or grant security interests.

Shareholder approval is generally not required for public limited companies (unless requested in the articles of incorporation), but the Board of Directors must approve the granting of guarantees and security interests. Shareholder approval is required for private limited companies.

Any personal guarantee granted by an individual must comply with the OHADA rules on personal security, such as handwritten consent of the amount and duration of the loan.

2.5 Are net worth, solvency or similar limitations imposed on the amount of a guarantee?

For a local bank financing a company, the common banking rules of the WAEMU (West African Economic and Monetary Union) zone provide that the bank ensures that the borrower is able to repay the loan. As such, it is generally imposed by the lender as a CP – a non-bankruptcy certificate from the corporate registry where the borrower is incorporated.

In case a security has been granted despite the existence of an insolvency procedure of the guarantor, Côte d'Ivoire courts will declare the security void.

2.6 Are there any exchange control or similar obstacles to enforcement of a guarantee?

Exchange control provisions apply on top of the financing transaction, mainly regarding the disbursement of the loan. The enforcement of a guarantee must comply with local OHADA rules as long as the asset granted as a security is located in Côte d'Ivoire.

3 Collateral Security

3.1 What types of collateral are available to secure lending obligations?

There are a number of different types of collateral and security interests available under OHADA law. The most common are the pledge agreement for agricultural goods or the pledge of professional equipment, mortgages, and the assignment of receivables.

3.2 Is it possible to give asset security by means of a general security agreement or is an agreement required in relation to each type of asset? Briefly, what is the procedure?

A separate agreement is necessary for each security granted. It is explained by the fact that each type of security has its own legal regime and requirements. For instance, when the law requests a registration of the security at the corporate registry, it is necessary to have a separate agreement to comply with such requirement.

We commonly see a facility agreement providing for all the securities that must be granted, but there is no general security agreement signed for all the securities to be granted and covering different assets.

Notwithstanding the above, it is possible to designate a security agent that will manage all the securities and ensure that they all comply with the applicable law.

3.3 Can collateral security be taken over real property (land), plant, machinery and equipment? Briefly, what is the procedure?

A security over real property is granted by a mortgage. Such agreement must comply with the local rules and be drafted by a notary public. Evaluation of the property must be conducted and proof of ownership provided. The agreement must outline whether it is granting first, second or third rank because the guarantor may have already granted a mortgage over the same property.

However, for machinery and equipment, a pledge is granted. This pledge does not prevent the guarantor from using the equipment. The equipment must be clearly described and the agreement must be registered at the corporate registry in order to be opposable to third parties.

3.4 Can collateral security be taken over receivables? Briefly, what is the procedure? Are debtors required to be notified of the security?

In granting an assignment of receivables, the guarantor must send a notification to his debtor, otherwise the debtor will continue to pay directly to the guarantor. Specific indications must be provided to the debtor regarding the payment modalities; for instance, providing another bank account where the secured debtor shall make the payments or designating the secured party or his representative.

In addition to the assignment of receivables considered as a security under OHADA law, we also have the delegation of receivables which is also a security but only under the general civil rules. A delegation of insurance proceeds is the most common security used. It still requires a notification or an acceptance of the insurer to avoid later litigation on the beneficiary of the sums to be paid.

3.5 Can collateral security be taken over cash deposited in bank accounts? Briefly, what is the procedure?

Security can be granted over cash deposited in bank accounts and the bank account holder must be notified of the security granted.

Such security is granted by way of an account pledge for the benefit of the lender. In order for the pledge to be perfected and enforceable, the guarantor must waive all disposal rights to the bank account. Such bank account pledge should therefore not be secured for an account used in the day-to-day activities of the guarantor.

The bank account pledge is most effective on a deposit account, which is generally the account where the receivables pledged are paid.

3.6 Can collateral security be taken over shares in companies incorporated in your jurisdiction? Are the shares in certificated form? Can such security validly be granted under a New York or English law governed document? Briefly, what is the procedure?

Security over shares of a company incorporated in Côte d'Ivoire can only be granted under OHADA law.

The pledge agreement needs to be registered at the corporate registry and the share register of the company must mention the security granted. There is no direct transfer of the shares as long as the facility agreement is still pending and default of payment has not yet been demonstrated.

3.7 Can security be taken over inventory? Briefly, what is the procedure?

A pledge granted over agricultural goods is generally granted with the involvement of a collateral management agreement. The goods are kept in the warehouse of the collateral manager who has the obligation to control the reception and exportation of the goods.

3.8 Can a company grant a security interest in order to secure its obligations (i) as a borrower under a credit facility, and (ii) as a guarantor of the obligations of other borrowers and/or guarantors of obligations under a credit facility (see below for questions relating to the giving of guarantees and financial assistance)?

Yes, subject to compliance with the applicable laws as described in question 2.2.

3.9 What are the notarisation, registration, stamp duty and other fees (whether related to property value or otherwise) in relation to security over different types of assets?

Stamp duties are applied on the agreements before there are registered at the corporate registry of the commercial court. Registration fees are also applicable and paid based on a rate on the principal secured obligation.

Notarisation of the agreements is necessary when it comes to a mortgage. Fees are paid on the basis of the value of the secured obligation.

It is the borrower's duty to pay all the fees incurred by the facility.

3.10 Do the filing, notification or registration requirements in relation to security over different types of assets involve a significant amount of time or expense?

Most security interests are established more or less immediately. The applicable costs are those mentioned in question 3.9. Lawyers' fees for counselling the lending bank are the borrower's responsibility.

3.11 Are any regulatory or similar consents required with respect to the creation of security?

There are no such consents required.

3.12 If the borrowings to be secured are under a revolving credit facility, are there any special priority or other concerns?

No, there are not.

3.13 Are there particular documentary or execution requirements (notarisation, execution under power of attorney, counterparts, deeds)?

There are no such requirements. However, if the credit facility is under Côte d'Ivoire law, stamp duties will apply to confirm the date of signature.

4 Financial Assistance

4.1 Are there prohibitions or restrictions on the ability of a company to guarantee and/or give security to support borrowings incurred to finance or refinance the direct or indirect acquisition of: (a) shares of the company; (b) shares of any company which directly or indirectly owns shares in the company; or (c) shares in a sister subsidiary?

The restrictions are set out in the OHADA Uniform Act on Commercial Companies and the Uniform Act on Securities. Indeed, it is forbidden to provide financial assistance to a borrower with the purpose of acquiring shares in the company.

5 Syndicated Lending/Agency/Trustee/Transfers

5.1 Will your jurisdiction recognise the role of an agent or trustee and allow the agent or trustee (rather than each lender acting separately) to enforce the loan documentation and collateral security and to apply the proceeds from the collateral to the claims of all the lenders?

Lenders may appoint a facility and/or security agent to represent them in all matters relating to the finance documents as well as any security interests. Such agents are allowed to enforce any rights that the lenders might have under the finance documents. Furthermore, the agent may enforce any collateral security and apply the proceeds from such enforcement in order to satisfy the secured claims of the lenders.

5.2 If an agent or trustee is not recognised in your jurisdiction, is an alternative mechanism available to achieve the effect referred to above which would allow one party to enforce claims on behalf of all the lenders so that individual lenders do not need to enforce their security separately?

This does not apply; see question 5.1 above.

5.3 Assume a loan is made to a company organised under the laws of your jurisdiction and guaranteed by a guarantor organised under the laws of your jurisdiction. If such loan is transferred by Lender A to Lender B, are there any special requirements necessary to make the loan and guarantee enforceable by Lender B?

A transfer of a loan is perfected and made valid and enforceable against third parties by way of an assignment of receivables and due notification of the debtor under the loan that is being transferred.

6 Withholding, Stamp and Other Taxes; Notarial and Other Costs

6.1 Are there any requirements to deduct or withhold tax from (a) interest payable on loans made to domestic or foreign lenders, or (b) the proceeds of a claim under a guarantee or the proceeds of enforcing security?

When the lender is a foreign entity, the borrower is required to withhold taxes on the revenue of interests paid to the lender.

6.2 What tax incentives or other incentives are provided preferentially to foreign lenders? What taxes apply to foreign lenders with respect to their loans, mortgages or other security documents, either for the purposes of effectiveness or registration?

Unless there is a tax treaty between Côte d'Ivoire and the country of the foreign lender, there is no other tax incentive.

Taxes due by the lender are mainly those on the revenue of interests paid. The other taxes incurred by the loan are the obligation of the borrower.

6.3 Will any income of a foreign lender become taxable in your jurisdiction solely because of a loan to or guarantee and/or grant of security from a company in your jurisdiction?

The income from the interest paid by the borrower is taxable in Côte d'Ivoire.

6.4 Will there be any other significant costs which would be incurred by foreign lenders in the grant of such loan/guarantee/security, such as notarial fees, etc.?

Please see question 3.9 above.

6.5 Are there any adverse consequences to a company that is a borrower (such as under thin capitalisation principles) if some or all of the lenders are organised under the laws of a jurisdiction other than your own? Please disregard withholding tax concerns for purposes of this question.

There are no adverse consequences in such case. The lenders are only requested to comply with local mandatory rules are far as securities are concerned.

7 Judicial Enforcement

7.1 Will the courts in your jurisdiction recognise a governing law in a contract that is the law of another jurisdiction (a "foreign governing law")? Will courts in your jurisdiction enforce a contract that has a foreign governing law?

Yes as long as the public order of Côte d'Ivoire is not threatened.

The courts of Côte d'Ivoire will not recognise the choice of a foreign law as the governing law of the facility agreement if such law was chosen as a method of avoiding rules or regulations of another jurisdiction which, as a matter of public policy, the courts of Côte d'Ivoire regard as being properly relevant to the facility agreement.

7.2 Will the courts in your jurisdiction recognise and enforce a judgment given against a company in New York courts or English courts (a "foreign judgment") without re-examination of the merits of the case?

No matter what foreign law governs the facility agreement, it is important to note that a foreign judgment is not directly enforceable in Côte d'Ivoire. It must go through the procedure of "Exequatur". This is not a re-litigation of the case, but a formal review of the case by a domestic competent court that would eventually render the judgment enforceable in Côte d'Ivoire.

The Exequatur is awarded when the following requirements are met:

- The decision must be provided from a competent jurisdiction according to the applicable laws of the country where it was made.
- The decision is not subject to appeal and is enforceable in that country.
- Due process has been observed: the condemned party must be called to the proceeding and must be given the opportunity to defend itself.
- There is no contradictory decision already in existence in Côte d'Ivoire before the foreign one has been rendered concerning the same case and the same parties.
- The decision is not contrary to public order.

7.3 Assuming a company is in payment default under a loan agreement or a guarantee agreement and has no legal defence to payment, approximately how long would it take for a foreign lender to (a) assuming the answer to question 7.1 is yes, file a suit against the company in a court in your jurisdiction, obtain a judgment, and enforce the judgment against the assets of the company, and (b) assuming the answer to question 7.2 is yes, enforce a foreign judgment in a court in your jurisdiction against the assets of the company?

The time a litigation procedure takes is highly dependent on the complexity of the case and the administrative organisation of the local courts.

Our experience leads us to advise that at least 12 months are necessary in order to obtain an enforceable decision (obtainment of an appeal decision included).

7.4 With respect to enforcing collateral security, are there any significant restrictions which may impact the timing and value of enforcement, such as (a) a requirement for a public auction, or (b) regulatory consents?

There are no significant restrictions in our jurisdiction.

7.5 Do restrictions apply to foreign lenders in the event of (a) filing suit against a company in your jurisdiction, or (b) foreclosure on collateral security?

There are no significant restrictions in our jurisdiction.

7.6 Do the bankruptcy, reorganisation or similar laws in your jurisdiction provide for any kind of moratorium on enforcement of lender claims? If so, does the moratorium apply to the enforcement of collateral security?

Yes. Please see question 8.1 below.

7.7 Will the courts in your jurisdiction recognise and enforce an arbitral award given against the company without re-examination of the merits?

Yes. The Exequatur rules apply here too.

8 Bankruptcy Proceedings

8.1 How does a bankruptcy proceeding in respect of a company affect the ability of a lender to enforce its rights as a secured party over the collateral security?

Following a bankruptcy order, no independent enforcement is, as a general rule, available for secured creditors. A creditor that has a valid and perfected pledge is paid by preference before other creditors who do not have a security.

8.2 Are there any preference periods, clawback rights or other preferential creditors' rights (e.g., tax debts, employees' claims) with respect to the security?

Preferential creditor rights are granted to: employees' claims; tax debts, legal expenses; security interests over real estate property; and security interests benefiting from a retention right (such as a share pledge, a securities account pledge or a bank account pledge).

8.3 Are there any entities that are excluded from bankruptcy proceedings and, if so, what is the applicable legislation?

Legal entities are mainly subject to bankruptcy proceedings.

8.4 Are there any processes other than court proceedings that are available to a creditor to seize the assets of a company in an enforcement?

There may be a direct transfer of the property when a mortgage is granted by a legal entity to another legal entity.

9 Jurisdiction and Waiver of Immunity

9.1 Is a party's submission to a foreign jurisdiction legally binding and enforceable under the laws of your jurisdiction?

Yes. The principles of freedom of choice of law and choice of forum apply when it concerns facility agreements, but not security agreements when the assets are located in Côte d'Ivoire.

9.2 Is a party's waiver of sovereign immunity legally binding and enforceable under the laws of your jurisdiction?

Waivers of sovereign immunity from jurisdiction are legally binding and enforceable under the laws of Côte d'Ivoire.

However, a waiver of sovereign immunity from jurisdiction does not entail a waiver of immunity from execution, which must be separately expressed in order for it to be equally binding and enforceable.

10 Licensing

10.1 What are the licensing and other eligibility requirements in your jurisdiction for lenders to a company in your jurisdiction, if any? Are these licensing and eligibility requirements different for a "foreign" lender (i.e. a lender that is not located in your jurisdiction)? In connection with any such requirements, is a distinction made under the laws of your jurisdiction between a lender that is a bank *versus* a lender that is a non-bank? If there are such requirements in your jurisdiction, what are the consequences for a lender that has not satisfied such requirements but has nonetheless made a loan to a company in your jurisdiction? What are the licensing and other eligibility requirements in your jurisdiction for an agent under a syndicated facility for lenders to a company in your jurisdiction?

A local entity granting credit must have a licence to do so in order to be called a bank or financial entity. The same requirement is not applicable when the borrower has obtained a loan from a foreign entity.

The security agent regime is governed by the OHADA Uniform Act on Securities.

11 Other Matters

11.1 Are there any other material considerations which should be taken into account by lenders when participating in financings in your jurisdiction?

The key legal issues to be considered when lending to Côte d'Ivoire entities, and taking security over Côte d'Ivoire assets, have been addressed above.

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IMBOUA - KOUAO - TELLA & ASSOCIES

IKT Law Firm is a certified law firm registered at the Côte d'Ivoire Bar Association since 2009.

It is a business-oriented law firm, with an emphasis on structured financing and corporate law. The IKT team is composed of lawyers and in-house counsels, all bilingual, with a strong experience in local and international transactions.

Regarding its litigation practice, the firm represents clients before all types of tribunals, whether it is in the regulatory first instance or appellate courts, and also before alternative dispute resolution tribunals such as the Arbitration Court of Côte d'Ivoire (CACI) and the OHADA Justice Arbitration Court (CCJA).

As for counselling matters, the firm aims to serve the needs of companies and individuals looking for the best advice to help them in their day-to-day or complex business decisions. As such matters are diverse and require the most time, we strongly analyse the client's activity and the legal issues they raise in terms of compliance and mitigation of risks.

In addition, IKT Law Firm regularly organises seminars with local clients to update them on new trends of the law regarding their activities.

The lawyers of IKT regularly take part in UIA meetings and training activities to extend their potential and network. The firm is also referenced in global directories as a firm with a strong potential in international transactions.

Chapter 56

Japan

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1 Overview

1.1 What are the main trends/significant developments in the lending markets in your jurisdiction?

Japanese lending has traditionally relied upon mortgages over real estate to secure loans. In the case of small and medium-sized entities, personal guarantees by representative directors of the borrowers have also been common (a guideline called the "*keieisha-hosho* guideline" on this type of guarantee became effective on February 1, 2014). While new types of asset-backed or cash flow financing such as (i) acquisition financing (leveraged buyout (LBO) financing, etc.), (ii) asset-based lending (ABL), (iii) debtor-in-possession (DIP) financing, and (iv) project financing are developing in Japan, the traditional practice of lending against real estate collateral remains one of the preferred methods among Japanese banks.

1.2 What are some significant lending transactions that have taken place in your jurisdiction in recent years?

Since the great earthquake and tsunami of March 11, 2011, there has been growing anti-nuclear sentiment in Japan and intensified analysis by policymakers regarding Japan's energy demands. Financing the costs of alternative clean energy solutions (such as solar, wind, hydro-power and geothermal) through project financing structures is one of the key focuses in Japan now and for the next decade.

2 Guarantees

2.1 Can a company guarantee borrowings of one or more other members of its corporate group (see below for questions relating to fraudulent transfer/financial assistance)?

Yes, guarantees from related companies are permissible in Japan.

2.2 Are there enforceability or other concerns (such as director liability) if only a disproportionately small (or no) benefit to the guaranteeing/securing company can be shown?

In general, there are no enforceability concerns, although directors may be personally in breach of their duty of care under the Companies Act (Act No. 86 of July 26, 2005, as amended) in such situations. That said, if only a disproportionately small benefit or no benefit at all is received by the guarantor, in a bankruptcy proceeding of the guarantor, the guarantee may be subject to avoidance by the bankruptcy trustee.

2.3 Is lack of corporate power an issue?

Corporate power is necessary for a guarantor to grant guarantees.

2.4 Are any governmental or other consents or filings, or other formalities (such as shareholder approval), required?

The Civil Code (Act No. 89 of April 27, 1896, as amended) requires that any guarantee agreement must be in writing. Shareholder approval is not required. Depending upon the materiality of the amount guaranteed, the board of directors' approval may be required. In practice, the loan and/or guarantee agreement will contain a representation and warranty as to the board of directors' approval, and such approval will often be a condition precedent to funding a loan.

2.5 Are net worth, solvency or similar limitations imposed on the amount of a guarantee?

Japanese law does not provide net worth, solvency or similar limitations on the amount of a guarantee. (Please note that, where an obligor has the obligation to furnish a guarantor, such guarantor must be a person with capacity to act, and have sufficient financial resources to pay the obligation. This does not apply in cases where the creditor designated the guarantor.)

2.6 Are there any exchange control or similar obstacles to enforcement of a guarantee?

No. However, please note that a payment exceeding JPY 30,000,000 from a resident in Japan to overseas by way of bank remittance may be subject to reporting requirements.

3 Collateral Security

3.1 What types of collateral are available to secure lending obligations?

In Japan, many types of property may be pledged to secure debt obligations, including real property (buildings and land), plant, machinery, equipment, receivables, accounts, shares and inventory.

3.2 Is it possible to give asset security by means of a general security agreement or is an agreement required in relation to each type of asset? Briefly, what is the procedure?

Different types of security interests may be created by one security agreement; however, as discussed in questions 3.3 to 3.8 below, the security interest in each type of asset must be perfected separately.

3.3 Can collateral security be taken over real property (land), plant, machinery and equipment? Briefly, what is the procedure?

(1) Real property (land)

Under Japanese law, a typical security interest upon real property is a mortgage (*teito-ken*). For a revolving facility with a maximum claim amount (*kyokudo-gaku*), a revolving mortgage (*ne-teito-ken*) is applicable.

A mortgage on land or a building is created by an agreement between a mortgagor and a mortgagee. In order to perfect the mortgage against a third party, the mortgage must be registered with the Legal Affairs Bureau (LAB) having jurisdiction over the property. There are approximately 500 LABs throughout Japan.

Under Japanese law, the land and any building on the land are treated independently. Therefore, the mortgagor of the land and the mortgagor of any building on the land could be different entities. It is, therefore, important to separately create and perfect the mortgage as a first lien upon both the land and the building. In Japan, almost all land (by parcel) and buildings (by building, upon completion) are already registered with the LAB. The registration of the mortgage is made as an addition to such existing registration. Therefore, it is necessary to investigate the title and confirm whether the property is already encumbered by an existing mortgage. Typically, a mortgage registration includes (i) the name and address of the debtor and mortgagor, (ii) the origin and date of the mortgage, (iii) the priority, and (iv) the claim amount (in the case of a revolving mortgage, the maximum claim amount). Though various covenants and other provisions may be included in the mortgage agreement, the full mortgage agreement is not recorded in the registration. Only the registrable items including those enumerated above will appear in a registration.

(2) Plant

A typical "plant" consists of land, a building, machinery and equipment. As mentioned above, land and a building can be collateralised by a mortgage (*teito-ken* or *ne-teito-ken*). Machinery and equipment are classified as movables, and can be collateralised by a security interest (*joto-tanpo*) (discussed below).

In addition, Japanese law provides for two comprehensive security interests for property located in a factory. One is a factory mortgage (*kojo-teito-ken*), and the other is a factory estate mortgage (*kojo-zaidan-teito-ken*). A factory mortgage over the land covers all machinery and equipment located in the factory. A factory estate mortgage is a very strong security interest that can actually eliminate pre-existing security interests over movables in the factory estate. Notice regarding the factory estate is published in the Japanese official gazette and if an existing security interest holder fails to object within a certain period (specified from one to three months), the existing security interest is extinguished. Both a factory mortgage and a factory estate mortgage require identification of each piece of machinery and equipment, and therefore require more burdensome procedures and costs than normal types of mortgages. The factory mortgage and factory estate mortgage are not very common and are used mostly for large factories.

(3) Machinery and equipment

Machinery and equipment are movables. Movables can be collateralised by way of assignment as security (*joto-tanpo*). This security interest can be created by a security agreement between an assignor and an assignee. In order to perfect this security interest, the target movable must be "delivered" from the assignor to the assignee. Delivery can be made by (i) physical delivery, (ii) constructive delivery, or (iii) (where the assignor is a legal entity (including a company)) if a movable assignment registration (*dosan-joto-toki*) is filed with the LAB, the registration itself is deemed delivery from the assignor to the assignee. The LAB located in the Nakano Ward of Tokyo is the exclusive designated LAB for any movable assignment registration.

In creation of *joto-tanpo*, it is necessary to identify the target movable by whatever means is enough to specify it, such as kind, location, number and so forth. This identification rule is also applicable in perfection of *joto-tanpo* by way of physical or constructive delivery. In perfection by movable assignment registration, there are two statutory ways to identify the target movable: (i) specification by kind and a definitive way to specify the target (such as a serial number); and (ii) specification by kind and location. The former is usually used for a fixed asset, and the latter is usually used for inventory (aggregate movables).

Note that the movable assignment registration is compiled by the assignor (not by the target movable). Therefore, unlike a real estate registration which can be searched by the property, a movable assignment registration cannot be searched by the target movable, and priority cannot be registered because there is no statutory registration system to reflect the priority in the movable assignment registration. There is continued debate as to whether a second lien (*joto-tanpo*) is valid. Anyone can search whether an assignor has already filed a movable assignment registration and obtain an outline certificate of the registration for a fee of JPY 500. If there is no existing movable assignment registration filed with the LAB, a certificate of non-existence of movable assignment registration will be issued. However, this does not mean there is no physical or constructive delivery. Therefore, it is necessary to perform due diligence with respect to possible physical or constructive delivery by an assignor. If a movable assignment registration has been filed with the LAB, the outline certificate describes (i) the existence of such registration, (ii) the timing of the assignment, and (iii) the name and address of the assignee, but it does not provide detailed information regarding the target movable. A comprehensive registration certificate is only accessible to limited persons, and in practice, a lender will ask the debtor to obtain the latest comprehensive certificate.

3.4 Can collateral security be taken over receivables? Briefly, what is the procedure? Are debtors required to be notified of the security?

A security interest in receivables (claim) may be taken by a pledge (*shichi-ken*) or assignment as security (*joto-tanpo*). These security interests can be created by a security agreement between the pledgor/assignor and pledgee/assignee.

In creation of the security interest, it is necessary to identify the target receivable enough to specify it (such as kind, date of origination and other items to the extent applicable). If the target is a claim to be generated in the future (*shorai-saiken*, "future claim"), the period (beginning and end dates of the period during which the claim will be generated) must be specified in the security agreement and in connection with perfection. If there is an agreement made between the debtor and the obligor of the target receivable which prohibits pledge/assignment of the target receivable, the pledge/assignment is basically invalid, with two exceptions: (i) if the pledgee/assignee is unaware of the prohibition agreement without gross negligence, the pledge/assignment shall be valid; and (ii) the pledge/assignment will become valid retroactively from the time of the pledge/assignment (to the extent not harmful to a third party) if the obligor of the target receivable consents to the pledge/assignment, even if there has been a prohibition agreement.

The pledgee/assignee can assert the security interest ***against the obligor of the target receivable*** upon (i) notice to the obligor from the pledgor/assignor, or (ii) acknowledgment of the obligor. The pledgee/assignee can assert the security interest ***against a third party*** (such as a double pledgee/assignee or bankruptcy trustee of the pledgor/assignor) upon (i) notice to the obligor of the target receivable from the pledgor/assignor by a certificate with (a stamp of) a fixed date, (ii) an acknowledgment of the obligor of the target receivable by a certificate with (a stamp of) a fixed date, or (iii) (only where the pledger/assignor is a legal entity (including a company)) a claim pledge/assignment registration with the special LAB located in Nakano Ward of Tokyo. The registration can be made with the LAB upon creation of the security interest without notice to the obligor. In such a case, practically, the notice to the obligor of the target receivable will be sent upon the event of default of the pledgor/assignor, and the notice must be accompanied by a registration certificate (this notice can be sent by the pledgee/assignee).

The claim assignment registration is not compiled based upon the target receivable, but by the assignor. Therefore, unlike the real estate registration, the claim assignment registration cannot be searched by the target receivables, and, as with movables, priority cannot be registered.

3.5 Can collateral security be taken over cash deposited in bank accounts? Briefly, what is the procedure?

There are various types of bank deposits in Japan. We will discuss two typical deposit claims used for a pledge: (i) a term deposit (*teiki-yokin*); and (ii) an ordinary deposit (*futsu-yokin*). Validity of a pledge over a term deposit is well established; however, there has been debate as to the validity of a pledge over an ordinary deposit because there is no Supreme Court decision addressing this issue. Nevertheless, a pledge over an ordinary deposit is often used for structured financing. As a pledge or assignment of a deposit is usually prohibited by the deposit agreement, a pledge without the bank's consent is invalid. A pledge over deposits is usually created by a standard form of pledge agreement created by the depository bank, including consent by such bank. If the bank's consent is made with a fixed date stamp, that consent constitutes perfection against a third party. If the lender is itself the depository bank, the bank can either set off or exercise the pledge over the deposit claim.

3.6 Can collateral security be taken over shares in companies incorporated in your jurisdiction? Are the shares in certificated form? Can such security validly be granted under a New York or English law governed document? Briefly, what is the procedure?

Under Japanese law, shares of stock companies (*kabushiki-kaisha*) incorporated in Japan can be pledged or assigned as security (*joto-tanpo*). The articles of incorporation of a Japanese stock company will specify whether the shares are represented by physical certificates. If the shares are "certificated" (i.e., if physical certificates representing the shares are issued or will be issued), a pledge can be created by physical delivery of the certificates to the pledgee, and perfected against the issuing company and any third party by continuous possession of the certificates by the pledgee. As this type of pledge is usually unregistered and thus unknown to the issuer (*ryaku-shiki-shichi*), any dividend will be paid to the pledgor, and upon an event of default, the pledgee has to seize the dividend before it is paid to the pledgor. In contrast, if the name and address of the pledgee and target shares are registered on the shareholders' list at the request of the pledgor (*toroku-shichi*), the dividend can be paid directly to the registered pledgee.

If the shares are not and will not be certificated, a pledge may be created by a security agreement between the pledgor and pledgee, and perfected against the issuer and any third party by registration of the pledge on the issuer's shareholders' list.

After January 5, 2009, all share certificates of all listed stock companies incorporated in Japan became null and void. The shares and shareholders of all listed companies are now subject to the book-entry system controlled by the Japan Securities Depositary Center, Inc. (JASDEC). A pledge over listed shares is created and perfected by registering the pledge with the pledgor's account established at the applicable institution under the book-entry system.

Please note that a company which is not listed may, in its articles of incorporation, restrict the transfer of shares and make any transfer subject to the approval of the issuer (such as consent by the board of directors).

Since the valid creation and perfection of a pledge over shares of stock companies (*kabushiki-kaisha*) incorporated in Japan should be governed by Japanese law, it is not practically recommended to elect New York law or English law as the governing law of the security agreement.

3.7 Can security be taken over inventory? Briefly, what is the procedure?

Yes, inventory is usually treated as an aggregate movable. Creation and perfection are as discussed in question 3.3 above.

3.8 Can a company grant a security interest in order to secure its obligations (i) as a borrower under a credit facility, and (ii) as a guarantor of the obligations of other borrowers and/or guarantors of obligations under a credit facility (see below for questions relating to the giving of guarantees and financial assistance)?

Yes, subject to the other items discussed within this chapter regarding guarantees and security interests.

3.9 What are the notarisation, registration, stamp duty and other fees (whether related to property value or otherwise) in relation to security over different types of assets?

Registration taxes are imposed on (i) mortgage registration (0.4% of the claim amount (as for revolving mortgage, 0.4% of the maximum claim amount)), (ii) movable assignment registration (JPY 7,500 per a filing (up to 1,000 movables)), and (iii) claim assignment registration (JPY 7,500 per a filing (up to 5,000 claims) and JPY 15,000 per a filing (exceeding 5,000 claims)). Creation of assignment as security (*joto-tanpo*) over claims may be subject to a fixed stamp duty of JPY 200 as discussed in question 6.2.

3.10 Do the filing, notification or registration requirements in relation to security over different types of assets involve a significant amount of time or expense?

No, except for the factory estate mortgage which requires the procedures discussed in question 3.3 above.

3.11 Are any regulatory or similar consents required with respect to the creation of security?

No regulatory consents are required to grant security, except for general consents for transfers required by the terms of the asset itself (such as licences).

3.12 If the borrowings to be secured are under a revolving credit facility, are there any special priority or other concerns?

Taking an example of a revolving mortgage over real property, loans up to the registered maximum amount will be secured by the mortgage in accordance with the priority of the original registration filing.

3.13 Are there particular documentary or execution requirements (notarisation, execution under power of attorney, counterparts, deeds)?

In general, most of the official documents are executed with a registered seal. The seal registration certificate is also necessary (for example, for filing an official registration). In many cases, there are alternative ways available to foreign lenders.

4 Financial Assistance

4.1 Are there prohibitions or restrictions on the ability of a company to guarantee and/or give security to support borrowings incurred to finance or refinance the direct or indirect acquisition of: (a) shares of the company; (b) shares of any company which directly or indirectly owns shares in the company; or (c) shares in a sister subsidiary?

(a) Shares of the company: no.

(b) Shares of any company which directly or indirectly owns shares in the company: no.

(c) Shares in a sister subsidiary: no.

Apart from financial assistance restrictions, the directors of a company may be deemed in breach of their fiduciary duty of care if the company provides a guarantee or security to secure the borrowings of its shareholder without gaining any benefit in return (as discussed in question 2.2 above).

5 Syndicated Lending/Agency/Trustee/Transfers

5.1 Will your jurisdiction recognise the role of an agent or trustee and allow the agent or trustee (rather than each lender acting separately) to enforce the loan documentation and collateral security and to apply the proceeds from the collateral to the claims of all the lenders?

In the practice of Japanese syndicated loans, an agent usually exists for the syndicated group. However, even if one of the syndicated secured lenders serves as such an agent, it cannot enforce the security interest held by other creditors. In addition, enforcement on behalf of other creditors may be prohibited by the Attorney Act (Act No. 205 of June 10, 1949).

Under the general rule of the Civil Code and other related laws, it is generally understood that the “secured creditor” and the “security holder” must be the same person/entity (“Same Person/Entity Principle”). However, under a security trust system, separation between the “secured creditor” and the “security holder” can be achieved. Until 2007, based on the Secured Bonds Trust Act (Act No. 52 of March 13, 1905), such security trust system only applied to bonds. In 2007, a new Trust Act (Act No. 108 of December 15, 2006) provided for a more general security trust system. Under the new system, if a trust is created with a security interest as the trust property and the terms of the trust provide that the beneficiary is the creditor whose claim is secured, the trustee can be a security trustee (“Security Trust”). As the holder of the security interest, the security trustee may, within the scope of affairs of the Security Trust (subject to instruction by trust beneficiaries in many cases), file petitions for enforcement and take other actions necessary, including distribution of proceeds.

One of the benefits of using a Security Trust is that no individual transfer and perfection procedures are necessary when a secured creditor assigns its secured claims because the security holder does not change under the Security Trust.

However, this new Security Trust system is not used often. While the Trust Act was amended to provide for the Security Trust system, other Japanese laws have not been amended to conform and retain features of the Same Person/Entity Principle. This lack of harmonisation creates practical enforcement risks that have yet to be tested in Japanese courts.

5.2 If an agent or trustee is not recognised in your jurisdiction, is an alternative mechanism available to achieve the effect referred to above which would allow one party to enforce claims on behalf of all the lenders so that individual lenders do not need to enforce their security separately?

Under Japanese practice, when a Security Trust is not used, secured creditors (such as syndicated loan lenders) elect a “security agent” for administrative purposes only (“Security Administrative Agent”).

The basic difference between the security trustee and the Security Administrative Agent is that the Security Administrative Agent is not a holder of all collateral security for all secured creditors. As a result, with respect to the Security Administrative Agent, (i) perfection must be obtained individually for each secured creditor, (ii) when a secured creditor assigns its secured claim and its collateral security, individual perfection procedures to transfer the collateral security are required, and (iii) each secured creditor has to take enforcement actions under its own name notwithstanding that syndicated secured creditors typically act in concert (subject to the majority approval of the syndication group).

Under Japanese law, when several secured creditors share the single/same collateral in the same ranking, there are two possible legal structures (where applicable): (i) “independent and in the same ranking security” (“Same Rank Security”) where each secured creditor owns independent security of the same ranking; and (ii) “joint share security” where all secured creditors share one security (“Joint Security”). The basic difference is that each secured creditor may enforce its security in the Same Rank Security, while unanimous consent of all secured creditors is required to enforce security in the Joint Security. However, secured creditors in a Same Rank Security often enter into an inter-creditor agreement prohibiting individual secured creditors from enforcing the collateral security without majority consent; and, in the case of a syndicated loan, such inter-creditor arrangement is usually provided for in the collateral agreements to which all secured creditors each having a Same Rank

Security are parties. Violation of the inter-creditor agreement does not invalidate the enforcement, but only constitutes a damage claim of the other secured creditors.

5.3 Assume a loan is made to a company organised under the laws of your jurisdiction and guaranteed by a guarantor organised under the laws of your jurisdiction. If such loan is transferred by Lender A to Lender B, are there any special requirements necessary to make the loan and guarantee enforceable by Lender B?

If the loan transfer is not prohibited by the terms of the loan documents, the loan can be transferred by agreement between Lenders A and B, and the guarantee is automatically transferred to the same assignee (Lender B). In order to perfect the loan transfer against the guarantor, according to a prevalent theory, either (i) a notice to the borrower, or (ii) consent by the borrower is sufficient. However, practically, it is sometimes prudent to send a certified notice to both the borrower and guarantor. In practice, however, instead of providing notice to both the borrower and guarantor, Japanese lenders often require certified written consents from both of them to be obtained in order to avoid any dispute regarding the transfer.

6 Withholding, Stamp and Other Taxes; Notarial and Other Costs

6.1 Are there any requirements to deduct or withhold tax from (a) interest payable on loans made to domestic or foreign lenders, or (b) the proceeds of a claim under a guarantee or the proceeds of enforcing security?

Yes. Under the Income Tax Act of Japan (Act No. 33 of March 31, 1965) ("Income Tax Act") and other relevant statutes, a 20.42% withholding tax (including Special Reconstruction Income Tax, which is imposed until December 2037) is levied on the interest paid to foreign lenders where such foreign lender is a corporation having neither a head nor main office in Japan under a loan.

However, if Japan and the country where the foreign lender resides are parties to a tax treaty (such as the United States or the United Kingdom), the withholding tax rate may be lowered or the obligation to withhold tax may be relieved entirely. For example, (i) no withholding tax is levied on interest paid to all UK lenders, and (ii) no more than 10% withholding tax is levied on interest paid to US lenders under the general rules provided by the tax treaties effective as of February 28, 2018. Under the tax treaty between the US and Japan, if a lender is a bank, insurance company or registered securities dealer, the obligation to withhold tax in Japan is relieved entirely. As of February 28, 2018, the tax treaty between the US and Japan is scheduled to be amended, subject to the US ratifying the amendment. After the amendment, all US lenders (including other lenders which are not listed above) are to be generally exempted from the withholding tax in Japan.

Withholding tax is not levied on interest paid to domestic lenders because that interest is taxed under the Corporation Tax Act of Japan (Act No. 34 of March 31, 1965) ("Corporation Tax Act").

6.2 What tax incentives or other incentives are provided preferentially to foreign lenders? What taxes apply to foreign lenders with respect to their loans, mortgages or other security documents, either for the purposes of effectiveness or registration?

Under the Corporation Tax Act and other local government tax laws, foreign creditors making loans to Japanese domestic borrowers, but not otherwise having a "permanent establishment" in Japan, are not required to pay (i) the national corporation income tax, (ii) the prefectural and municipal inhabitants' tax, or (iii) the prefectural enterprise tax. The effective corporate tax rate for the fiscal years commencing until March 31, 2018 is 29.97% (based on the standard tax rate, including local tax) and the effective corporate tax rate for the fiscal year commencing on or after April 1, 2018 is scheduled to be 29.74%. Activities in Japan such as (i) having a branch office, (ii) performing operating construction work for more than one year, or (iii) having independent agent(s), may constitute having a "permanent establishment" in Japan. If a tax treaty exists between Japan and the country where the foreign lender resides (such as the United States and the United Kingdom), special preferential tax treatment may be applicable to interest income.

A stamp tax is imposed based on the amount of indebtedness evidenced by a loan agreement and can range from JPY 200 to JPY 600,000. A flat fee stamp tax of JPY 200 is required for a guarantee. Collateral agreements such as mortgages and pledge agreements are in general not subject to additional stamp tax. However, certain types of collateral agreements collateralising claims (such as trade receivables) by way of assignment as security (*joto-tanpo*), as opposed to a pledge (*shichi-ken*) may be subject to a fixed stamp duty of JPY 200 applicable to claim assignment agreements.

Registration tax is discussed in question 3.9.

Stamp tax and registration tax apply without regard to the foreign or domestic status of a lender.

6.3 Will any income of a foreign lender become taxable in your jurisdiction solely because of a loan to or guarantee and/or grant of security from a company in your jurisdiction?

No. There is no corporation income tax or individual income tax under the Corporation Tax Act or the Income Tax Act specifically applicable to foreign lenders solely due to the fact they are lending to Japanese borrowers (or accepting a guarantee or security in connection with a loan to a Japanese borrower).

6.4 Will there be any other significant costs which would be incurred by foreign lenders in the grant of such loan/guarantee/security, such as notarial fees, etc.?

No. Documents can be notarised to facilitate compulsory execution in the future. If documents are notarised, a creditor does not need to obtain a court judgment when filing an attachment.

Possible additional fees include (i) process fees based on the Foreign Exchange and Foreign Trade Control Act (Act No. 228 of December 1, 1949) ("Foreign Exchange Act") (mainly attorneys' fees), (ii) attorneys' fees and other fees required to draft contracts and process various registrations, and (iii) tax accountant fees.

6.5 Are there any adverse consequences to a company that is a borrower (such as under thin capitalisation principles) if some or all of the lenders are organised under the laws of a jurisdiction other than your own? Please disregard withholding tax concerns for purposes of this question.

As a basic rule, before starting to lend in Japan, foreign lenders must acquire a licence as a "branch office of a foreign bank" residing in Japan under the Banking Act (Act No. 59 of 1981) or register as a "money lender" under the Money Lending Business Act (Act No. 32 of May 13, 1983).

Based on the Foreign Exchange Act, a foreign lender (including both individuals and corporations) which lends money to a Japanese corporation is required to report to a government authority (such as the Ministry of Finance) if certain conditions are met. In most cases, only *post facto* reporting is applicable, and it is usually not burdensome. Also, there are wide exemptions from the reporting requirement (including, but not limited to, such cases: (i) if the lender of loans is a bank or other financial institutions specified in a Cabinet Order; (ii) if the term of loans does not exceed one year; or (iii) if the amount of loans does not exceed JPY 100 million).

7 Judicial Enforcement

7.1 Will the courts in your jurisdiction recognise a governing law in a contract that is the law of another jurisdiction (a "foreign governing law")? Will courts in your jurisdiction enforce a contract that has a foreign governing law?

Yes; in principle, they will.

Article 7 of the Act on General Rules for Application of Laws (Act No. 78 of June 21, 2006) adopts a "party autonomy rule" whereby the formation and effect of a juridical act shall be governed by the law of the place chosen by the parties at the time of the act.

7.2 Will the courts in your jurisdiction recognise and enforce a judgment given against a company in New York courts or English courts (a "foreign judgment") without re-examination of the merits of the case?

Generally, courts in Japan will enforce a New York or English court judgment without re-examination of the merits; however, courts in Japan may evaluate the merits to the extent necessary to determine that the judgment satisfies the criteria for recognition.

Article 118 of the Code of Civil Procedure (Act No. 109 of June 26, 1996, as amended) ("Code of Civil Procedure") and Article 24 of the Civil Execution Act (Act No. 4 of March 30, 1979, as amended) ("Civil Execution Act") establish the mechanism for recognition and enforcement of foreign judgments.

The Civil Execution Act specifically provides that "the judgment granting execution shall be rendered without reviewing the substance of the judgment of a foreign court"; however, it also provides that (i) the foreign judgment must be final and non-appealable, and (ii) the judgment must fulfil the four conditions set out in Article 118 of the Code of Civil Procedure, as follows:

(i) The foreign court must have had jurisdiction over the defendant.

(ii) The defendant must have received adequate service of process.

(iii) The foreign judgment must not violate the public policy of Japan. Particular types of awards, such as punitive damages, may violate this requirement. When a public policy defence is raised, a Japanese court will look beyond the judgment to the underlying transaction. A defendant can also raise a public policy defence if the procedures through which the judgment was rendered were not consistent with Japanese public policy.

(iv) Reciprocity is assured. Japan has reciprocity with both the United States and England.

7.3 Assuming a company is in payment default under a loan agreement or a guarantee agreement and has no legal defence to payment, approximately how long would it take for a foreign lender to (a) assuming the answer to question 7.1 is yes, file a suit against the company in a court in your jurisdiction, obtain a judgment, and enforce the judgment against the assets of the company, and (b) assuming the answer to question 7.2 is yes, enforce a foreign judgment in a court in your jurisdiction against the assets of the company?

It differs depending upon the circumstances, but generally it would take approximately six months to one year to complete such proceedings.

7.4 With respect to enforcing collateral security, are there any significant restrictions which may impact the timing and value of enforcement, such as (a) a requirement for a public auction, or (b) regulatory consents?

If a secured lender intends to foreclose the secured assets non-consensually, it may file a petition for a public auction of the collateral with the court, if applicable (typically, real estate). Before payment is made by the winning bidder at the real estate auction, a private sale would take place if there is a consensual arrangement with the debtor.

Other than regulatory consents that may be specific to the nature of the collateral as a regulated asset, no general regulatory consents are required to enforce collateral.

7.5 Do restrictions apply to foreign lenders in the event of (a) filing suit against a company in your jurisdiction, or (b) foreclosure on collateral security?

In general, there are no restrictions on foreign lenders seeking to file suits against a company in Japan or to foreclosure on collateral.

7.6 Do the bankruptcy, reorganisation or similar laws in your jurisdiction provide for any kind of moratorium on enforcement of lender claims? If so, does the moratorium apply to the enforcement of collateral security?

Yes, the in-court insolvency proceedings described below provide a stay against the enforcement of certain claims.

Japanese law provides for two types of restructuring proceedings (Corporate Reorganisation and Civil Rehabilitation) and two types of liquidation proceedings (Bankruptcy and Special Liquidation).

In Corporate Reorganisation proceedings, unsecured and secured creditors are stayed from exercising their rights (security interests) outside of the proceedings.

In Civil Rehabilitation proceedings, unsecured creditors are stayed from exercising their rights outside of the proceedings, but secured creditors are not stayed from exercising their security interests (although secured creditors may become subject to a suspension order by the court having the effect of a temporary stay).

In Bankruptcy and Special Liquidation proceedings, unsecured creditors are stayed from exercising their rights outside of the proceedings, but secured creditors are not stayed from exercising their security interests (although secured creditors may become subject to a suspension order by the court in Special Liquidation proceedings).

7.7 Will the courts in your jurisdiction recognise and enforce an arbitral award given against the company without re-examination of the merits?

Yes. The Code of Civil Procedure does not specifically discuss the enforcement of a foreign arbitral award. However, Article 45 of the Arbitration Law (Act No. 138 of August 1, 2003) discusses recognition of arbitral awards generally, providing that "an arbitral award (irrespective of whether or not the place of arbitration is in the territory of Japan; this shall apply throughout this chapter) shall have the same effect as a final and conclusive judgment". The Arbitration Law is based upon the UNCITRAL Model Law on International Commercial Arbitration. Japan is also party to various international protocols and bilateral treaties, such as the New York Convention that addresses recognition and enforcement of foreign arbitral awards. Japan acceded to the New York Convention on June 20, 1961 and the Convention entered into force on September 18, 1961.

8 Bankruptcy Proceedings

8.1 How does a bankruptcy proceeding in respect of a company affect the ability of a lender to enforce its rights as a secured party over the collateral security?

As stated in question 7.6 above, in Corporate Reorganisation proceedings, secured creditors are stayed from enforcing their security interests. The claims of secured creditors will be treated as secured claims up to the value of the collateral as of the date of the commencement of the Corporate Reorganisation proceedings. Such value will be determined by way of an amicable settlement between the parties, a valuation order or a judgment by the court. Secured creditors will receive repayment in accordance with the reorganisation plan as approved by the borrower's creditors and confirmed by the court. In proceedings other than Corporate Reorganisation, secured creditors may enforce their security interests outside of the relevant proceedings. In practice, however, secured creditors sometimes refrain from exercising their security interests in exchange for settlements where the value of the relevant collaterals are agreed upon and repaid.

8.2 Are there any preference periods, clawback rights or other preferential creditors' rights (e.g., tax debts, employees' claims) with respect to the security?

In a Corporate Reorganisation proceeding, the Trustee exercises the right of avoidance. In the case of a Civil Rehabilitation proceeding, the Supervisor exercises the right of avoidance.

If a loan is "new money" and the collateral is fair equivalent value, the secured transaction (collateralisation) is, as a basic rule, not subject to avoidance. However, if the change of the type of the property (e.g. from real property to cash) gives rise to an actual risk of the debtor's disposition prejudicial to the unsecured ordinary creditors (in a Corporate Reorganisation, secured and unsecured creditors), and the debtor had such intention and the lender was aware of the debtor's intention as of the time of the transaction, such transaction may be subject to avoidance.

If a secured creditor obtained security for an existing debt knowing that the debtor became "unable to pay debts", the lien could be avoided. If collateralisation for an existing debt was carried out within 30 days prior to the debtor becoming "unable to pay debts" in the event where the debtor did not owe any duty to provide such security, it could also be avoided.

8.3 Are there any entities that are excluded from bankruptcy proceedings and, if so, what is the applicable legislation?

Among the four insolvency proceedings stated in question 7.6 above, Civil Rehabilitation and Bankruptcy are available for both legal entities (including companies) and individuals, while Corporate Reorganisation and Special Liquidation are limited to stock companies (*kabushiki-kaisha*). Note that there is a special legislation that applies to Corporate Reorganisation, Civil Rehabilitation and Bankruptcy proceedings of financial institutions (including banks).

8.4 Are there any processes other than court proceedings that are available to a creditor to seize the assets of a company in an enforcement?

A secured creditor may exercise its rights independently from the Civil Rehabilitation, Special Liquidation or Bankruptcy (however, in the Civil Rehabilitation and Special Liquidation, such exercise may be subject to a suspension order by the court).

9 Jurisdiction and Waiver of Immunity

9.1 Is a party's submission to a foreign jurisdiction legally binding and enforceable under the laws of your jurisdiction?

Under the Code of Civil Procedure, the amendment of which has been effective since April 1, 2012, the parties' agreement on the foreign (non-Japanese) jurisdiction is, as a basic rule, legally valid and enforceable if:

(i) it is made with respect to an action based on certain legal relationships and made in writing;

(ii) the designated foreign court is able to exercise its jurisdiction over the case by the foreign law and in fact; and

(iii) the exclusive jurisdiction of a court of Japan over an action in question is not provided for in laws or regulations.

Please note that jurisdiction over actions relating to (i) consumer contracts, or (ii) labour relationships are subject to the independent rule specified under the amended Code of Civil Procedure.

See question 7.2 regarding recognition of foreign judgments.

9.2 Is a party's waiver of sovereign immunity legally binding and enforceable under the laws of your jurisdiction?

A waiver of sovereign immunity is legally valid and enforceable subject to the conditions in the Act on the Civil Jurisdiction of Japan with respect to a Foreign State, etc. (Act No. 24 of April 24, 2009) (the "Immunity Act").

The Immunity Act is based on the United Nations Convention on Jurisdictional Immunities of States and Their Property (2004) and is effective from April 1, 2010.

10 Licensing

10.1 What are the licensing and other eligibility requirements in your jurisdiction for lenders to a company in your jurisdiction, if any? Are these licensing and eligibility requirements different for a "foreign" lender (i.e. a lender that is not located in your jurisdiction)? In connection with any such requirements, is a distinction made under the laws of your jurisdiction between a lender that is a bank *versus* a lender that is a non-bank? If there are such requirements in your jurisdiction, what are the consequences for a lender that has not satisfied such requirements but has nonetheless made a loan to a company in your jurisdiction? What are the licensing and other eligibility requirements in your jurisdiction for an agent under a syndicated facility for lenders to a company in your jurisdiction?

See questions 5.1, 5.2 and 6.5.

11 Other Matters

11.1 Are there any other material considerations which should be taken into account by lenders when participating in financings in your jurisdiction?

No; however, foreign lenders should note that court dockets in Japan are not available online and are not accessible to the general public. In general, there is also less transparency in court proceedings in Japan than in some jurisdictions, fewer hearings and *ex parte* communications are permitted. In particular, this lack of publicly available information can pose concerns for distressed debt investors regarding trading restrictions and non-public information.

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Chapter 57

Jersey

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1 Overview

1.1 What are the main trends/significant developments in the lending markets in your jurisdiction?

Locally, there has been continued activity in relation to the development of the financial services businesses. There has been a further round of consolidation and private equity investment into Jersey-based trust and company administration businesses and in most cases leverage has been used in relation to acquisitions.

In respect of real estate finance, lending to Jersey corporate structures holding foreign real estate assets, including limited partnerships and unit trusts, continues to be significant. The general perception is that the acquisition activity in respect of large real estate assets, particularly in prime London locations, has decreased which has had an impact on the origination of new loans; however, refinancing and renewals of existing facilities continue apace.

In contrast, origination in the fund finance sector has remained strong, with high volumes of both new loans as well as re-financings of existing facilities. Facility sizes range from €50 million to over €1 billion, including capital call and subscription facilities as well as co-investment and GP leverage.

Similarly, we have noted a steady stream of large acquisition financings for a variety of asset classes, with the largest facilities being used in connection with the purchase or the post-acquisition leveraging of large infrastructure assets. In the infrastructure space, large debt funds have been very active.

Listings on The International Stock Exchange of public and more specialist debt securities remain popular, as do the use of Jersey corporates as issuers for high-yield and corporate bonds.

1.2 What are some significant lending transactions that have taken place in your jurisdiction in recent years?

In the real estate sector, we have seen large numbers of facilities relating to UK real estate assets, typically ranging from £30 million to £150 million, although we have provided advice alongside English counsel on several larger facilities, including a £430 million facility to a listed REIT.

We have advised on several fund finance transactions approaching €1 billion. A significant amount of lending to investment funds has been originated by Jersey-based banks.

Acquisition finance facilities have included facilities for infrastructure projects of over £500 million and leveraged facilities for private equity acquisitions of over US$1 billion.

Despite a strong corporate bond market over the past few years, we continue to see large revolving credit facilities for quality listed companies, including facility amounts of over $1 billion.

Note issuance by Jersey-issuing entities has ranged from $200 million to over $1 billion.

2 Guarantees

2.1 Can a company guarantee borrowings of one or more other members of its corporate group (see below for questions relating to fraudulent transfer/financial assistance)?

Yes, guarantees are commonly used by group companies. They are usually created by written agreement. Corporate benefit should be considered and this is covered in greater detail at question 2.2 below.

The Security Interests (Jersey) Law 2012 (the "**Security Interests Law**") expressly provides that a security interest can be created to secure the obligation of a third party, which simplifies documentation and removes the need to include a limited recourse guarantee in Jersey security agreements.

2.2 Are there enforceability or other concerns (such as director liability) if only a disproportionately small (or no) benefit to the guaranteeing/securing company can be shown?

A Jersey company has unlimited corporate capacity under the Companies (Jersey) Law 1991 (the "**Companies Law**").

When a company enters into a finance transaction, a transacting party should consider whether there is corporate benefit for the company. There is a risk that a company could seek to have the transaction set aside on the basis that the directors approving the transaction were acting outside their statutory duty to act in the best interests of the company. This can happen where:

- there is little or no corporate benefit to the company; and
- the transacting party knows or ought to know that there is little or no corporate benefit.

This risk is avoided if both:

- all the shareholders of the Jersey company authorise or ratify the particular transaction; and
- the Jersey company can pay its debts as they fall due at the time of, and immediately following the entry into the transaction.

If there is no discernible corporate benefit to entry into a finance transaction, there is also a risk that a transaction could be set aside on the company's bankruptcy.

2.3 Is lack of corporate power an issue?

Article 18 of the Companies Law removed the concept of external *ultra vires*, meaning that nothing in a company's Memorandum or Articles of Association can limit the power of a Jersey company. That being said, the Memorandum and Articles of Association should still be reviewed to ensure there are no limits on the authority of the directors to enter into the required documents.

2.4 Are any governmental or other consents or filings, or other formalities (such as shareholder approval), required?

As per the above, shareholder approval is advisable if there are corporate benefit concerns. A guarantee does not need to be registered in Jersey.

2.5 Are net worth, solvency or similar limitations imposed on the amount of a guarantee?

No, although the solvency of the company should be considered when entering into a guarantee. If a company enters into a transaction with a person for cause (similar to consideration under English law) the value of which, in money or equivalent, is significantly less than the value of the cause provided by that person, the transaction may be susceptible to challenge as a transaction at an undervalue and attacked by (i) the Viscount of the Royal Court of Jersey (the insolvency officer of the Royal Court) (the "**Viscount**") in a *désastre* under the Bankruptcy (*Désastre*) (Jersey) Law 1990 (the "**Désastre Law**") and (ii) by a liquidator in a creditor's winding up under the Companies Law.

This applies if the transaction was entered into during the five years preceding the commencement of the *désastre* or winding up (no time limit applies to transactions involving persons connected with or an associate of the insolvent debtor).

However, a transaction is not vulnerable to attack as a transaction at an undervalue if either:

- The relevant company:
  - was able to pay its debts as they fall due at the time it entered into the transaction; and
  - did not become insolvent on a cash flow basis as a result of entering into the transaction.
- The court is satisfied that both:
  - the company entered into the transaction in good faith for the purpose of carrying on its business; and
  - at the time it entered into the transaction, there were reasonable grounds for believing that the transaction would benefit the company.

2.6 Are there any exchange control or similar obstacles to enforcement of a guarantee?

If court proceedings are brought against a guarantor company, the enforceability of that company's obligations can be qualified if the following Jersey customary law rights of a surety are available to it:

- *Droit de discussion* – this is the right to require that recourse is made against the assets of the borrower and that those assets are exhausted before any claim is enforced against the guarantor.
- *Droit de division* – this is the right to require that liability of co-guarantors is divided or apportioned between them.

It is market practice for a lender to require a specific waiver of these rights.

3 Collateral Security

3.1 What types of collateral are available to secure lending obligations?

Common types of collateral that are secured are: real estate; shares; units in a unit trust; bank accounts; and contract rights.

3.2 Is it possible to give asset security by means of a general security agreement or is an agreement required in relation to each type of asset? Briefly, what is the procedure?

It is possible to take "a debenture style" security under the Security Interests Law over all present and future intangible movable property held by the grantor in Jersey from time to time. The attachment of a security interest to collateral is not affected by the security agreement providing an express right of the grantor to deal with the collateral free from the security interest and without a duty to account for the proceeds or to replace the collateral. Jersey law does not have a concept of a floating charge. The security would be taken by way of a security interest agreement entered into under the 2012 Law. In order for a security interest to attach to collateral (on which the security becomes enforceable against the grantor), the following conditions must be satisfied:

- Value must have been given in respect of the security agreement. Value means something sufficient to support an onerous contract, and includes an antecedent debt or liability. It does not matter to whom value is given or from whom the value arises.
- The grantor must have rights, or the power to grant rights to a secured party, in the collateral. A trustee can therefore grant valid security under the Security Interests Law.
- The secured party has possession or control of the collateral and/or the security agreement is in writing and contains a description of the collateral that is sufficient for it to be identified. Even where there is no agreement in writing, there must still be a "security agreement".

Perfection of a security interest is necessary for the purposes of priority and gives protection against third parties, which is particularly important in insolvency. The method of attachment and perfection will depend on the type of collateral secured. The three ways for the secured party to obtain perfection are:

- by possession of documentary intangibles such as negotiable instruments or bearer securities;
- by control of the collateral such as bank accounts (including security accounts) and investment securities; and/or
- by registration of a financing statement on the Jersey Security Interests Register in its favour in respect of the collateral.

3.3 Can collateral security be taken over real property (land), plant, machinery and equipment? Briefly, what is the procedure?

Security can be taken over real estate by way of (i) hypothec (for freehold and flying freehold properties (where individual parts of a property are sold for exclusive ownership)) and the hypothec can be judicial or conventional or by way of (ii) share security (for share transfer properties where a Jersey holding company owns the freehold title to the real estate). A hypothec is a charge which can attach to freehold and flying freehold properties. Paper leases cannot be hypothecated, while contract leases can be hypothecated if the lease terms expressly permit it. Hypothecs can be specific (that is, over one property) or general (that is, attaching to all real estate that the borrower owns at the date of registration).

Share security would be taken by way of a security interest agreement entered into under the 2012 Law.

In relation to plant, machinery and equipment, the only method of creating security over tangible movables in Jersey is by way of pledge. To pledge property there must be actual physical (as opposed to constructive) delivery of the tangible movable property pledged into the creditor's possession.

There is a right of retention. As a matter of customary law (absent any Jersey judicial authority on this point) the creditor should have an implied right of sale when the grantor is in default and there is likely to be an express power of sale in the pledge document.

3.4 Can collateral security be taken over receivables? Briefly, what is the procedure? Are debtors required to be notified of the security?

Typically, security in respect of contract rights and receivables is created by way of a security interest agreement entered into under the 2012 Law by way of description and registration. Although it is no longer necessary to give notice to the counterparty, there are usually advantages to doing so (for example, to obtain, by way of acknowledgment to the notice a waiver of any conflicting provisions in the underlying contract and/or a confirmation that the counterparty will make payments directly to the secured party).

Common types of receivables include:

- Rent payable under a lease agreement.
- A general partner's right to call for capital from the partners of a limited partnership.
- Debts and other rights to the payment of money.
- Rights under performance contracts.
- Bank accounts into which the receivables are paid and other cash deposited with banks.

The Security Interests Law also contains specific provisions in relation to outright assignments of receivables which are defined as monetary entitlements arising from the supply of goods and services (other than insurance services) or the supply of energy.

3.5 Can collateral security be taken over cash deposited in bank accounts? Briefly, what is the procedure?

Yes, this is a common form of security taken in Jersey. The method will depend on whether the account is with the secured party or a third party bank.

Security will be created by way of a security interest agreement under the Security Interests Law. Control would be obtained by the:

- account being transferred into the name of the secured party with the written agreement of the grantor and the account bank;
- account bank agreeing in writing to act on the secured party's instructions directing disposition of funds in the account;
- account being assigned to the secured party and written notice of such being given to the account bank; or
- account bank being the secured party.

Typically, security over third party bank accounts is taken by assignment. Although not necessary to perfect the security, it is usual to obtain an acknowledgment of the notice from the account bank, which will include, for example, a waiver of:

- Any terms and conditions which may restrict or prohibit the creation of the security.
- Its rights of set-off over the account.

3.6 Can collateral security be taken over shares in companies incorporated in your jurisdiction? Are the shares in certificated form? Can such security validly be granted under a New York or English law governed document? Briefly, what is the procedure?

Yes, security can be taken over shares in a Jersey company in a certificated format. Security would be taken by way of a security interest agreement under the Security Interests Law. Control would be obtained by the secured party either:

- being registered as the holder of the securities; or
- having possession of the certificate representing the securities.

Security cannot be validly granted over shares in a Jersey company under a New York or English law governed document.

3.7 Can security be taken over inventory? Briefly, what is the procedure?

Jersey law does not have a concept of a floating charge. Therefore, security over tangible movables such as inventory in Jersey would have to be taken by way of pledge. Please see question 3.3 above.

3.8 Can a company grant a security interest in order to secure its obligations (i) as a borrower under a credit facility, and (ii) as a guarantor of the obligations of other borrowers and/or guarantors of obligations under a credit facility (see below for questions relating to the giving of guarantees and financial assistance)?

Yes – a typical security package we see in Jersey is: (i) borrower grants security over any accounts it holds in Jersey; (ii) borrower's shareholder(s) grant(s) security in respect of the shares in the borrower; and (iii) the lender of any intercompany loans to the borrower grants security over those contract rights.

3.9 What are the notarisation, registration, stamp duty and other fees (whether related to property value or otherwise) in relation to security over different types of assets?

There are registration fees associated with using the securities register. These are outlined on the Registry website:

- registration – £8 per year of registration up to a maximum fee of £150 if the registration will run longer than 20 years (there is no concept of infinite registration);
- discharge – no fee;
- amendment of registration – £8;
- extension of period of registration – same cost scheme as above;
- global change of multiple registrations (other than expiry date) – £100;
- search – £4 to view a financing statement; and
- filing a change demand – £25.

Stamp duty is payable when a lender registers security over real estate situated in Jersey. Stamp duty is calculated at the rate of 0.5% of the amount of debt secured over the property in favour of the lender, plus a Court fee of £80.

Land transaction tax ("**LTT**") is payable when a lender takes security over a share transfer property situated in Jersey and is calculated at a rate of 0.5% of the amount of the debt to be secured, plus an administration fee of £80. LTT applies only in relation to residential property, where the articles of the property owning company confer rights of occupation to their shareholders.

There are no relevant notary fees.

3.10 Do the filing, notification or registration requirements in relation to security over different types of assets involve a significant amount of time or expense?

For security which is created over intangible moveable property under the Security Interests Law, the registration requirements do not involve a signification amount of time or expense.

For security which is registered over Jersey immovable property, the Billet (the acknowledgment document creating a judicial hypothec) or the contract creating the charge (in the case of a simple conventional hypothec) must be registered with the Royal Court of Jersey, which can only take place on a Friday afternoon (subject to Court holidays). The stamp duty must be paid at the time of registration. Once registered, the Billet or contract (as the case may be) becomes a matter of public record.

3.11 Are any regulatory or similar consents required with respect to the creation of security?

A consent should be obtained from the grantor prior to the registration of the security interest on the Jersey Security Interests Register, pursuant to which the grantor consents to the registration and for any personal data to be publicly available.

3.12 If the borrowings to be secured are under a revolving credit facility, are there any special priority or other concerns?

The definition of secured obligations/liabilities in the security agreement should provide for further advances to ensure that the priority of the original advance will not be lost in respect of further advances.

3.13 Are there particular documentary or execution requirements (notarisation, execution under power of attorney, counterparts, deeds)?

No, there are not.

4 Financial Assistance

4.1 Are there prohibitions or restrictions on the ability of a company to guarantee and/or give security to support borrowings incurred to finance or refinance the direct or indirect acquisition of: (a) shares of the company; (b) shares of any company which directly or indirectly owns shares in the company; or (c) shares in a sister subsidiary?

(a) Shares of the company

The concept of financial assistance was abolished in Jersey in 2008. Jersey companies are not prohibited from giving financial assistance for the acquisition of their own shares. If financial assistance raises questions relating to corporate benefit, or amounts to a distribution, the relevant statutory procedures must be complied with.

(b) Shares of any company which directly or indirectly owns shares in the company

Jersey companies are not prohibited from giving financial assistance for the acquisition of shares of any company which directly or indirectly owns shares in the company. If financial assistance raises questions relating to corporate benefit, or amounts to a distribution, the relevant statutory procedures must be complied with.

(c) Shares in a sister subsidiary

Jersey companies are not prohibited from giving financial assistance for the acquisition of shares of shares in a sister subsidiary. If financial assistance raises questions relating to corporate benefit, or amounts to a distribution, the relevant statutory procedures must be complied with.

5 Syndicated Lending/Agency/Trustee/Transfers

5.1 Will your jurisdiction recognise the role of an agent or trustee and allow the agent or trustee (rather than each lender acting separately) to enforce the loan documentation and collateral security and to apply the proceeds from the collateral to the claims of all the lenders?

Jersey law recognises the concept of agency and trust relationships and accordingly an agent or trustee would be able to enforce the loan documentation and collateral security and apply the proceeds in the manner set out in the loan agreement or intercreditor agreement.

5.2 If an agent or trustee is not recognised in your jurisdiction, is an alternative mechanism available to achieve the effect referred to above which would allow one party to enforce claims on behalf of all the lenders so that individual lenders do not need to enforce their security separately?

This is not applicable.

5.3 Assume a loan is made to a company organised under the laws of your jurisdiction and guaranteed by a guarantor organised under the laws of your jurisdiction. If such loan is transferred by Lender A to Lender B, are there any special requirements necessary to make the loan and guarantee enforceable by Lender B?

The transfer provisions will usually be set out in the loan agreement and guarantee and these should be complied with.

If there are no such transfer provisions, the benefit of the loan and the guarantee should be validly assigned to Lender B in order to ensure that the guarantee is enforceable by Lender B. For completeness, notice of the assignment should be given to the company and the guarantor. If the loan is not fully utilised and Lender A was under an obligation to make further advances, the loan would require to be novated as opposed to transferred. If the loan is not novated to Lender B this could have implications on the enforceability of the guarantee.

6 Withholding, Stamp and Other Taxes; Notarial and Other Costs

6.1 Are there any requirements to deduct or withhold tax from (a) interest payable on loans made to domestic or foreign lenders, or (b) the proceeds of a claim under a guarantee or the proceeds of enforcing security?

No, there are not.

6.2 What tax incentives or other incentives are provided preferentially to foreign lenders? What taxes apply to foreign lenders with respect to their loans, mortgages or other security documents, either for the purposes of effectiveness or registration?

Foreign lenders do not receive preferential tax treatment when compared to Jersey lenders. However, Jersey can generally ensure tax neutrality, and avoidance of double taxation.

6.3 Will any income of a foreign lender become taxable in your jurisdiction solely because of a loan to or guarantee and/or grant of security from a company in your jurisdiction?

No, it will not.

6.4 Will there be any other significant costs which would be incurred by foreign lenders in the grant of such loan/guarantee/security, such as notarial fees, etc.?

Please see questions 3.9 and 3.10 above.

6.5 Are there any adverse consequences to a company that is a borrower (such as under thin capitalisation principles) if some or all of the lenders are organised under the laws of a jurisdiction other than your own? Please disregard withholding tax concerns for purposes of this question.

No, there are not.

7 Judicial Enforcement

7.1 Will the courts in your jurisdiction recognise a governing law in a contract that is the law of another jurisdiction (a "foreign governing law")? Will courts in your jurisdiction enforce a contract that has a foreign governing law?

The courts in Jersey will recognise a foreign governing law provided it is a valid choice of law for the issue in question upon proof of the relevant provisions of the governing law.

7.2 Will the courts in your jurisdiction recognise and enforce a judgment given against a company in New York courts or English courts (a "foreign judgment") without re-examination of the merits of the case?

The enforcement of foreign judgments is governed by the Judgments (Reciprocal Enforcement) (Jersey) Law 1960. If a final and conclusive judgment under which a sum of money is payable (not being a sum payable in respect of taxes or other charges of a like nature or in respect of a fine or other penalty) were obtained in a Reciprocal Enforcement Court (as defined below) having jurisdiction in a case against a company, such judgment would, on application to the Royal Court of Jersey, be registered without reconsidering its merits and would thereafter be enforceable.

The Reciprocal Enforcement Courts means the following superior courts: (a) in England and Wales, the Supreme Court of the United Kingdom, the Court of Appeal and the High Court of Justice; (b) in Scotland, the Supreme Court of the United Kingdom, the Court of Session and the Sheriff Court; (c) in Northern Ireland, the Supreme Court of the United Kingdom and the Court of Judicature of Northern Ireland; (d) in the Isle of Man, Her Majesty's High Court of Justice of the Isle of Man (including the Staff of Government/Appeal Division); and (e) in Guernsey, the Royal Court of Guernsey and the Court of Appeal of Guernsey. The creditor of such a judgment must apply to have it enforced in Jersey within six years from the date the decision is handed down, or the date of the judgment on the last appeal. Such registration will not require the consideration of the merits of a case.

Where the above law does not apply, including New York judgments, foreign judgments will be recognised at customary/common law. Subject to the principles of private international law, by which for example foreign judgments may be impeachable, as applied by Jersey law (which are broadly similar to the principles applied under the common law rules of England), if a Foreign Judgment (as defined below) were obtained the judgment creditor must begin a fresh action in the Royal Court of Jersey, relying on the unsatisfied Foreign Judgment as a cause of action. The matter will usually be determined summarily without a full trial. The judgment debtor can oppose the application for summary judgment and/or defend the claim, but there are only limited grounds on which enforcement will be refused and a full factual enquiry is rarely necessary.

The grounds for refusing to enforce a judgment are substantially similar to the grounds on which registration can be set aside (i.e the foreign court had no jurisdiction, or there were procedural inadequacies in obtaining the Foreign Judgment). If the court is satisfied that the judgment must be enforced, it will be entered in favour of the judgment creditor and be enforceable in Jersey as a domestic judgment.

7.3 Assuming a company is in payment default under a loan agreement or a guarantee agreement and has no legal defence to payment, approximately how long would it take for a foreign lender to (a) assuming the answer to question 7.1 is yes, file a suit against the company in a court in your jurisdiction, obtain a judgment, and enforce the judgment against the assets of the company, and (b) assuming the answer to question 7.2 is yes, enforce a foreign judgment in a court in your jurisdiction against the assets of the company?

(a) Proceedings in respect of a debt for a liquidated sum can be commenced by way of a simple summons, which can be prepared and served within a few days. The summons must be served four clear days before the return date to which the company is summoned. If the company does not attend at the return date, judgment in default can be obtained (i.e. in as quickly as two weeks).

If the company defends the claim, the Royal Court of Jersey will place the action on the pending list (effective immediately). An application for summary judgment can be brought at this time, which we expect could be heard and determined within 4–6 weeks.

If the application for summary judgment is defended, and is unsuccessful, the matter would proceed to a trial and could take up to one year for it to be heard and a subsequent judgment to be issued.

The length of time to effect enforcement depends on the process used.

A monetary judgment is immediately enforceable by distraint against the judgment debtor's assets. The Viscount will take possession of and effect a sale of the debtor's assets and apply the proceeds in satisfaction of the judgment, subject to certain notification requirements. The timing of this process depends on the Viscount's availability and the number of assets to be dealt with.

If the debtor owns property in Jersey, orders can be sought one month following the issue of a court judgment (provided it remains unsatisfied), for an "*Acte Vicomte chargé d'écrire*". The effect of this declaration is that if the judgment is not satisfied within a further two months, the debtor's property will be deemed to have been renounced. At that time a creditor can seek orders for "*dégrèvement*" (for immoveable property) and "*réalisation*" (for moveable property). The timing of either of these enforcement processes once commenced is difficult to ascertain as once orders are made, the sale and dealing of the assets is conducted by the *Attournées*. However, we generally understand that, from the making of an order, a *dégrèvement* process (including the hearing) may take approximately 4–6 weeks. Following the hearing the creditor who elects to take the property, subject to claims of superior lenders, will be immediately entitled to the asset. The timeframe for a *réalisation* may take approximately 2–3 months depending on the liquidity of the assets.

An application can also be made by a creditor of a company with a liquidated claim exceeding £3,000 that it be declared *en désastre*, on the basis that it is unable to pay its debts as it falls due (please also see question 8.4). Such an application can be made quickly (within 48 hours). If a declaration is made by the Royal Court of Jersey, and after a one month period within which the debtor can object has expired, the Viscount will begin the process of collecting in the debtor's assets and distributing them to all creditors on the basis of a statutory waterfall. It is difficult to give an estimate to the Viscount's process, but generally a creditor can expect this to take approximately six to 18 months (depending on the complexity).

(b) Once a foreign judgment is registered in Jersey, the creditor must serve a notice of registration on the debtor providing the timeframe (generally 14 or 28 days) within which the debtor may apply to have the registration set aside. Once the time for challenging registration has passed, the foreign judgment is enforceable from that point on in the same way as a domestic judgment.

7.4 With respect to enforcing collateral security, are there any significant restrictions which may impact the timing and value of enforcement, such as (a) a requirement for a public auction, or (b) regulatory consents?

There is no requirement for a public auction in relation to the enforcement of security granted under the Security Interests Law. Generally speaking, enforcement does not require consent from the Viscount or an order from a court. Please also see question 8.4 in relation to enforcement of security.

However, enforcement of security over real estate in Jersey (see question 8.4 for further detail), will involve the Royal Court of Jersey and the Viscount and will be subject to the requirements of Article 27 of the Désastre Law which provides that the Viscount may sell the property by public auction or public tender.

7.5 Do restrictions apply to foreign lenders in the event of (a) filing suit against a company in your jurisdiction, or (b) foreclosure on collateral security?

No restrictions apply to foreign lenders beyond those which apply to Jersey lenders.

7.6 Do the bankruptcy, reorganisation or similar laws in your jurisdiction provide for any kind of moratorium on enforcement of lender claims? If so, does the moratorium apply to the enforcement of collateral security?

Pursuant to Article 10 of the Bankruptcy (*Désastre*) (Jersey) Law 1990 there is a statutory moratorium on actions and enforcement, with effect from the date of the declaration of *en désastre*. Legal/enforcement action may only be commenced or continued with consent of the Viscount or by order of the Court. If the creditor is a company, any transfer of shares not made with the sanction of the Viscount or any alteration in the status of the company's members which is made after the declaration is void.

However, a secured party under the Security Interests (Jersey) Law 2012 is not prevented from exercising a power under Part 7 of the Security Interests (Jersey) Law 2012 in relation to the relevant collateral, including a transfer of shares. No consent of the Viscount nor order of the Court is required.

7.7 Will the courts in your jurisdiction recognise and enforce an arbitral award given against the company without re-examination of the merits?

Arbitration is rarely used as a method of commercial dispute resolution in Jersey. However, domestic arbitral awards are enforceable in Jersey with leave of the court under The Arbitration (Jersey) Law 1998 (the "**Arbitration Law**").

In addition to the domestic procedure above, the Arbitration Law provides that a foreign arbitral award handed down in a country that is a signatory to the New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards 1958 (the "**New York Convention**") is enforceable as if it were a domestic arbitral award.

Further, other foreign awards from certain non-New York Convention states may also be enforceable under the Arbitration Law if the state in question is a signatory to the Geneva Convention on the Execution of Foreign Arbitral Awards 1927 ("**Geneva 1927 Convention**") in the same way as a domestic award or "by action".

Such awards must meet certain standards. They are recognised if the arbitration:

a) was made pursuant to an agreement for arbitration that was valid under the law by which it is governed;
b) was made by the tribunal provided for in the agreement or constituted in a manner agreed by the parties;
c) was made in conformity with the relevant law governing arbitration;
d) is final in the relevant jurisdiction;
e) conforms to the definition of arbitration under Jersey law; and
f) enforcement would not be contrary to the law, or public policy of Jersey.

8 Bankruptcy Proceedings

8.1 How does a bankruptcy proceeding in respect of a company affect the ability of a lender to enforce its rights as a secured party over the collateral security?

In the event of a declaration of *en désastre* under Article 3 of the Désastre Law, the property and powers of a company vest in the Viscount and the Désastre Law states that no further enforcement action may be taken against the company in respect of debts which are provable in a *désastre*. In the case of a creditors' winding up under Chapter 4 of Part 21 of the Companies Law, although there is no automatic vesting, the liquidator has similar powers to the Viscount and the Companies Law provides that after commencement of the creditors' winding up, no further action shall be taken or proceeded with against the company except by leave of the court.

Notwithstanding the above, following the implementation of the Security Interests Law, there is greater protection available to a secured party with a security interest in the event of insolvency of the company so that a secured party can, without the consent of the Viscount, and without an order of the court, exercise a power of enforcement under the Security Interests Law in relation to the relevant collateral. The secured party's powers to appropriate or sell the collateral will not be affected by the insolvency.

However, the provisions of Jersey law enabling the setting aside of transactions at an undervalue and preferences still apply. A security interest will be void against the Viscount or a liquidator and the company's creditors, if it is not perfected before the grantor becomes 'bankrupt' – 'bankrupt' referring to any formal Jersey state of *désastre*, per Article 57 of the Security Interests Law.

8.2 Are there any preference periods, clawback rights or other preferential creditors' rights (e.g., tax debts, employees' claims) with respect to the security?

Under the Security Interests Law, a secured party with a perfected security interest takes in priority to any other creditor. If the secured party has sold or appropriated the collateral and the net value or proceeds of sale (as appropriate) of the collateral exceeds the amount of the debt owed to the secured party, the secured party must pay the amount of any resulting surplus in the following order:

- Any person who has a subordinate security interest in the collateral and has registered a financing statement over that security interest (where the registration remained effective immediately before the appropriation or sale).
- Any other person (other than the grantor) who has given the secured party notice that that person claims an interest in the collateral, and in respect of which the secured party is satisfied that that person has a legally enforceable interest in the collateral.
- The grantor.

Under the Security Interests (Jersey) Law 1983 (the "**1983 Security Interests Law**"), the secured party must apply the proceeds of sale in the following order:

- Payment of the costs and expenses of the sale.
- Discharge of any prior security interest.
- Discharge of all monies properly due in relation to the obligation secured by the security agreement.
- Payment, in due order of priority, of the secured parties whose security interests were created after those being enforced under the security agreement.
- In relation to the balance (if any remains), payment to the grantor or, if the grantor is bankrupt or is subject to any other judicial arrangement due to its insolvency, to the Viscount, receiver or other proper officer.

  Money or monies in a bank account must be applied under the 1983 Security Interests Law as if they were proceeds of sale.

  If more than one creditor holds the same security interest (and each security interest is created under the Security Interests Law 1983) over the same asset, priority is determined by the date of creation of the security interest.

As stated above, if a declaration for *en désastre* is made, a secured party under the Security Interests Law is entitled to enforce their security over the collateral, which will not fall into the *désastre* estate. Once this has occurred, any surplus will fall into the *désastre* estate to be dealt with by the Viscount in the usual way.

Creditors who hold a judicial or conventional hypothec registered against real estate are entitled to a preference over the proceeds of sale of any property on which their charge is secured. If there are a number of registered hypothec, preference is determined by the date of creation. This is not subject to any other preference or clawback rights. Where the asset owner has been declared *en désastre*, the collateral will fall into the *désastre* estate and the Viscount will take the collateral subject to the hypothec.

8.3 Are there any entities that are excluded from bankruptcy proceedings and, if so, what is the applicable legislation?

The Désastre Law sets out the persons in respect of whose property an *en désastre* declaration can be made, and includes any person:

(a) who is, or was, at any time within the period of 12 months immediately preceding the date of the application, ordinarily resident in Jersey;

(b) who carries on, or has carried on, at any time within the period of three years immediately preceding the date of the application, business in Jersey;

(c) who has in Jersey immovable property capable of realisation at the time of the application;

(d) who, being a company, is registered under the Companies Law or has been dissolved pursuant to that Law;

(e) who is an incorporated limited partnership; or

(f) who is a limited liability partnership,

whether or not the debtor is present in Jersey at the time of application for a declaration or at the time of the declaration.

No *en désastre* declaration of may be made in respect of:

- Separate limited partnerships.
- Limited partnerships.

It is not clear as a matter of Jersey law whether or not the assets of a trustee as trustee of a trust can be declared *en désastre*. We are not aware of any instance in which such a declaration has been made. If, however, the assets of a trustee were declared *en désastre* and in the event that any document was held by the Jersey courts to constitute a transaction at an undervalue and/or the giving of a preference to any person, the Jersey courts would have the power, depending, *inter alia,* on the period of time elapsed since the transaction was entered into, to set aside such transaction.

8.4 Are there any processes other than court proceedings that are available to a creditor to seize the assets of a company in an enforcement?

Security agreements over intangible movable property other than cash created under the Security Interests Law.

The Security Interests Law introduced expanded enforcement powers. The secured party can enforce by way of sale or appropriation of the collateral or proceeds. In addition, the secured party can take any of the following ancillary actions:

- Take control or possession of the collateral or proceeds.
- Exercise any of the rights of the grantor in relation to the collateral or proceeds.
- Instruct any person who has an obligation in relation to the collateral or proceeds to carry out the obligation for the benefit of the secured party (for example, directing the actions of an intermediary who holds a securities account for the grantor).
- Apply any remedy that the security agreement provides for as a remedy that is exercisable pursuant to the power of enforcement, to the extent that it does not conflict with the Security Interests Law. Bespoke enforcement powers can therefore be included as appropriate to the collateral secured.

More than one enforcement option can be taken, and taking one or more of the enforcement options specified above does not preclude the exercise of other rights of the secured party.

The power of enforcement is exercisable once an event of default has occurred and written notice specifying the event of default has been served on the grantor by the secured party.

If enforcement is by way of sale or appropriation, the secured party must give the grantor 14 days prior written notice. Importantly, in contrast to the 1983 Security Interests Law, the grantor can agree in writing (typically in the security agreement) to waive its right to notice of appropriation or sale.

The secured party is obliged on sale or appropriation, to give at least 14 days prior written notice to any person who, 21 days before the sale or appropriation, has a registered security interest in the collateral, or any person other than the grantor who has an interest in the collateral.

There are specific carve-outs from the obligation to give notice, to the extent, for example, that the security property is a quoted investment security.

Self-sale is now expressly permitted.

On appropriation or sale, the secured party must:

- Take all commercially reasonable steps to determine or, in the case of a sale, obtain the fair market value of the collateral, as at the time of the relevant appropriation or sale.
- Act in a commercially reasonable manner in relation to the appropriation or sale.
- Enter (in the case of a sale only) into any agreement for or in relation to the sale on commercially reasonable terms.

The duty of the secured party is owed to the grantor and also to any other person to whom the secured party was required to give notice of appropriation or sale.

If, in exercising its powers of enforcement, a secured party appropriates or sells collateral, it must, within the 14 days after the day on which the collateral is appropriated or sold, give a written statement of account setting out certain information in relation to that appropriation or sale to:

- The grantor (subject to it having waived this requirement).
- Any person with a registered subordinate security interest.
- Any person claiming an interest in the collateral.

If, in exercising its powers of enforcement, a secured party appropriates or sells collateral, it must pay to certain specified persons the amount of any resulting surplus by satisfying the claims of those persons in the prescribed order or alternatively can pay any amount of resulting surplus into the Royal Court of Jersey.

Security agreements under the 1983 Security Interests Law.

For security created under and governed by the 1983 Security Interest Law, a power of sale is the only specified means of enforcement (other than in relation to cash or a negotiable instrument, which can be appropriated). A secured party's ability to enforce its security by a contractual mechanism is untested in the courts, but is often provided for in security agreements.

The power of sale can be exercised after the occurrence of a default event under the security agreement. The secured party must:

- Serve notice of default on the grantor.
- Require the grantor to remedy the default (if the grantor is capable of it).

If the grantor fails to remedy the default within 14 days after notice, the power of sale becomes exercisable.

The secured party must take all reasonable steps to ensure that the sale is made both:

- Within a reasonable time.
- For a price corresponding to the value on the open market at the time of sale of the collateral being sold.

Real estate

A secured creditor can enforce against Jersey real estate through either of the following:

Dégrèvement. A particular immovable has its encumbrances removed so that a creditor can take it free and clear of all charges. It is a bankruptcy for the purposes of Jersey law:

- The process is complicated and is carried out under the 1880 law on immovable property. It can only be commenced by a secured creditor and results in one creditor keeping the property.
- The creditor taking the property must pay off all earlier charges on the property. The creditor is not required to pay or return to the debtor any difference between the value of the property and the level of his claim or charge by which he has taken. If a secured creditor does not take the property when required to in accordance with the date of his charge, he loses his charge and becomes an unsecured creditor.

Désastre. The entire property of the debtor is declared *en désastre*. This is a formal declaration of bankruptcy under Jersey law. It can be commenced by the debtor or by a creditor with a liquidated claim of £3,000 or more. All of the debtor's property vests in the Viscount. The Viscount must get in and distribute all of the debtor's assets for the creditors' benefit. This includes immovables (real property). On realisation of any immovables, creditors with security are paid under their security before any amounts left over go into the bankrupt estate.

There is no equivalent to the English law concept of administration.

In unusual circumstances, the Courts of Jersey can permit an insolvent company (but not one that has been declared *en désastre* to be wound up if it is of the opinion that either it is:

- Just and equitable.
- Expedient in the public interest.

The application to the court on these grounds can be made by the Jersey company (or its directors or shareholders) and certain government and regulatory officials.

9 Jurisdiction and Waiver of Immunity

9.1 Is a party's submission to a foreign jurisdiction legally binding and enforceable under the laws of your jurisdiction?

Please see questions 7.1 and 7.2 above.

9.2 Is a party's waiver of sovereign immunity legally binding and enforceable under the laws of your jurisdiction?

Yes, it is.

10 Licensing

10.1 What are the licensing and other eligibility requirements in your jurisdiction for lenders to a company in your jurisdiction, if any? Are these licensing and eligibility requirements different for a "foreign" lender (i.e. a lender that is not located in your jurisdiction)? In connection with any such requirements, is a distinction made under the laws of your jurisdiction between a lender that is a bank *versus* a lender that is a non-bank? If there are such requirements in your jurisdiction, what are the consequences for a lender that has not satisfied such requirements but has nonetheless made a loan to a company in your jurisdiction? What are the licensing and other eligibility requirements in your jurisdiction for an agent under a syndicated facility for lenders to a company in your jurisdiction?

There are no licensing requirements in Jersey for foreign lenders lending to a Jersey company.

If a lender carries on business in Jersey or is a Jersey company it will be subject to the Proceeds of Crime (Jersey) Law 1999 (the "**Proceeds of Crime Law**"). Under the Proceeds of Crime (Supervisory Bodies) (Jersey) Law 2008, if the lender does not have a registered service provider in Jersey, it may need to apply to be registered with the Jersey Financial Services Commission (the "**JFSC**") to be supervised in relation to its compliance with relevant anti-money laundering and counter-terrorism legislation. Whether or not a lender requires to apply to be registered with the JFSC to be supervised, it will require to comply with relevant anti-money laundering and counter-terrorism legislation.

11 Other Matters

11.1 Are there any other material considerations which should be taken into account by lenders when participating in financings in your jurisdiction?

Jersey is a politically stable and fiscally advantageous financial centre which has has been at the forefront of the global finance industry for over 50 years. The Island enjoys economic stability, political independence, tax neutrality and sophisticated legal, regulatory and technological infrastructure. It has a global reputation founded on a robust legal framework and sound corporate governance practices.

Jersey's evolution as an international finance centre is founded on its close ties to the City of London and its growth as a jurisdiction of choice in the European as well as Middle Eastern, North American and Asian markets.

In 2016, the Financial Action Task Force ("**FATF**") confirmed that Jersey is compliant or largely compliant with 48/49 of the FATF recommendations in respect to anti-money laundering and combating the financing of terrorism. In 2017, Standard & Poor's confirmed Jersey's credit as AA-, one of the highest possible ratings.

The International Stock Exchange offers an efficient listing service and has received a number of international recognitions making it an attractive and increasingly popular option for listing debt securities.

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Robin is consistently recognised for his ability to deal with a wide range of international corporate and finance transactions. He has acted on numerous significant portfolio acquisitions and disposals. He often acts for both lenders and borrowers on complex financings, refinancings and restructurings and has significant experience in relation to the financing of investment funds.

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Laura acts on a wide range of banking, real estate finance, corporate finance and fund finance matters. She specialises in advising international financial institutions and corporate borrowers in relation to real estate finance transactions and funds finance transactions involving Jersey structures.

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CAREY OLSEN

Carey Olsen is a leading offshore law firm. We advise on Bermuda, British Virgin Islands, Cayman Islands, Guernsey and Jersey law across a global network of nine international offices.

We are a full-service law firm working across banking and finance, corporate and M&A, investment funds and private equity, trusts and private wealth, dispute resolution, insolvency and property law.

We work alongside all of the major onshore law firms, accountancy firms and insolvency practitioners on corporate transactions and matters involving our jurisdictions.

Our advice is delivered by an approachable and experienced team of globally-minded lawyers who work in partnership with our clients to help them achieve their objectives. We have the expertise and resources to handle the most complex international transactions combined with a personal approach to business.

Luxembourg

Michel Bulach

Wildgen

Giuseppe Cafiero

1 Overview

1.1 What are the main trends/significant developments in the lending markets in your jurisdiction?

The law of December 23, 2016 on credit agreements for consumers relating to residential immovable property, implementing the 2014/17/EU directive, entered into force in Luxembourg on January 1, 2017, aiming at, *inter alia*, (i) reinforcing consumers' rights through pre-contractual requirements and a reflection period mechanism, consumers' creditworthiness assessments, formalisation of the calculation of the annual percentage rate of charges and early repayment of mortgages, and (ii) creating a new professional actor in the lending market, i.e. a credit intermediary.

1.2 What are some significant lending transactions that have taken place in your jurisdiction in recent years?

In recent years, Luxembourg's market has seen an increase in financing granted by regulated and/or unregulated alternative lending players other than standard banking institutions, offering a wide range of traditional or non-traditional debt instruments. Luxembourg is a marketplace for alternative financing through bonds issuance, including green bonds and foreign currency bonds (renminbi). We also note a growing interest in ICO financing.

2 Guarantees

2.1 Can a company guarantee borrowings of one or more other members of its corporate group (see below for questions relating to fraudulent transfer/financial assistance)?

Yes, subject to certain requirements (see questions 2.2, 2.3 and 4.1).

2.2 Are there enforceability or other concerns (such as director liability) if only a disproportionately small (or no) benefit to the guaranteeing/securing company can be shown?

In such circumstances, (i) the relevant guarantee could be considered as not being in the corporate interest of the company (or of its corporate group) and declared unenforceable or void, and (ii) directors/managers could be subject to civil sanctions for mismanagement and criminal sanctions for misuse of corporate assets.

2.3 Is lack of corporate power an issue?

Yes.

Any act taken by a Luxembourg company shall comply with its corporate purpose.

A Luxembourg limited liability company is bound towards third parties by any acts of its board of directors/managers, even those exceeding its corporate purpose, unless it proves that the third party knew of such acts, or could not, in view of the circumstances, have been unaware of it, without the mere publication of the articles of association constituting such proof. The articles of association may authorise one or more members of the board of directors/managers to represent the company toward third parties, either singly or jointly. A clause to that effect is valid *vis-à-vis* third parties.

A Luxembourg unlimited liability company is only bound towards third parties by acts falling within its corporate purpose. Directors/managers could be personally considered bound by the relevant guarantee if the guarantee exceeds the corporate purpose of the company, unless the shareholders ratify it afterwards.

2.4 Are any governmental or other consents or filings, or other formalities (such as shareholder approval), required?

No governmental or other consents or filings are required in relation to the granting of a guarantee by a Luxembourg company.

The relevant transaction should be approved by the board of directors/managers of a Luxembourg company, as the granting of a guarantee is an act of management.

No shareholder approval is required, unless this is provided for in the articles of association of the company.

2.5 Are net worth, solvency or similar limitations imposed on the amount of a guarantee?

No specific limitations are imposed on the amount of the guarantee.

According to some practitioners, the guarantee should be limited to 90–95% of the net assets of the company to justify a corporate interest and/or avoid a risk of bankruptcy.

2.6 Are there any exchange control or similar obstacles to enforcement of a guarantee?

There are no such obstacles.

3 Collateral Security

3.1 What types of collateral are available to secure lending obligations?

Pledge over financial instruments and claims governed by the Luxembourg law of August 5, 2005 on financial collateral arrangements, as amended (the "Law of 2005"), is the most common collateral security used in the Luxembourg market to secure lending obligations.

The Law of 2005 provides for other types of collateral securities, such as (i) the transfer of title of ownership of financial instruments for security purposes, (ii) repurchase agreements or fiduciary transfer arrangements, and (iii) netting arrangements.

Mortgages and antichresis are collateral securities covering immovable properties.

Securities can be granted over commercial assets by way of a commercial pledge (*gage commercial*) or through a pledge over business as a going concern (*gage sur fonds de commerce*).

3.2 Is it possible to give asset security by means of a general security agreement or is an agreement required in relation to each type of asset? Briefly, what is the procedure?

It is not possible to give asset security by means of a general security agreement under Luxembourg law.

However, the Law of 2005 allows the granting of a pledge over all the receivables and financial instruments presently or in the future owned by the pledgor without the need to specifically designate them. However, a specific perfection would be required for each specific pledged receivables or financial instrument.

Pledge over business as a going concern allows the pledge of a large part (but not all) of the assets of an operational company (see question 3.3).

It is, therefore, common practice to enter into a specific agreement for each type of asset.

3.3 Can collateral security be taken over real property (land), plant, machinery and equipment? Briefly, what is the procedure?

Collateral securities over immovable properties are granted though a mortgage, under notarial deed, registered with the public registrar of mortgages. It is enforceable towards third parties from the moment of such registration. The registration is valid for 10 years and is renewable.

Pledge over business as a going concern of operational companies allows the pledge of a large part of a debtor's assets (goodwill, company's logo, trademark, patents, lease rights, furnishings, machinery, equipment, inventory up to 50% of its value). It can be made through a notarial deed or under private seal and granted only in favour of credit institutions or authorised breweries. It shall be registered with the public registrar of mortgages and becomes enforceable towards third parties from the moment of such registration.

Commercial pledges can be granted under private seal over machinery and equipment that is presently or will in the future be owned by the debtor without the need to specifically designate them. Perfection can be made through physical dispossession (at the premises of the pledgee, at customs, or in a public warehouse) or by way of virtual dispossession through the notification of the pledge to, or confirmation of the pledge by, the debtor or the third party holding the assets. The notification and the acknowledgment of the pledge are made either through a notarial deed or under private seal. In this latter case, if a third party challenges the date of notification or acknowledgment of the pledge, it may be evidenced by any means. Even before the notification or the acknowledgment, the pledge may be enforced against the debtor if it can be evidenced that he was aware of such pledge.

3.4 Can collateral security be taken over receivables? Briefly, what is the procedure? Are debtors required to be notified of the security?

Yes, collateral security can be taken over receivables by way of a pledge under private seal (see question 3.2).

Between the parties, the pledge over the receivables is valid and binding as from the date of the pledge agreement.

In order to be perfected and enforceable against third parties, it must be notified to, or acknowledged by, the debtor. The notification and the acknowledgment of the pledge are made through a notarial deed or under private seal. In this latter case, if a third party challenges the date of notification or acknowledgment of the pledge, it may be evidenced by any means. Even before the notification or the acknowledgment, the pledge may be enforced against the debtor if it can be evidenced that he was aware of such pledge.

3.5 Can collateral security be taken over cash deposited in bank accounts? Briefly, what is the procedure?

Yes, collateral security can be taken over cash deposited in bank accounts by means of a pledge under private seal.

From a Luxembourg law perspective, a cash bank account is considered as a receivable/claim held by a client towards its bank and therefore follows the same rules as those applicable to a pledge over receivables (see question 3.4).

In practice, perfection of the pledge is made through a notification of the pledge sent by the pledgor to the bank, requesting the bank to acknowledge the pledge.

Both notices are negotiated in advance with banks who generally request limitation/exclusion of liabilities provisions in their favour and, inversely, where pledgees request to obtain (i) waivers from the banks in respect of their rights on the bank accounts (i.e. waiver of pledge, right of set-off, lien, right of retention, right of combination of accounts…), and (ii) the consent from the bank to follow pledgees' instructions upon receipt of the enforcement notification of the pledge.

3.6 Can collateral security be taken over shares in companies incorporated in your jurisdiction? Are the shares in certificated form? Can such security validly be granted under a New York or English law governed document? Briefly, what is the procedure?

Collateral security can be taken over shares of Luxembourg companies by way of a pledge under private seal.

Public limited liabilities companies (*sociétés anonymes*) can issue shares under registered form, bearer form or dematerialised form.

Pledges over shares under registered form are perfected through the registration of the pledge in the shareholders' register of the relevant company.

Shares under bearer form shall be deposited with a professional depositary in Luxembourg (credit institutions; certain professionals of the financial sector; lawyers; chartered accountants; independent auditors) who shall maintain a register of bearer shares in Luxembourg. Perfection may be done by entering the pledge in the register of the depositary.

Pledge over shares in dematerialised form are perfected through the registration of the shares as pledged in the relevant securities accounts on which they are held.

Private limited liability companies (*sociétés à responsabilité limitée*) can only issue corporate units which cannot be under bearer form. They must maintain a corporate units register. Perfection is made through the notification and/or acknowledgment of the pledge by the relevant company. For evidence purposes, the pledge is generally recorded in the corporate units register. Where the pledge is granted over a part of the corporate units, the enforcement of the pledge is subject to the prior approval of the shareholders' meeting representing at least ¾ of the corporate capital of the company.

Theoretically, it would be possible to have a pledge over shares of a Luxembourg company governed by a foreign law. However, from an international private law perspective, although the contractual relationship between the parties would be governed by the foreign law (*lex contractus*), the law of location of the assets (*lex rei sitae*), i.e. Luxembourg law, would apply to the content of the *in rem* aspects of the security (in particular the perfection, enforceability, enforcement). This would generate both legal and practical issues and would not be recommended.

3.7 Can security be taken over inventory? Briefly, what is the procedure?

Yes. See question 3.3.

3.8 Can a company grant a security interest in order to secure its obligations (i) as a borrower under a credit facility, and (ii) as a guarantor of the obligations of other borrowers and/or guarantors of obligations under a credit facility (see below for questions relating to the giving of guarantees and financial assistance)?

Yes, as long as (i) the company and the other borrowers and/or guarantors are part of the same corporate group, and (ii) the transaction falls within its corporate object, is in the best corporate interest of the company (or of the corporate group) and does not constitute financial assistance.

3.9 What are the notarisation, registration, stamp duty and other fees (whether related to property value or otherwise) in relation to security over different types of assets?

No notarisation, registration, stamp duty or other fees are required in relation to collateral securities subject to the Law of 2005 on commercial pledges. They can voluntarily be submitted for registration, in which case a fixed registration duty of €12 applies. There is a risk that a 0.24% registration duty may be due in case a collateral agreement mentioning a loan agreement is used in court.

With respect to mortgages, registration duties of 0.24% plus an inscription duty of 0.05% applies on the amount of the secured debt. Notaries' fees are also due.

A pledge over a going concern may be documented by a private or notarial deed. Such pledge shall be registered and the registration will trigger a tax of 0.05% on the total amount of the secured debt at the time of the first registration and at the time of the renewal of this registration every 10 years.

3.10 Do the filing, notification or registration requirements in relation to security over different types of assets involve a significant amount of time or expense?

No, with respect to the timing. See question 3.9 for applicable expenses.

3.11 Are any regulatory or similar consents required with respect to the creation of security?

No, except with respect to securities over shares in regulated entities.

3.12 If the borrowings to be secured are under a revolving credit facility, are there any special priority or other concerns?

There are no special priority or other concerns.

3.13 Are there particular documentary or execution requirements (notarisation, execution under power of attorney, counterparts, deeds)?

No, except for mortgage deeds and pledges over business as a going concern (see question 3.3).

4 Financial Assistance

4.1 Are there prohibitions or restrictions on the ability of a company to guarantee and/or give security to support borrowings incurred to finance or refinance the direct or indirect acquisition of: (a) shares of the company; (b) shares of any company which directly or indirectly owns shares in the company; or (c) shares in a sister subsidiary?

(a) Shares of the company

Luxembourg public and private limited liability companies are prohibited from (i) making loans or advances using company funds, (ii) providing security with a view to the acquisition of shares or corporate units in the company, or (iii) taking a pledge on the company's shares or corporate units, except if the conditions laid down by articles 430-19 and 430-20 of the Luxembourg law of August 10, 1915 on commercial companies, as amended, are met in the case of public limited liability companies.

Breach of such provisions may lead to civil and criminal sanctions for directors/managers.

(b) Shares of any company which directly or indirectly owns shares in the company

No, subject to the corporate interest requirement.

(c) Shares in a sister subsidiary

No, subject to the corporate interest requirement.

5 Syndicated Lending/Agency/Trustee/Transfers

5.1 Will your jurisdiction recognise the role of an agent or trustee and allow the agent or trustee (rather than each lender acting separately) to enforce the loan documentation and collateral security and to apply the proceeds from the collateral to the claims of all the lenders?

The Law of 2005 explicitly provides that collateral may be provided in favour of a person acting for the account of the beneficiaries of the collateral, a fiduciary or a trustee. They are therefore allowed to enforce collateral securities governed by the Law of 2005.

5.2 If an agent or trustee is not recognised in your jurisdiction, is an alternative mechanism available to achieve the effect referred to above which would allow one party to enforce claims on behalf of all the lenders so that individual lenders do not need to enforce their security separately?

This is not applicable in Luxembourg.

5.3 Assume a loan is made to a company organised under the laws of your jurisdiction and guaranteed by a guarantor organised under the laws of your jurisdiction. If such loan is transferred by Lender A to Lender B, are there any special requirements necessary to make the loan and guarantee enforceable by Lender B?

Transfers of loans are generally made through an assignment or novation.

The transfer of a loan through an assignment is enforceable against the debtors and third parties as from the notification to, or acceptance by, the debtor of the assignment. Both the notification and acceptance are made through a notarial deed or under private seal. In this latter case, if a third party challenges the date of notification or acknowledgment of the assignment, it may be evidenced by any means.

In case of assignment of claims, the guarantee attached to the claims is automatically transferred to the new creditor (except first demand guarantees).

The transfer through novation requires the agreement of all the concerned parties (i) to replace the existing contractual relationship between the debtor and Lender A by a new contractual relationship between the same debtor and Lender B, and (ii) to fully discharge the debtor towards Lender A.

Through the novation mechanism, the guarantee will be extinguished and not transferred to Lender B, unless Lender A expressly reserved the guarantee under the relevant guarantee agreement. It is common practice to insert in collateral security arrangements a clause whereby the beneficiary of the guarantee explicitly reserves the guarantee in case of novation.

6 Withholding, Stamp and Other Taxes; Notarial and Other Costs

6.1 Are there any requirements to deduct or withhold tax from (a) interest payable on loans made to domestic or foreign lenders, or (b) the proceeds of a claim under a guarantee or the proceeds of enforcing security?

Luxembourg generally does not levy a withholding tax on arm's-length interest, except for interest on certain profit-sharing bonds or similar instruments and interest paid as a profit share under certain silent partnership type arrangements, subject to the application of the Luxembourg law dated December 23, 2005 introducing final withholding tax on certain interest income, as amended.

There is no withholding tax on proceeds derived from a payment under a guarantee or in case of enforcement of a security.

6.2 What tax incentives or other incentives are provided preferentially to foreign lenders? What taxes apply to foreign lenders with respect to their loans, mortgages or other security documents, either for the purposes of effectiveness or registration?

No specific tax or other incentives are provided to foreign lenders.

See question 3.9 concerning taxes that may apply to loans, mortgages or other security documents.

6.3 Will any income of a foreign lender become taxable in your jurisdiction solely because of a loan to or guarantee and/or grant of security from a company in your jurisdiction?

Income of a foreign lender will not become taxable in Luxembourg in this case.

6.4 Will there be any other significant costs which would be incurred by foreign lenders in the grant of such loan/guarantee/security, such as notarial fees, etc.?

In case a notarial deed is required for any security instrument, the notarial fees will be determined based on the official scale of notaries and be based on the amount at stake (i.e. the value of the assets secured or the amount guaranteed).

6.5 Are there any adverse consequences to a company that is a borrower (such as under thin capitalisation principles) if some or all of the lenders are organised under the laws of a jurisdiction other than your own? Please disregard withholding tax concerns for purposes of this question.

There are no adverse consequences.

7 Judicial Enforcement

7.1 Will the courts in your jurisdiction recognise a governing law in a contract that is the law of another jurisdiction (a "foreign governing law")? Will courts in your jurisdiction enforce a contract that has a foreign governing law?

The Rome Convention on the law applicable to contractual obligations dated June 19, 1980 (the "Rome Convention") with respect to agreements entered into before **December 17, 2009** and Regulation (EC) no 593/2008 of the European Parliament and of the Council of June 17, 2008 with respect to agreements entered into as from **December 17, 2009** (the "Rome Regulation") apply in Luxembourg.

Under Luxembourg law, parties can freely choose the law applicable to their agreement.

Luxembourg courts will recognise a foreign governing law in a contract and enforce it subject to the following restrictions provided for in the Rome Convention and the Rome Regulation:

- Luxembourg overriding mandatory provisions;
- Luxembourg public policy;
- where all the elements relevant to the situation at the time of the choice are located in a country other than the country whose law has been chosen, the Luxembourg court may decide to apply the provisions of the law of that country; and
- depending on the date of the agreement, Luxembourg courts may give effect to the mandatory rules of the law of another country (i) with which the situation has a close connection, or (ii) where the obligations arising out of the contract have to be or have been performed.

7.2 Will the courts in your jurisdiction recognise and enforce a judgment given against a company in New York courts or English courts (a "foreign judgment") without re-examination of the merits of the case?

English court decisions

Decisions issued by English courts will be recognised and enforced in Luxembourg in accordance with (i) Council Regulation (EC) no 44/2001 of December 22, 2000 for decisions issued before **January 10, 2015**, and (ii) Regulation (EU) no 1215/2012 of the European Parliament and of the Council of December 12, 2012 for decisions issued after **January 10, 2015**.

An English court's decision can be recognised in Luxembourg without any special procedure being required.

Under no circumstances may a foreign judgment be reviewed as to its substance.

However, an English court decision may not be recognised in Luxembourg:

- if such recognition is manifestly contrary to Luxembourg public policy;
- where it was given in default of appearance, if the defendant was not served with the document which instituted the proceedings or with an equivalent document in sufficient time and in such a way as to enable him to arrange for his defence, unless the defendant failed to commence proceedings to challenge the judgment when it was possible for him to do so;
- if it is irreconcilable with a judgment given in a dispute between the same parties in Luxembourg; or
- if it is irreconcilable with an earlier judgment given in another Member State or in a third State involving the same cause of action and between the same parties, provided that the earlier judgment fulfils the conditions necessary for its recognition in Luxembourg.

New York court decisions

A final New York court decision would be enforced in Luxembourg subject to the filing of the judgment before a Luxembourg court having jurisdiction of an action for exequatur, provided that:

- such judgment is enforceable where it was rendered;
- the court that rendered the judgment had jurisdiction according to Luxembourg principles of conflicts of jurisdiction and, in particular, that Luxembourg courts did not have exclusive jurisdiction over the case at hand;
- the court that rendered the judgment has complied with its national jurisdiction rules;
- the judgment rendered is not inconsistent with the solution that a Luxembourg court has found in application of the laws determined pursuant to the Luxembourg principles of conflicts of laws;
- the courts that rendered the judgment complied with its national order of procedure and, in particular, with the rights of the defendant; and
- the enforcement of such judgment is not contrary to Luxembourg public policy.

Main Luxembourg case law considers re-examination of the merits of the claim to be excluded.

7.3 Assuming a company is in payment default under a loan agreement or a guarantee agreement and has no legal defence to payment, approximately how long would it take for a foreign lender to (a) assuming the answer to question 7.1 is yes, file a suit against the company in a court in your jurisdiction, obtain a judgment, and enforce the judgment against the assets of the company, and (b) assuming the answer to question 7.2 is yes, enforce a foreign judgment in a court in your jurisdiction against the assets of the company?

(a) In case the commercial procedure is applicable, a decision can be obtained within six months to one year and, for a civil procedure, between one and one-and-a-half years.

(b) English court decisions issued after January 10, 2015 can be directly transmitted to a Luxembourg bailiff to implement enforcement proceedings.

New York court decisions are subject to the standard exequatur proceedings and the requirement to first obtain an exequatur judgment issued by a Luxembourg court, which can be obtained within one year.

7.4 With respect to enforcing collateral security, are there any significant restrictions which may impact the timing and value of enforcement, such as (a) a requirement for a public auction, or (b) regulatory consents?

Except for regulated entities, no regulatory consent is required to enforce a Luxembourg collateral security.

Collateral security governed by the Law of 2005 can be enforced upon the occurrence of a default event and without prior notice, unless otherwise agreed by the parties. The Law of 2005 provides for a wide range of private enforcement means (appropriation; public or private sale; netting) which do not require any prior consent, court intervention, nor a need to proceed with any formalities.

With respect to mortgages, an enforceable decision or title would be required to seize the real estate and then to have it sold through public auction by a public notary. First ranking mortgages can provide for the possibility for the creditor to sell the real estate under private seal (*clause de voie parée*) by a Luxembourg notary as long as it is stipulated in a notarial deed. The seizing procedure would then not be required.

For commercial pledges, enforcement shall be made:

- either through public auction in accordance with the modalities contractually determined by the parties. In the absence of such agreement, the modalities will be determined by the courts; or
- through appropriation, where the creditor shall cause a judgment to be issued ordering that he retain the pledged collateral as payment up to the amount of his claim, in accordance with an expert valuation.

7.5 Do restrictions apply to foreign lenders in the event of (a) filing suit against a company in your jurisdiction, or (b) foreclosure on collateral security?

No particular restrictions apply for foreclosure on collateral security.

Foreign claimants may elect domicile in Luxembourg, which is generally made at the offices of their Luxembourg lawyers (for written procedures where the appointment of a Luxembourg lawyer is mandatory, the election of domicile is automatically made at his address).

A financial guarantee to cover the payment of the costs and damages to which the foreign claimant could be condemned could be ordered by a Luxembourg court.

7.6 Do the bankruptcy, reorganisation or similar laws in your jurisdiction provide for any kind of moratorium on enforcement of lender claims? If so, does the moratorium apply to the enforcement of collateral security?

Yes.

With respect to bankruptcy proceedings (*faillite*), collateral securities cannot be enforced before the closure of the claims verification process.

A moratorium applies to all creditors (including preferred creditors) in case of controlled management proceedings (*gestion contrôlée*).

A moratorium applies to moratorium of payments (*sursis de paiement*) and composition procedures (*concordat préventif de faillite*), but not to preferred creditors.

In any event, such moratoriums do not apply in favour of creditors secured by a collateral security under the Law of 2005.

7.7 Will the courts in your jurisdiction recognise and enforce an arbitral award given against the company without re-examination of the merits?

Foreign arbitral awards are enforceable in Luxembourg in accordance with the requirements set forth in article 1250 of the *Nouveau Code de Procédure Civile* ("NCPC") by an enforcement order of the chairman of the district court (*président du tribunal d'arrondissement*) in whose jurisdiction the party against whom the enforcement is sought has his domicile or, in the absence of domicile, his residence.

Pursuant to article 1251 of the NCPC or, where appropriate, relevant provisions of the New York Arbitration Convention and/or the European Arbitration Convention, a Luxembourg court may deny enforceability of an arbitral award if:

- the parties did not have the capacity to conclude the arbitration agreement;
- the arbitration agreement is not valid pursuant to its governing law;
- the rights of the defence have been infringed;
- the arbitral award can still be appealed before the arbitrators and, if the arbitrators did not make the arbitral award enforceable, notwithstanding an appeal;
- the arbitral award or its enforcement is contrary to Luxembourg public policy or if the dispute was not arbitrable; and
- there is cause for having the arbitral award set aside pursuant to article 1244 (3) to (12) of the NCPC or, where appropriate, article V of the New York Arbitration Convention or relevant provisions of the European Arbitration Convention is established.

Assuming that the above-mentioned conditions are met, Luxembourg courts will recognise and enforce an arbitral award given against a company without re-examination of the merits.

8 Bankruptcy Proceedings

8.1 How does a bankruptcy proceeding in respect of a company affect the ability of a lender to enforce its rights as a secured party over the collateral security?

See question 7.6.

8.2 Are there any preference periods, clawback rights or other preferential creditors' rights (e.g., tax debts, employees' claims) with respect to the security?

Under Luxembourg law, certain acts (i.e. deeds of transfer, commutative contracts or onerous contracts, payments related to non-matured debts) are null and of no effect towards the mass of creditors when they have been made during the so-called "suspect period" (i.e. maximum six months) or within 10 days before such period,

In any event, all acts and payments made in fraud of creditors are null, whatever the date on which they occurred, even before the suspect period.

Any other payments made by the bankrupt for matured debts and any other onerous acts taken during the suspect period can be cancelled if the contracting party of the bankrupt was aware that the latter was unable to pay its debts (*en cessation de paiement*).

Such restrictions do not apply to collateral securities governed by the 2005 Law.

Luxembourg law provides for preferential creditors' rights (court costs, salaries, social securities, tax, etc.). Luxembourg collateral securities are considered as out of the scope of insolvency proceedings and are not subject to such preferential creditors' rights.

8.3 Are there any entities that are excluded from bankruptcy proceedings and, if so, what is the applicable legislation?

Regulated entities are generally subject to particular insolvency proceedings rules; in particular:

- Luxembourg credit institutions and certain professionals of the financial sectors which are subject to specific prudential

rules and obligations in relation to recovery planning, intra-group financial support and early intervention laid down by the law of April 5, 1993 on the financial sector, as amended (the "Law of 1993"); and
- Luxembourg insurance/reinsurance companies which are subject to specific provisions on reorganisation measures and winding-up procedures laid down by the law of Law of December 7, 2015 on the insurance sector, as amended.

8.4 Are there any processes other than court proceedings that are available to a creditor to seize the assets of a company in an enforcement?

Yes. See question 7.4.

9 Jurisdiction and Waiver of Immunity

9.1 Is a party's submission to a foreign jurisdiction legally binding and enforceable under the laws of your jurisdiction?

Under Luxembourg law, parties may freely choose to submit their dispute to a foreign jurisdiction, subject to the following conditions:
- the dispute is based on cross-border elements; and
- Luxembourg courts (or another foreign court) do not have exclusive jurisdiction for the concerned matter (i.e. real estate, consumers, insurance, employment).

9.2 Is a party's waiver of sovereign immunity legally binding and enforceable under the laws of your jurisdiction?

As long as such waiver of immunity is certain and irrevocable, it should be legally binding and enforceable in Luxembourg.

10 Licensing

10.1 What are the licensing and other eligibility requirements in your jurisdiction for lenders to a company in your jurisdiction, if any? Are these licensing and eligibility requirements different for a "foreign" lender (i.e. a lender that is not located in your jurisdiction)? In connection with any such requirements, is a distinction made under the laws of your jurisdiction between a lender that is a bank *versus* a lender that is a non-bank? If there are such requirements in your jurisdiction, what are the consequences for a lender that has not satisfied such requirements but has nonetheless made a loan to a company in your jurisdiction? What are the licensing and other eligibility requirements in your jurisdiction for an agent under a syndicated facility for lenders to a company in your jurisdiction?

Activity regarding the granting of loans to the public is a regulated activity in Luxembourg reserved for Luxembourg credit institutions and certain Luxembourg professionals of the financial sector in accordance with the Law of 1993.

Credit institutions established within the EU/EEA Member States and duly authorised in their home jurisdiction to perform lending activities may provide cross-border lending activity in Luxembourg, subject to the conditions provided for in the Law of 1993.

Credit institutions established outside of the EU/EEA Member States which are occasionally and temporarily active in Luxembourg are subject to licence requirements, in particular to an accreditation of the Luxembourg Minister of Finance, under the condition that the concerned credit institution is subject to similar rules of accreditation and monitoring in its country of origin as those in force in Luxembourg.

11 Other Matters

11.1 Are there any other material considerations which should be taken into account by lenders when participating in financings in your jurisdiction?

Under Luxembourg law, interest may not accrue on interest that is due on principal, unless such interest has been due for at least one year.

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Mentioned as Wildgen's primary contact for banking and finance matters by independent specialised directories, Michel is an experienced lawyer and a much-valued expert for his clients who appreciate his "diligent efficiency" and his "excellent communication".

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Over the years, he has developed a sound expertise in securitisation matters and structured finance transactions, focusing mainly on RMBS/CMBS transactions and more generally on non-performing receivables.

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LUXEMBOURG LAW FIRM

Since 1923, Wildgen has been at the heart of law practice in Luxembourg. Today, it is one of the best known and most well-respected independent business law firms in Luxembourg, possessing a strong track record and continuing to offer sound technical expertise. For decades, we have served our clients as a full-service financial, corporate, investment fund, tax, and business law firm. The Banking and Finance team has proved to be a highly reliable partner for local and foreign credit institutions and financial players, for lenders and borrowers. The team is particularly active in the areas of corporate structuring, bank lending and structured finance transactions for SMEs, international groups, financial firms, and high-net-worth individuals. Wildgen is frequently involved in advisory work for refinancing projects, as well as the setting-up and development of securitisation structures and operations in capital markets.

Mexico

Gonzalez Calvillo, S.C.

José Ignacio Rivero Andere

1 Overview

1.1 What are the main trends/significant developments in the lending markets in your jurisdiction?

Mexico and the U.S. are not only neighbours, but strategic partners, whose cultures, nationals and economies are extremely interlinked and interdependent. Among others: (a) Mexico is the second country worldwide in terms of exports to the U.S.; (b) low inflation in the U.S. is dependent on the low costs of the manufacturing industry in Mexico; and (c) 36.3 million out of the 323.1 million U.S. population are identified as having full or partial Mexican ancestry.

2017 was the first year of the Trump administration, which has adopted policies that deeply affect Mexico. Amid these policies are:

- the U.S. tax reform, which will require Mexico to revisit its own tax framework to make it competitive and attractive for U.S. companies doing business in the country;
- the current renegotiation of NAFTA, the result of which may deeply influence both the Mexican and the U.S. economies; and
- in immigration, the building of a wall between the Mexican and U.S. borders, and the termination of DACA.

Furthermore, in 2018, Mexico will have presidential elections, and thus far the left-wing candidate is expected to win, a circumstance which will generate anxiety in the Mexican economy as his policies seem to be antagonistic to the *status quo*.

Despite the foregoing, the structural reforms carried out in the current administration of Enrique Peña Nieto continue to materialise, particularly in the Telecommunications, Infrastructure, Energy, and Gas sectors, which have witnessed significant foreign and domestic investments and thus, notwithstanding the nervousness being generated by the U.S.-Mexico relations and the forthcoming elections, we expect to continue seeing a great deal of economic activity during 2018.

1.2 What are some significant lending transactions that have taken place in your jurisdiction in recent years?

Over the last six years, since the beginning of the current administration, Mexico has witnessed the enactment of several structural reforms that are transforming the country and are generating significant investments and a relatively good amount of economic activity in the context of the world's economy.

In line with the foregoing, Mexico has seen and will continue to see important financial transactions in the Telecommunications, Infrastructure, Energy, and Gas sectors, such as: (a) the USD$2 billion financing of the Red Compartida (the Mexican public telecommunications network), which is one of the largest infrastructure and telecommunications projects in Mexico in recent years, and in which I acted as counsel to the lenders; (b) the financing of the new airport of Mexico City, which is expected to be one of the largest and most sophisticated airports in the world; and (c) several multimillion dollar lending transactions in the Energy and Gas sectors.

2 Guarantees

2.1 Can a company guarantee borrowings of one or more other members of its corporate group (see below for questions relating to fraudulent transfer/financial assistance)?

Yes. Guarantees can be created either under Mexican or foreign law, provided that, when created under foreign law, certain provisions shall be included in the foreign documents to ensure enforceability of a judgment thereof in Mexico against the Mexican guarantor.

2.2 Are there enforceability or other concerns (such as director liability) if only a disproportionately small (or no) benefit to the guaranteeing/securing company can be shown?

Regarding director's liability, there is none from a legal perspective so long as, to the extent applicable, in approving the transaction the directors comply with their statutory duties, which generally are: (a) in private companies, refrain from voting in matters with respect to which they have a conflict; and (b) in public entities, duties of loyalty and care.

In connection with enforcement, there are no concerns except that enforceability can be limited by bankruptcy *(concurso mercantil)*, insolvency, liquidation, reorganisation, moratorium, labour, tax and other laws of general application relating to, or affecting the, obligations of debtors and the rights of creditors.

2.3 Is lack of corporate power an issue?

Yes. For a guarantee to be valid (a) the purpose of the company as per its bylaws must include authority for the company to guarantee third-party obligations, (b) as applicable, corporate approvals have to be implemented, and (c) the relevant documents have to be entered into by a duly appointed representative of the Mexican guarantor.

2.4 Are any governmental or other consents or filings, or other formalities (such as shareholder approval), required?

Corporate approvals may be required depending on the bylaws of the company.

Third party consents may be required depending on the contractual obligations assumed by the company.

Generally, no governmental consents/approvals/filings would be required, except for some regulated entities.

2.5 Are net worth, solvency or similar limitations imposed on the amount of a guarantee?

No; however, it is important to note that the enforceability of a guarantee can be limited as provided in question 2.2 above.

2.6 Are there any exchange control or similar obstacles to enforcement of a guarantee?

No exchange control.

Regarding enforcement of foreign guarantees, please refer to the answers above and note that provisions of article 1347-A of the Mexican Commerce Code, will need to be fulfilled for a foreign judgment to be enforced in Mexico.

3 Collateral Security

3.1 What types of collateral are available to secure lending obligations?

Generally, and except for certain type of public assets, collateral can be created over any type of assets, through security trusts, pledges, and mortgages.

3.2 Is it possible to give asset security by means of a general security agreement or is an agreement required in relation to each type of asset? Briefly, what is the procedure?

1. Pledge over Equity Interests: To perfect collateral in Mexico over equity interests issued by a Mexican company, a Mexican stock/partnership interests pledge agreement needs to be implemented, jointly with the delivery to the pledgee of (i) if applicable, stock certificates duly endorsed in guarantee, (ii) evidence of registration of the pledge in the shareholders'/partners' registry book of the issuer, and (iii) stock powers to be exercised upon the occurrence/continuance of an enforcement event.

2. Pledge over Movable Assets: To perfect collateral in Mexico over any type of assets (other than equity interests and real estate), a Mexican floating lien/regular asset pledge agreement needs to be implemented. When structured as a floating lien pledge, the possession of the pledged assets will remain with the pledgor; when structured as a regular pledge, the possession of the pledged assets will be transferred to the pledgee.

In connection with items 1 and 2 above, it is important to note that the signatures of the parties to the equity interests pledge (to ensure priority over tax credits) and the floating lien/regular asset pledge (to comply with perfection requirements under Mexican law), must be ratified before a Mexican notary public, and the agreement shall be registered at the *Registro Único de Garantías Mobiliarias*. To accomplish the notarial ratification, representatives of such parties must be present at closing to execute the agreement and the ratification deed in front of a Mexican notary public with a valid Mexican law power of attorney. Also, in case the floating lien/regular asset pledge covers any trademarks or other intellectual property registered in Mexico, such pledge shall also be registered at the Mexican Institute of Industrial Property (IMPI). Additional formalities and third-party consents may apply depending on the nature of the grantor and the collateral assets.

3. Security Trust: As an alternative to the pledge structures referred in items 1 and 2 above, and to the mortgage structure referred in question 3.3 below, a Mexican security trust structure can be implemented and used to create, among others, a general security structure encompassing all or a substantial number of the assets of a grantor or a relevant project.

In general, under a trust, the sponsors/security providers will transfer ownership/title of assets to a trustee (a Mexican bank or a financial entity authorised to act as such), with the purpose of (i) securing the payment and the performance of obligations under the relevant financing documents, (ii) managing the collateral assets, and/or (iii) serving as a source of payment of the relevant debt.

The formalities for incorporating, operating and transferring assets to a trust will depend on the nature of the sponsors/security providers and the assets involved. These formalities include the ratification of the signatures of the parties involved and of the trust agreement before a Mexican notary public, and the registration of the trust agreement at the *Registro Único de Garantías Mobiliarias*.

The primary advantages of the trust structure are that it makes the collateral assets remote to the bankruptcy of the sponsors/security providers as there is a "true sale" of the assets to the trustee, and that it gives additional control and enforcement capabilities over the assets in an enforcement event. The primary disadvantages of the trust structure are that it may interfere with the operations of the sponsors/security providers and affect third parties related to their business (as the assets are transferred to a third-party trustee), and that its implementation represents additional costs.

3.3 Can collateral security be taken over real property (land), plant, machinery and equipment? Briefly, what is the procedure?

Collateral over Real Estate (land and buildings): To perfect collateral in Mexico over Mexican land and/or buildings, a Mexican mortgage shall be implemented.

- In terms of Mexican law, a mortgage must be granted through a notarial deed and thus representatives of the grantor shall be present at closing in Mexico to execute the same before a notary public with a valid Mexican law power of attorney.
- In addition, and in terms of Mexican law, for a mortgage to produce effects *vis-à-vis* third parties, it shall be registered at the *Registro Público de la Propiedad* of the place where the mortgaged assets are located.
- In connection with the creation of security over machinery and equipment, please refer to question 3.2, item 2.

3.4 Can collateral security be taken over receivables? Briefly, what is the procedure? Are debtors required to be notified of the security?

Please refer to question 3.2, item 2.

Additionally, regarding debtors' notification, debtors are not required to be notified for the collateral to be perfected; however, it is convenient to carry out notifications so that debtors acknowledge the existence of the collateral and the fact that once and if enforced, they must pay the creditors resulting from the enforcement.

3.5 Can collateral security be taken over cash deposited in bank accounts? Briefly, what is the procedure?

Please refer to question 3.2, item 2.

3.6 Can collateral security be taken over shares in companies incorporated in your jurisdiction? Are the shares in certificated form? Can such security validly be granted under a New York or English law governed document? Briefly, what is the procedure?

Please refer to question 3.2, item 1.

Regarding certificate formalities, they depend on the corporate form of the issuer but generally shares are in certificated form.

Regarding the possibility of creating collateral over these assets through foreign documents, this is not possible.

3.7 Can security be taken over inventory? Briefly, what is the procedure?

Please refer to question 3.2, item 2.

3.8 Can a company grant a security interest in order to secure its obligations (i) as a borrower under a credit facility, and (ii) as a guarantor of the obligations of other borrowers and/or guarantors of obligations under a credit facility (see below for questions relating to the giving of guarantees and financial assistance)?

Yes. Any collateral over assets located in Mexico must be governed by Mexican law.

3.9 What are the notarisation, registration, stamp duty and other fees (whether related to property value or otherwise) in relation to security over different types of assets?

In most cases where security is granted, the participation of a notary public is required. Notarial fees are variable and will depend on the type of document and/or security interest being created; these fees are topped out in most cases but can be high (although, in large transactions or when topped fees are high, notaries can and will typically grant fee discounts).

Registration fees for security over real estate are associated with security registration at public registries. All security over real estate must be registered at the local public registry of property for the security to be perfected and opposable to third parties, and fees will also greatly vary from state to state. In most cases, registration fees are also topped out by local authorities, but in some cases special discounts may apply when the security is associated with benefits for the locality or state (i.e., infrastructure, investment, etc.).

While registration of security over assets other than from real estate, such as receivables, cash deposited in bank accounts, inventory and similar assets will typically be required (depending on the type of security being created), documents evidencing security over these movable assets are, as of recently, electronically registered at the *Registro Único de Garantías Mobiliarias*, and there are no material fees payable for such registration.

Please note that, in addition to the above, in some other cases and in certain local jurisdictions, additional taxes or fees may apply on perfection and/or registration of security.

3.10 Do the filing, notification or registration requirements in relation to security over different types of assets involve a significant amount of time or expense?

The time and/or expenses associated with creating, perfecting and registering security in Mexico vary on a case-by-case basis. The number of secured assets, type and extent of security, nature of the assets in security (i.e. real estate, receivables, etc.) all play a role in determining the amount of time and expense.

Registration of real estate-backed security can take anywhere from a few days to a couple of months, depending on the locality where it needs to take place. Registration of security over movable assets can be done in a matter of days and at marginal cost. As for costs associated with creation, notarisation and perfection, please refer to the foregoing answers.

3.11 Are any regulatory or similar consents required with respect to the creation of security?

There can be, if the project involves regulated entities/assets. Security over permits, concessions, procurement contracts, licences and other regulated assets (such as pipelines, water treatment plants, energy plants, mining properties), or over companies or entities that use, procure, manage and/or operate such assets, will typically require prior governmental approval to create security over them (or, at best, prior notice to the relevant authorities).

3.12 If the borrowings to be secured are under a revolving credit facility, are there any special priority or other concerns?

No, there are not.

3.13 Are there particular documentary or execution requirements (notarisation, execution under power of attorney, counterparts, deeds)?

Please refer to questions 3.2, 3.9 and 3.10.

4 Financial Assistance

4.1 Are there prohibitions or restrictions on the ability of a company to guarantee and/or give security to support borrowings incurred to finance or refinance the direct or indirect acquisition of: (a) shares of the company; (b) shares of any company which directly or indirectly owns shares in the company; or (c) shares in a sister subsidiary?

No, not generally.

5 Syndicated Lending/Agency/Trustee/Transfers

5.1 Will your jurisdiction recognise the role of an agent or trustee and allow the agent or trustee (rather than each lender acting separately) to enforce the loan documentation and collateral security and to apply the proceeds from the collateral to the claims of all the lenders?

Yes. Mexico would recognise the role of security agents. In some cases, the granting of a Power of Attorney to the agent by the secured parties to act as such may be advisable.

5.2 If an agent or trustee is not recognised in your jurisdiction, is an alternative mechanism available to achieve the effect referred to above which would allow one party to enforce claims on behalf of all the lenders so that individual lenders do not need to enforce their security separately?

This is not applicable in Mexico.

5.3 Assume a loan is made to a company organised under the laws of your jurisdiction and guaranteed by a guarantor organised under the laws of your jurisdiction. If such loan is transferred by Lender A to Lender B, are there any special requirements necessary to make the loan and guarantee enforceable by Lender B?

Specific contractual requirements may apply. Also, unless the Mexican borrower entity is notified of the assignment, it will be released of its obligations by paying to Lender A.

6 Withholding, Stamp and Other Taxes; Notarial and Other Costs

6.1 Are there any requirements to deduct or withhold tax from (a) interest payable on loans made to domestic or foreign lenders, or (b) the proceeds of a claim under a guarantee or the proceeds of enforcing security?

Yes. Withholding taxes generally apply to interest payable to foreign lenders, as well as to the proceeds of a claim or an enforcement of security that are destined for payment of interests, commissions or fees (and not principal). The withholding rate will depend on the underlying transaction, the characteristics and nature of the relevant lender, the applicability of international taxation treaties and other related factors.

Please note that withholding requirements do not apply to Mexican banks and financial entities, which will calculate and pay their taxes in accordance with applicable Mexican tax laws.

6.2 What tax incentives or other incentives are provided preferentially to foreign lenders? What taxes apply to foreign lenders with respect to their loans, mortgages or other security documents, either for the purposes of effectiveness or registration?

Mexico has entered into many treaties to avoid double taxation with different countries, and each treaty or agreement provides for distinct types of privileges, restrictions, fees, and, in some cases, exemptions thereof.

6.3 Will any income of a foreign lender become taxable in your jurisdiction solely because of a loan to or guarantee and/or grant of security from a company in your jurisdiction?

Foreign lenders are required to pay income tax if they have a permanent establishment within Mexican territory, or when the income comes from sources within the Mexican territory.

6.4 Will there be any other significant costs which would be incurred by foreign lenders in the grant of such loan/guarantee/security, such as notarial fees, etc.?

Please refer to section 3.

6.5 Are there any adverse consequences to a company that is a borrower (such as under thin capitalisation principles) if some or all of the lenders are organised under the laws of a jurisdiction other than your own? Please disregard withholding tax concerns for purposes of this question.

No, there are not.

7 Judicial Enforcement

7.1 Will the courts in your jurisdiction recognise a governing law in a contract that is the law of another jurisdiction (a "foreign governing law")? Will courts in your jurisdiction enforce a contract that has a foreign governing law?

Yes. Mexican law allows the parties to choose the governing law and submission to jurisdiction; also, Mexican courts will recognise a judgment under a foreign law governed agreement, so long as such foreign laws do not contravene Mexican law principles.

7.2 Will the courts in your jurisdiction recognise and enforce a judgment given against a company in New York courts or English courts (a "foreign judgment") without re-examination of the merits of the case?

Please refer to question 7.1.

7.3 Assuming a company is in payment default under a loan agreement or a guarantee agreement and has no legal defence to payment, approximately how long would it take for a foreign lender to (a) assuming the answer to question 7.1 is yes, file a suit against the company in a court in your jurisdiction, obtain a judgment, and enforce the judgment against the assets of the company, and (b) assuming the answer to question 7.2 is yes, enforce a foreign judgment in a court in your jurisdiction against the assets of the company?

Timing depends on the circumstances of the particular cases, applicable foreign governing laws, and applicable foreign jurisdictions, as well as on the consistency with Mexican law principles.

7.4 With respect to enforcing collateral security, are there any significant restrictions which may impact the timing and value of enforcement, such as (a) a requirement for a public auction, or (b) regulatory consents?

Yes. Foreclosure of a mortgage or a regular pledge will typically require a summary judicial procedure that would ultimately result in public auctions to sell (or transfer) the collateral as payment to the lenders. For non-possessory pledges and security trusts, it is possible to choose between a judicial and a non-judicial procedure.

As for regulatory consents, typically the same consents required, if applicable, for the creation of security will apply to its foreclosure (especially if the receiver or buyer of the assets is not the same entity as that which requested the original consent), but in many cases, the original consent would cover the ability to foreclose on the assets, subject in some cases to prior notice to the relevant authorities. Also, enforcement can be significantly affected or impacted in case of reorganisations or bankruptcy under applicable law.

7.5 Do restrictions apply to foreign lenders in the event of (a) filing suit against a company in your jurisdiction, or (b) foreclosure on collateral security?

Generally, no; however, restrictions applicable to foreign investors or creditors to own or operate certain assets (restrictions on foreign investment) will apply to foreign investors or creditors in the event of a foreclosure.

7.6 Do the bankruptcy, reorganisation or similar laws in your jurisdiction provide for any kind of moratorium on enforcement of lender claims? If so, does the moratorium apply to the enforcement of collateral security?

Yes. From the date of the bankruptcy judgment to the end of the reorganisation stage, no claim or foreclosure will be enforceable against the company pursuant to the Federal Bankruptcy Law.

7.7 Will the courts in your jurisdiction recognise and enforce an arbitral award given against the company without re-examination of the merits?

Yes. Mexican courts have a legal obligation to recognise contractual submission of disputes to international arbitration, as well as international arbitral awards, subject to compliance with procedural and formal requirements under the Mexican Commerce Code and applicable international treaties. Please note that enforcement of an arbitral award may be denied, among other applicable matters if: (i) one of the parties to the arbitration agreement did not have adequate or sufficient legal capacity to enter into such arrangement or such arrangement is not valid under the laws chosen by the parties; (ii) service of process is not correctly and legally completed; (iii) the award refers to a controversy which, under the terms of the arbitration agreement, was not subject to arbitration or contains a decision that exceeds the terms of such arbitration agreement; (iv) the subject matter of the arbitration procedure cannot be arbitrated or the enforcement of the award is contrary to Mexican law, public policy of Mexico, international treaties or agreements binding upon Mexico; or (v) the award is not final in the jurisdiction where it was obtained.

8 Bankruptcy Proceedings

8.1 How does a bankruptcy proceeding in respect of a company affect the ability of a lender to enforce its rights as a secured party over the collateral security?

Mexico's Federal Bankruptcy Law is the general statute governing reorganisation and bankruptcy proceedings throughout Mexico. Reorganisation and/or bankruptcy proceedings will directly affect enforcement of a security for a lender, but the impact will greatly vary depending on the legal robustness of the security received by such lender.

In general terms, and subject to exemptions and rights, the Federal Bankruptcy Law treats a lender secured under a security structure created under a pledge or a mortgage as a secured creditor. Important benefits afforded to a secured creditor are priority ranking, continued ordinary interest accrual, loan currency protection and (subject to some exemptions) ability to participate or not in the eventual creditor agreement that concludes the reorganisation proceeding; in the event no agreement is reached and the relevant company becomes bankrupt, secured creditors have the right to foreclose on their security, and they have the same right if such an agreement is validly reached but not signed by the relevant creditor.

Because, as explained above, under a trust title, the assets that form the trust estate are transferred to the relevant trustee and therefore subtracted from the patrimony of the relevant company; lenders secured by or through a trust have, through this agreement, a bankruptcy remote vehicle under applicable law. Please note, however, that in recent cases, while this remoteness has been generally accepted by Mexican courts, precautionary measures issued by Mexican courts have temporarily frozen enforcement and foreclosure of assets under trusts on the basis, among others, of the need for the company subject to the reorganisation procedure to use such assets for its survival.

8.2 Are there any preference periods, clawback rights or other preferential creditors' rights (e.g., tax debts, employees' claims) with respect to the security?

Yes. The Federal Bankruptcy Law and its associated regulations establish clawback rights (general 270 clawback period for fraudulent conveyance) and also sets forth a list which, subject to exemptions and interpretation, sets forth the following ranking priorities for creditors: (i) singularly privileged creditors (i.e. burial and sickness expenses); (ii) secured creditors (those secured with an *in rem* guarantee, such as the pledges and mortgage agreements); (iii) specially privileged creditors; and (iv) common (typically unsecured) creditors. However, please note that credits against the asset mass, such as certain tax or labour credits, debts incurred while at the reorganisation process, asset maintenance and other similar costs, may have higher ranking than secured credits and will typically be paid first.

8.3 Are there any entities that are excluded from bankruptcy proceedings and, if so, what is the applicable legislation?

Yes. Governmental entities (i.e., states, municipalities, and certain government entities) are not subject to the Federal Bankruptcy Law. However, they can (and have) implemented trust structures to guarantee debt instrument offerings and other forms of financing, even governmental procurement, and ascertain that assets transferred to such trust are considered to be isolated from the reach of said governmental entity and could be subject to the Federal Bankruptcy Law.

8.4 Are there any processes other than court proceedings that are available to a creditor to seize the assets of a company in an enforcement?

Yes; however, please note that Mexican law does not allow the actual seizing or taking possession of assets through out-of-court proceedings; therefore, any actual seizure or taking possession of project assets prior to the conclusion of an out-of-court proceeding of foreclosure must be undertaken and approved by the applicable courts.

9 Jurisdiction and Waiver of Immunity

9.1 Is a party's submission to a foreign jurisdiction legally binding and enforceable under the laws of your jurisdiction?

Please refer to question 7.1.

9.2 Is a party's waiver of sovereign immunity legally binding and enforceable under the laws of your jurisdiction?

Sovereign immunity is not recognised in Mexico; thus, a waiver of immunity is generally valid in Mexico.

10 Licensing

10.1 What are the licensing and other eligibility requirements in your jurisdiction for lenders to a company in your jurisdiction, if any? Are these licensing and eligibility requirements different for a "foreign" lender (i.e. a lender that is not located in your jurisdiction)? In connection with any such requirements, is a distinction made under the laws of your jurisdiction between a lender that is a bank *versus* a lender that is a non-bank? If there are such requirements in your jurisdiction, what are the consequences for a lender that has not satisfied such requirements but has nonetheless made a loan to a company in your jurisdiction? What are the licensing and other eligibility requirements in your jurisdiction for an agent under a syndicated facility for lenders to a company in your jurisdiction?

In general, there are no licencing or other eligibility requirements applicable under Mexican laws.

11 Other Matters

11.1 Are there any other material considerations which should be taken into account by lenders when participating in financings in your jurisdiction?

No, there are not.

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José Ignacio Rivero is a business-oriented lawyer with over 15 years of experience providing legal and business advice to clients in banking and finance, capital markets, corporate law, mergers and acquisitions, real estate, and private equity. He has developed a practice focus in structured finance, finance strategy, refinancing, secured loans, among others.

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He worked as foreign associate at the firm Proskauer Rose LLP in New York and obtained a Master of Laws degree (LL.M.), from Northwestern University and the certificate in business administration, from the Kellogg School of Management.

Founded in 1987, we have rewritten the full-service firm model by blending it with our transactional and deal-making core. Throughout the past 30 years, we have grown steadily while very selectively. We have a broad, solid and energetic partnership base of 20 and close to 80 dedicated lawyers comprising the legal team.

The firm is known for its ability to build cross-disciplinary teams in the most challenging and sophisticated transactions and has extensive experience providing legal, business and regulatory advice to multinational and domestic companies in a broad range of areas of practice.

Our business and legal practice is well diversified, by representing a blend of local and multinational clients across regulated and non-regulated industries, such as domestic and international financial institutions, governmental entities, companies, businesses and individuals, including a substantial number of Fortune 500 companies in a wide variety of practice areas.

Mozambique

Nuno Morgado Pereira

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1 Overview

1.1 What are the main trends/significant developments in the lending markets in your jurisdiction?

Mozambique is currently experiencing two main trends in opposite directions.

The first main trend is the general slowing down of lending activity in the country, which is the result of the decrease in growth rates in the last two years. The principle cause of this decrease is the suspension of international support for the Government's state budget (due to the "USD 2 bn hidden debt case") which in turn is seriously affecting liquidity in the day-to-day economy and lack of foreign reserves at Mozambique's central bank, the Bank of Mozambique. To contain inflation and the decrease in foreign exchange reserves, the Bank of Mozambique has not only increased benchmark interest rates, but also the levels of foreign exchange reserves that commercial banks are required to hold with the central bank. This means that the local banks are experiencing great liquidity levels, but are not lending as much as they could, due to the decrease in economic growth and increase in credit risk inherent to the current economic environment. Therefore, as far as the Mozambican banking sector is concerned, lending activity is low and restricted to those sectors of the economy which are still experiencing good activity levels, namely to export-oriented manufacturers and imports of essential goods.

The second main trend in the Mozambican economy relates to large-scale natural resources projects in the north of the country, namely the gas projects led by ENI and Anadarko and the coal project of the Brazilian mining company Vale do Rio Doce, now in joint venture with Japanese conglomerate Mitsui. The fact that these projects have finally kicked-off has given a confidence boost to economic agents, but this is still not sufficient to balance the economic slowdown explained above. The gas and mining projects are seen as a stand-alone phenomenon, detached from the country's real economy (at least for the time being) but are still having a positive effect given the massive amounts of capital required to finance the projects and all other activities connected to them.

1.2 What are some significant lending transactions that have taken place in your jurisdiction in recent years?

The gas and coal projects in the north off the country are capital intensive and require large-scale financing from the world's leading financial institutions.

Early in 2018, the Floating Liquified Natural Gas project in Palma, Cabo Delgado province, in a consortium led by ENI, came to financial close with a USD 8 bn syndicated facility led by Standard Bank and ICBC.

Another very significant transaction is the multi-billion-dollar financing of the USD 4 bn Nacala Corridor Rail and Port project in Mozambique and Malawi. This is the largest ever successful project financing of infrastructure development in Sub-Saharan Africa. The Project comprises the construction, refurbishment, and operation of a 912 km railway line through Mozambique and Malawi, as well as the construction and operation of a coal terminal at the port of Nacala-a-Velha, Mozambique. The railway will link Vale Mozambique's Moatize coal project in Tete Province, Mozambique, with the port.

2 Guarantees

2.1 Can a company guarantee borrowings of one or more other members of its corporate group (see below for questions relating to fraudulent transfer/financial assistance)?

As a general rule, corporate powers are restricted to those rights and obligations that are necessary or appropriate to pursuing the purpose of the company (which is, generally, to make a profit).

Under Article 88(3) of the Mozambican Commercial Code, there is a legal presumption that granting guarantees in respect of obligations of other entities is contrary to the purpose of a company, unless there is a justifiable self-interest of the company in providing the guarantee or the company in question is in a group relationship with the other.

Such a justifiable self-interest of the company is evident in the provision of downstream guarantees, but is less evident in the provision of upstream and cross-stream guarantees. In the case of upstream and cross-stream guarantees it is advisable for the necessary resolutions to be passed justifying the self-interest of the company, which may be an indirect one, in providing the guarantee.

2.2 Are there enforceability or other concerns (such as director liability) if only a disproportionately small (or no) benefit to the guaranteeing/securing company can be shown?

In such situations, it is likely that there is no justifiable self-interest of the company in providing the guarantee/security and, unless the company is in a group or control relationship with the entity whose obligations it guarantees/secures, the provision of the guarantee/security may be considered null and void.

The provision of the guarantee or security with disproportionately small (or no) benefit to the company may give rise to a breach of duties of directors towards the company and, therefore, to liability.

2.3 Is lack of corporate power an issue?

Yes, please see question 2.1 above.

2.4 Are any governmental or other consents or filings, or other formalities (such as shareholder approval), required?

Except for certain state-owned and other public sector companies, unless there is a restriction contained in the articles of association of the company, in principle, no governmental approvals, consents, filings or other formalities are required by law, for a guarantee provided by a Mozambican company to be enforceable.

However, it is common practice for there to be a requirement for either shareholder approval or board approval for granting the guarantee. Usually, such approval will contain an express reference to the benefit of the company from the provision of the guarantee (even if the benefit is an indirect one) or to the group relationship (if any) with the entity benefiting from the provision of the guarantee.

Moreover, the Mozambican Commercial Code provides that guarantees/security must be registered in an internal record book of the company.

2.5 Are net worth, solvency or similar limitations imposed on the amount of a guarantee?

No, they are not, but please see question 2.2 above as to corporate benefit.

2.6 Are there any exchange control or similar obstacles to enforcement of a guarantee?

In general terms, the import and export of foreign exchange, and the provisions of security or guarantees by a Mozambican entity to a foreign lender, are subject to prior authorisation by the Bank of Mozambique. However, there is a limited exception under Law 11/2009 (the "**Foreign Exchange Law**") and the Bank of Mozambique regulation – Aviso no. 20/GBM/2017 (the "**Foreign Exchange Regulation**", and together with the Foreign Exchange Law, "**Foreign Exchange Rules**"). Under this exception, the authorisation process can be carried out through the commercial bank used for the purpose of the import of foreign exchange.

In turn, the export of foreign exchange will only be subject to the required filing with the Bank of Mozambique, which is also done through the commercial bank in question, if the original transaction underlying the import of foreign exchange or provision of security, has previously been authorised. If no prior authorisation has been obtained, then an authorisation will be required for the export of foreign exchange resulting from the enforcement of a guarantee.

Foreign lenders must therefore ensure that the necessary authorisations are obtained from the outset so as to avoid having to obtain a specific authorisation whilst exporting funds deriving from the enforcement of security locally in Mozambique.

3 Collateral Security

3.1 What types of collateral are available to secure lending obligations?

There are various types of collateral available to secure lending obligations, such as:

(i) mortgage over real estate, aircraft, vessels, cars and industrial units (e.g. factories);

(ii) pledge over movable assets not referred to in (i) above;

(iii) pledge over a business (including inventory) – only possible if pledgee is a credit institution;

(iv) pledge of rights (including credits and receivables); and

(v) escrow of income deriving from real estate, aircrafts, vessels or cars.

Moreover, sureties, debt confessions, rights of retention or novation or assignment of receivables and other credit rights are possible.

3.2 Is it possible to give asset security by means of a general security agreement or is an agreement required in relation to each type of asset? Briefly, what is the procedure?

Under Mozambican law, the provision of generic security (i.e. over the assets of a given entity generically) is considered null and void because of a lack of determination of the specific assets that become subject to the security.

Therefore, it is necessary for a security agreement to identify, to the greatest extent possible, the assets subject to the security created by the agreement. The security agreement must at least contain certain criteria which would make it possible to identify the secured assets at a given time. The agreement must be signed by both securing and secured party, with the respective signatures certified by a notary public.

In relation to mortgages and pledges or escrow of incomes it is made through a public deed which must be signed before a notary public following which the public deed must be registered at the appropriate registry office, in accordance with the type of asset that is being encumbered.

3.3 Can collateral security be taken over real property (land), plant, machinery and equipment? Briefly, what is the procedure?

The Mozambique Constitution provides that the State is the sole owner of all land, which cannot be owned by an individual or a company. However, the State may grant the right to use land by issuing a title for the right to use and benefit from the land (in Portuguese, "*Direito de Uso e Aproveitamento da Terra",* DUAT"*).* The DUAT enables its holder to build any infrastructures or immovable asset and register it. Following the assets registration, the holder of a DUAT may create security interests over such real estate by means of a mortgage, although not over the land itself. The DUAT itself cannot be assigned by way of security or pledge.

It is possible to create a mortgage over machinery and equipment thereof by a public deed, which must include a clear identification of the plant and other assets that will be mortgaged.

3.4 Can collateral security be taken over receivables? Briefly, what is the procedure? Are debtors required to be notified of the security?

Yes, security is created by pledges over the receivables. A public deed is required, and it is also necessary to give notice of the creation of pledges to the debtors, so that they can be enforced against any third parties.

3.5 Can collateral security be taken over cash deposited in bank accounts? Briefly, what is the procedure?

Yes, pledges can be taken over cash deposited in bank accounts, which are considered pledges over credits or receivables. As with the creation of the pledge over receivables, the creation of a pledge over cash deposited in a bank account will require the execution of a public deed and notice to the bank where the account is held.

3.6 Can collateral security be taken over shares in companies incorporated in your jurisdiction? Are the shares in certificated form? Can such security validly be granted under a New York or English law governed document? Briefly, what is the procedure?

Yes, collateral security may be taken over shares in companies incorporated in Mozambique as a pledge of shares, but the perfection requirements will vary in accordance with the nature of the company.

In the case of public limited liability companies (*sociedades anónimas*), whose share capital is represented by shares (*acções*), the perfection requirements include: pledging of shares, which requires the endorsement of the share certificates by the pledger (debtor), registration of the pledge in the company's registration book, and delivery of the share certificates to the pledgee (creditor) for its perfection. If the shares are warrant-to-bearer, the delivery of the shares will be sufficient to create the security.

Regarding private limited liability companies (*sociedades por quotas*), whose share capital is represented by quotas, the perfection requirements include the execution of the pledge agreement by means of a public deed, notification to the company of the creation of the pledge (if prior consent is not required), and registration of the pledge with the Legal Entities Registry Office.

3.7 Can security be taken over inventory? Briefly, what is the procedure?

Yes, security over inventory is possible if such security is granted in favour of a credit institution. The procedure includes the execution of a written agreement.

3.8 Can a company grant a security interest in order to secure its obligations (i) as a borrower under a credit facility, and (ii) as a guarantor of the obligations of other borrowers and/or guarantors of obligations under a credit facility (see below for questions relating to the giving of guarantees and financial assistance)?

Yes, but please see the restrictions on the provision of guarantees in question 2.1 above, which are also applicable in relation to the provision of a security interest by companies.

3.9 What are the notarisation, registration, stamp duty and other fees (whether related to property value or otherwise) in relation to security over different types of assets?

The creation of any type of securities are subject to notarial fees, registration fees and stamp duty which is calculated based on the type of security and the period for which it is granted. Mortgages and pledges are subject to stamp duty of 0.3%, unless the transaction is deemed ancillary to another transaction (loan), already subject to stamp duty as follows:

(a) for loans with maturity five years or more, a rate of 0.5% will apply, in addition to the fixed fee charged by the notary to certify the signatures;

(b) for loans with maturity of more than one but less than five years, a rate of 0.4% will apply, in addition to the fixed fee charged by the notary to certify the signatures; and

(c) for loans with maturity of no more than one year, a rate of 0.03% will apply, in addition to the fixed fee charged by the notary to certify the signatures.

3.10 Do the filing, notification or registration requirements in relation to security over different types of assets involve a significant amount of time or expense?

The filing, notification and registration procedures can be more efficient and may not take a significant amount of time, but it will depend on the amounts involved and the location where these acts take place, as timeframes may vary according to whether the acts take place in Maputo (the capital) or in other provinces.

3.11 Are any regulatory or similar consents required with respect to the creation of security?

No regulatory or similar consents apply, except for assets held by state-owned entities or shares of concessionaires of public services, which must be assessed on a case-by-case basis.

If a foreign lender is involved, the creation of security is subject to prior authorisation from the Bank of Mozambique.

3.12 If the borrowings to be secured are under a revolving credit facility, are there any special priority or other concerns?

No, there are not.

3.13 Are there particular documentary or execution requirements (notarisation, execution under power of attorney, counterparts, deeds)?

Yes, the creation of security over real estate requires the execution of a deed, usually made before a notary, as does a pledge of shares. If a power of attorney is required to execute these acts, it must also be executed before a notary public, and if the power of attorney is to be executed outside Mozambique, it must be legalised before the Ministry of Foreign Affairs and the local Mozambican Consulate. The execution of a deed in Mozambique before a notary requires the parties (whether Mozambican or foreign entities) to have a legal entity and tax identification number. The provision of this number is also required to register a security interest in favour of a given entity.

4 Financial Assistance

4.1 Are there prohibitions or restrictions on the ability of a company to guarantee and/or give security to support borrowings incurred to finance or refinance the direct or indirect acquisition of: (a) shares of the company; (b) shares of any company which directly or indirectly owns shares in the company; or (c) shares in a sister subsidiary?

(a) Shares of the company

A company may not provide security or a guarantee to a third party for such party to acquire the shares in the company.

(b) Shares of any company which directly or indirectly owns shares in the company

No express prohibition exists. However, corporate powers of the company may be restricted in respect of granting of guarantees or security – please see question 2.1 above.

(c) Shares in a sister subsidiary

No express prohibition exists, but the corporate powers of the company may be restricted in respect of granting of guarantees or security – please see question 2.1 above.

5 Syndicated Lending/Agency/Trustee/Transfers

5.1 Will your jurisdiction recognise the role of an agent or trustee and allow the agent or trustee (rather than each lender acting separately) to enforce the loan documentation and collateral security and to apply the proceeds from the collateral to the claims of all the lenders?

In Mozambique, the system is more limited because, if the agent is to have the benefit of security under Mozambican law, it can only render its services if it has first been recognised and authorised by the Bank of Mozambique, under the Law of Credit Institutions and Financial Companies.

5.2 If an agent or trustee is not recognised in your jurisdiction, is an alternative mechanism available to achieve the effect referred to above which would allow one party to enforce claims on behalf of all the lenders so that individual lenders do not need to enforce their security separately?

Yes. A power of attorney may be given to one creditor to enforce the claims against debtors.

5.3 Assume a loan is made to a company organised under the laws of your jurisdiction and guaranteed by a guarantor organised under the laws of your jurisdiction. If such loan is transferred by Lender A to Lender B, are there any special requirements necessary to make the loan and guarantee enforceable by Lender B?

Yes, notice to the borrower and guarantor of the assignment is required, as is registration of the security (if subject to registration) with the appropriate registry (land registry, commercial registry, motor vehicle registry, financial intermediary or company books, as applicable).

In addition, the assignment of security against a company that is subject to insolvency proceedings will, from a practical perspective, also require notice being given to the court of the assignment so that the new creditor can be recognised in the insolvency proceedings.

However, please note that there may be situations in which the guarantee may not be assigned. For example, if the parties have restricted the ability of the guarantor to assign, or if the guarantee has been provided *intuitu personae* (i.e. the nature of the guarantee is not separable from the person or the borrower).

6 Withholding, Stamp and Other Taxes; Notarial and Other Costs

6.1 Are there any requirements to deduct or withhold tax from (a) interest payable on loans made to domestic or foreign lenders, or (b) the proceeds of a claim under a guarantee or the proceeds of enforcing security?

The Corporate Income Tax ("**CIT**") must be withheld upon the payment of the interest on loans made to domestic or foreign lenders. Interest payments between resident companies are subject to CIT withholding at the rate of 20%, except in the situation where the creditor is a bank. Interest derived from treasury bonds and public securities listed on the Mozambique Stock Exchange is subject to CIT withholding at a reduced rate of 10%. Nevertheless, certain exemptions from CIT withholding may apply in the following scenarios:

- interest or similar payments in respect of loans, credit or arrears in payment, accruing to credit institutions resident for tax purposes in Mozambique, subject to CIT in respect of such interest, even if exempt regarding the same; and
- interest or any increase in value, deriving from the extension of the maturity date or arrears in payment, when such credit results from sales or services provided by corporate persons or other entities which are subject to CIT in respect of such interest or increase.

In the case of payment of interest on loans made to foreign lenders, upon the payment of the interest, the entity resident in Mozambique must withhold CIT at a rate of 20%, and this rate is considered definitive.

There are no specific withholding tax rules for claims under a guarantee or the proceeds of enforcing a security.

In fact, in the case of issuance of guarantees, including mortgages, bank guarantees, securities and pledges (unless ancillary to a contract already subject to stamp duty), the following rates apply: 0.02% a month for each month or fraction, 0.2% and 0.3% a year on the amount involved, depending on whether or not the repayment period is less than one year, less than five years, or more than five years, respectively.

6.2 What tax incentives or other incentives are provided preferentially to foreign lenders? What taxes apply to foreign lenders with respect to their loans, mortgages or other security documents, either for the purposes of effectiveness or registration?

There are no tax incentives provided preferentially to foreign lenders. The Tax Benefits Code provides for certain tax incentives which are only applicable to investment under the investment legislation. These include a general incentive scheme and a specific investment scheme regarding certain sectors of activity, but they are not specifically related to loans.

As regards taxes applicable to foreign lenders, please see our comments above in question 6.1. In addition, please bear in mind that granting a loan or credit arrangement is subject to stamp duty, as follows:

- loan or credit arrangement for less than one year: 0.03% a month or part thereof;
- loan or credit arrangement for one to five years: 0.4% a year; and
- loan or credit arrangement for five or more years: 0.5% a year.

6.3 Will any income of a foreign lender become taxable in your jurisdiction solely because of a loan to or guarantee and/or grant of security from a company in your jurisdiction?

Yes, as mentioned above, in the case of payment of interest on loans made to foreign lenders, upon the payment of the interest, the entity resident in Mozambique must withhold CIT at a rate of 20%, and this rate is considered definitive.

6.4 Will there be any other significant costs which would be incurred by foreign lenders in the grant of such loan/guarantee/security, such as notarial fees, etc.?

Certain transaction costs will apply irrespective of whether the lender is a foreign or domestic entity. These include notarial and registration fees in the context of the granting or the perfection of security in Mozambique.

6.5 Are there any adverse consequences to a company that is a borrower (such as under thin capitalisation principles) if some or all of the lenders are organised under the laws of a jurisdiction other than your own? Please disregard withholding tax concerns for purposes of this question.

No, there are not.

7 Judicial Enforcement

7.1 Will the courts in your jurisdiction recognise a governing law in a contract that is the law of another jurisdiction (a "foreign governing law")? Will courts in your jurisdiction enforce a contract that has a foreign governing law?

In accordance with the general principle set out in the Mozambican Civil Code, the parties to an agreement may elect the law governing the agreement, provided that such election corresponds to a serious interest of the parties or is the law of a jurisdiction which has a connection with the agreement and is legitimate in the context of the principles of private international law.

If a contract contains a choice of forum clause, in principle, Mozambican courts will not hear any case arising from the contract subject to the jurisdiction of foreign courts. However, once the foreign court has issued its judgment, it is possible to apply to the Mozambican courts for recognition and enforcement of that judgment.

7.2 Will the courts in your jurisdiction recognise and enforce a judgment given against a company in New York courts or English courts (a "foreign judgment") without re-examination of the merits of the case?

Any final judgment obtained in a competent jurisdiction in respect of any sums payable in connection with the Term Loan Agreement would be enforced by the courts of Mozambique under the conditions set out in the Code of Civil Procedure, without re-examination of the merits of the case provided that:

(a) there are no doubts about the authenticity or substance of the document in which the judgment is given, and the judgment is final and conclusive;

(b) the defendant has been served with notice of the proceedings, unless there is a basis under Mozambican law to waive the requirement for initial notification; and, if judgment was made against the defendant immediately, without the defendant having filed a defence, the notification must have been served on the defendant directly;

(c) any conditions imposed by the law of the country in which the judgment was given, which are conditions to its enforcement in the Mozambican courts, have been complied with;

(d) the judgment was issued by a foreign court, the jurisdiction of which had not been claimed fraudulently, and the judgment does not pertain to matters subject to the exclusive jurisdiction of the Mozambican courts;

(e) the judgment would not be adjudged *res judicata* by the Mozambican courts;

(f) the defendant was served with the action in accordance with the law of the country in which the judgment was issued and the principles of the right to a fair trial (*principio do contraditório*) and equal treatment of the parties have been complied with;

(g) if the judgment was made against a Mozambican citizen, it must not offend the provisions of private law in Mozambique, when by this the matter should be resolved under the rules of conflict of Mozambican law; and

(h) it does not contravene the principles of Mozambican public order.

7.3 Assuming a company is in payment default under a loan agreement or a guarantee agreement and has no legal defence to payment, approximately how long would it take for a foreign lender to (a) assuming the answer to question 7.1 is yes, file a suit against the company in a court in your jurisdiction, obtain a judgment, and enforce the judgment against the assets of the company, and (b) assuming the answer to question 7.2 is yes, enforce a foreign judgment in a court in your jurisdiction against the assets of the company?

In general, filing a suit in Mozambique, obtaining a judgment and enforcing it takes on average 24 months. Enforcing a foreign judgment in Mozambique against the assets of the company could take at least 12 months. In both scenarios, the timeframe for enforcement of the court decision will depend on how long it takes to identify the assets to be seized and the workload of the judge deciding on the case.

7.4 With respect to enforcing collateral security, are there any significant restrictions which may impact the timing and value of enforcement, such as (a) a requirement for a public auction, or (b) regulatory consents?

Yes, timing of the enforcement may be affected in the event that there is a public auction of the assets or in the event that such auctions are not successful, if, for instance, no offers higher than the reserve price are received.

Regulatory consents may also impose a significant delay in the conclusion of the enforcement in the event that the sale of the enforced assets to the acquirer is subject to obtaining regulatory consents, in the context of activities subject to licensing.

7.5 Do restrictions apply to foreign lenders in the event of (a) filing suit against a company in your jurisdiction, or (b) foreclosure on collateral security?

No, in principle, no such restrictions will apply.

7.6 Do the bankruptcy, reorganisation or similar laws in your jurisdiction provide for any kind of moratorium on enforcement of lender claims? If so, does the moratorium apply to the enforcement of collateral security?

Yes, pursuant to the Mozambican Insolvency Code, the start of insolvency proceedings will suspend all proceedings to enforcement collateral security.

7.7 Will the courts in your jurisdiction recognise and enforce an arbitral award given against the company without re-examination of the merits?

Although Mozambique is a signatory to the New York Arbitration Convention, the country has a reservation that any arbitral award given in another contracting state will only be recognised without re-examination of the merits of the claim on the basis of reciprocity, where the arbitral awards have been pronounced in the territory of another contracting state.

The enforcement of any arbitral decision given in a state which is not party to the New York Arbitration Convention is subject to re-examination of its merits.

8 Bankruptcy Proceedings

8.1 How does a bankruptcy proceeding in respect of a company affect the ability of a lender to enforce its rights as a secured party over the collateral security?

Under the Mozambican Insolvency Code, the start of insolvency proceedings will suspend all enforcement proceedings against the company and the debtor will be unable to carry on its business activity.

Under the applicable rules, securities over the debtor's assets will be enforced within the bankruptcy proceedings.

8.2 Are there any preference periods, clawback rights or other preferential creditors' rights (e.g., tax debts, employees' claims) with respect to the security?

Under the Mozambican Insolvency Code, creditors are usually paid in the following order:

(i) employment credits;
(ii) secured credits;
(iii) tax credits;
(iv) ordinary credits;
(v) contractual and tax penalties; and
(vi) subordinated credits.

In cases where different securities have been granted over the same asset, the first creditor will be paid first, and the rest will follow under the same criteria.

The granting of security by the insolvent entity to secure previous debt shall be considered ineffective against the insolvent estate irrespective of whether or not the creditor has knowledge of the economic and financial hardship situation of the debtor.

In addition, any acts, including the granting of security or provision of guarantees carried out with the intention to defraud creditors may be clawed back if fraudulent collusion between the debtor and the other contracting party and the effective damage suffered by the insolvent estate are proven.

8.3 Are there any entities that are excluded from bankruptcy proceedings and, if so, what is the applicable legislation?

Yes, the Mozambican Republic and public companies are excluded from bankruptcy proceedings.

8.4 Are there any processes other than court proceedings that are available to a creditor to seize the assets of a company in an enforcement?

No, please refer to the answer provided in question 8.1.

9 Jurisdiction and Waiver of Immunity

9.1 Is a party's submission to a foreign jurisdiction legally binding and enforceable under the laws of your jurisdiction?

Yes, it is. Parties may choose to be bound under a foreign jurisdiction – please refer to question 7.1 above.

9.2 Is a party's waiver of sovereign immunity legally binding and enforceable under the laws of your jurisdiction?

In the event that an entity benefits from sovereign immunity, waiver of that benefit will not be valid in Mozambique.

10 Licensing

10.1 What are the licensing and other eligibility requirements in your jurisdiction for lenders to a company in your jurisdiction, if any? Are these licensing and eligibility requirements different for a "foreign" lender (i.e. a lender that is not located in your jurisdiction)? In connection with any such requirements, is a distinction made under the laws of your jurisdiction between a lender that is a bank *versus* a lender that is a non-bank? If there are such requirements in your jurisdiction, what are the consequences for a lender that has not satisfied such requirements but has nonetheless made a loan to a company in your jurisdiction? What are the licensing and other eligibility requirements in your jurisdiction for an agent under a syndicated facility for lenders to a company in your jurisdiction?

A foreign lender must be accredited to be recognised in Mozambique to provide financial services. Under the Law of Credit Institutions and Financial Companies, banks are the only credit institutions able to provide credits and other financial services.

Any lender who provides loans without meeting the legal requirements is subject to criminal liability which will be assessed under the Criminal Code.

11 Other Matters

11.1 Are there any other material considerations which should be taken into account by lenders when participating in financings in your jurisdiction?

We believe that the questions above fairly address the main material issues that generally arise in the context of lending transactions.

Nuno Morgado Pereira

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Nuno Morgado Pereira is an associate lawyer of PLMJ, in Lisbon, being also a member of the banking and finance department of TTA law firm, in Maputo. Nuno's practice covers a broad range of banking & finance and foreign investment matters, since he has been involved in a large proportion of the firm's recent financial transactions, public-private partnerships and project finance matters, including real estate investment projects, oil & gas projects and industrial-related projects. His experience includes construction, corporate, finance and commercial contracts and special ability dealing with the Bank of Mozambique, in relation to not only regulatory control matters, but also foreign exchange regulation, since he also holds a Master's degree in Public and Administrative Law.

Nuno earned his law degree from Universidade Nova de Lisboa in 2011, and his Master's degree from Universidade Católica Portuguesa, in 2013. He is also entitled to practise under both Portuguese and Mozambican law as a member of the Portuguese and Mozambican Bar Associations since 2015 and 2016, respectively.

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Gonçalo dos Reis Martins has gained a comprehensive experience over the last 15 years in advising leading international and domestic investment and retail banks, other financial institutions and asset managers in a wide range of transactions, including syndicated loans for Portuguese blue chip corporates, asset finance transactions for the oil industry, project finance, direct lending, multi-jurisdictional supply chain finance transactions and Islamic finance work. He has also been involved in the development of the contractual framework in offering by banks of new technology-based products for retail clients as well as in the engagement of Portuguese banks by Fintech companies.

Before joining PLMJ he worked at another leading Portuguese law firm and gained valuable international experience, having been seconded to the Capital Markets department of Simmons & Simmons and Morgan Stanley's Legal Department (Fixed Income Division), both in London.

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TTA is a law firm that brings together a group of leading Mozambican professionals who share extensive knowledge of the local legal world and a culture of international legal service. What unites this team is a common interest and satisfaction in working in and for Mozambique, in strict compliance with the rules of professional ethics of the Mozambican bar association.

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The PLMJ Finance team acts in all areas of banking, finance and capital markets.

In the banking and finance segments, the team regularly deals with domestic and cross-border operations in the areas of corporate finance, real estate financing, leveraged and acquisition finance, asset finance, project finance, structured finance, factoring and trade finance.

Norway

Advokatfirmaet CLP DA

Ragnhild Steigberg

1 Overview

1.1 What are the main trends/significant developments in the lending markets in your jurisdiction?

The Norwegian lending market is still recovering from the steep drop in oil prices and the consequential financial distress for many borrowers in the shipping/offshore sector, which started in 2014. Several of the largest Norwegian banks have significant exposure to the shipping/offshore market, and are involved with ongoing processes of restructuring and rescheduling of debt, of which the outcome is still uncertain. With oil prices rising again (February 2018), the situation is improving. Norwegian banks are also obliged to be compliant with the EU Capital Requirements Directive (2013/36 (CRD IV)) and the Capital Requirement Regulation (575/213 (CRR)), which has forced some Norwegian banks to reduce their lending exposure in order to comply with capital adequacy rules. The real estate market, both private housing and commercial property, is, however, strong, and many banks have continued to increase their lending within the real estate sector. On the leveraged side, we see an increase in deals with a light covenant structure, with favourable pricing for the borrower. It will be interesting to see whether Norwegian (and other Nordic banks) will be able to compete with foreign banks on the applicable terms going forward.

Where the Norwegian bank market may not have been as active as before in terms of new deals, the Norwegian bond market has provided substantial financing, and reached an all-time high in 2017. Real estate and shipping are some of the sectors that have taken large parts of this market, and banks are financing themselves through the issuance of covered bonds. In addition to availability, there are some cases where the bond market has been able to compete with the bank market in terms of pricing.

1.2 What are some significant lending transactions that have taken place in your jurisdiction in recent years?

In November 2016, CigitalGroup (owned by HgCapital) as borrower, secured a NOK 3,674 million-equivalent (as subsequently upsized by an additional NOK 600 million) facility from Norwegian banks DNB Bank ASA as Agent and Security Agent, and DNB Bank ASA and Skandinaviska Enskilda Banken AB (Publ) as Bookrunners, Mandated Lead Arrangers and Lenders, for the purpose of financing the acquisition of parts of the Visma-group. The transaction marked one of the largest software buyouts in Europe.

The restructuring of the "Norske Skog" debt, and the negotiations between the various groups of creditors also raised much attention this year, before the company went into bankruptcy proceedings at the end of 2017. Also, the restructuring of Seadrill Limited's debt, which bank debt is mainly governed by Norwegian law, has raised attention in the industry and is still ongoing.

2 Guarantees

2.1 Can a company guarantee borrowings of one or more other members of its corporate group (see below for questions relating to fraudulent transfer/financial assistance)?

According to the Norwegian Limited Liability Companies Act, and the corresponding Norwegian Public Limited Liability Company Act of 13 June 1997 (hereinafter collectively referred to as the "NLC"), a private or a public limited liability company can provide guarantees for the benefit of its parent company or another company within its corporate group (Nw: *konsern*). This, however, only applies where such parent company is a Norwegian company, or where such other company within its corporate group has a parent company incorporated in Norway. In cases where there is not a Norwegian parent company, the company may only provide such guarantee if the guarantee will benefit the financial interest of the group of companies which the company forms a part of. It is not sufficient that the guarantee benefits only the company which the guarantee is provided in favour of, it will also need to benefit at least one other company of this group. Guarantees may also generally be provided to the benefit of other members of its corporate group, but, unless it satisfies the requirements above, such guarantee will be heavily restricted and subject to procedural requirements, which makes their value limited.

2.2 Are there enforceability or other concerns (such as director liability) if only a disproportionately small (or no) benefit to the guaranteeing/securing company can be shown?

According to the NLC, the board of directors of a Norwegian company may not take any actions which may give certain shareholders or other parties an unreasonable advantage at the cost of the remaining shareholders or the company. Providing a guarantee/security without sufficient corporate benefit may constitute such unreasonable advantage, and will, in such case, be prohibited. A breach of this prohibition may result in the guarantee/security being deemed invalid and/or unenforceable, unless the beneficiary was, in good faith, acting diligently. The relevant director(s) may also, in addition to or as an alternative to such invalidity and/or enforceability, be held liable for damages incurred by the company, its shareholders, or its or the company's creditors.

2.3 Is lack of corporate power an issue?

Neither each separate director, nor any member of the company's administration, has general corporate power to bind a company in respect of providing guarantees or security, unless it is otherwise stated in the company's articles of association. Providing guarantees or security will often be considered a matter of significance to the company, and need therefore to be approved by the company's board of directors. The board of directors can then delegate such powers to any director, members of the administration, attorneys or others, in which case such person will be acting on the authority granted by the board of directors. If, for example, a board member has acted without the necessary approval of the board of directors when issuing a guarantee, such guarantee may be invalid, unless the beneficiary was, in good faith, acting diligently. Consequently, we generally advise clients to obtain evidence of corporate power by way of a board resolution approving such guarantee, and the authorisation of the person acting on behalf of the company in relation thereto to avoid any subsequent dispute relating to corporate power.

2.4 Are any governmental or other consents or filings, or other formalities (such as shareholder approval), required?

No governmental consents are required for a company to provide a guarantee, nor are there any filings or other formal requirements. Generally, shareholders' approval is not required, but for guarantees that do not fulfil the requirements described above under question 2.1, shareholders' approval is necessary to ensure the validity and enforceability of such guarantee. As mentioned, this is not very practical.

2.5 Are net worth, solvency or similar limitations imposed on the amount of a guarantee?

There are no net worth, solvency or other absolute limitations on the amount of a guarantee, provided that sufficient corporate benefit is always present. However, when a guarantee is provided for the benefit of a financial institution, the guarantee needs to contain a cap which represents the highest amount which can be recovered pursuant to such guarantee. The parties to a guarantee are free to agree on the amount of such cap, and are not bound by net worth, solvency or similar limitations when doing so.

2.6 Are there any exchange control or similar obstacles to enforcement of a guarantee?

There are no such restrictions applicable to the enforcement of a guarantee.

3 Collateral Security

3.1 What types of collateral are available to secure lending obligations?

Norwegian law only allows for assets specifically listed in relevant legislation to be used as collateral for a lending obligation. These include, *inter alia*, real estate, shares, aircraft, vessels, rigs, claims (including bank accounts, insurance claims, loans, receivables, etc.), inventory, and machinery and plant. Norwegian law does not allow for a general floating charge covering all assets of the company, as is the case in many other jurisdictions.

3.2 Is it possible to give asset security by means of a general security agreement or is an agreement required in relation to each type of asset? Briefly, what is the procedure?

As mentioned above, a general all-asset floating charge is not possible. However, drafting wise, it is possible to include all assets which are to be pledged into one general security agreement as opposed to having numerous security agreements. All assets which are to be covered by that agreement will need to be sufficiently identified according to their relevant legal requirements, and perfection of the security will need to be done in relation to each type of asset (registration, notification, etc.) as applicable.

3.3 Can collateral security be taken over real property (land), plant, machinery and equipment? Briefly, what is the procedure?

Yes, this can be done. Security over real property (ownership, rights under leasing agreement and certain other rights) is established by the parties entering into a mortgage agreement, which is perfected by registration with the land register on a designated mortgage form. The mortgagor may typically continue to use the real property irrespective of the mortgage for as long as no event of default has occurred.

Security over machinery and plant (including equipment) is also established by the parties entering into a mortgage agreement, which is perfected by registration with the register of movable assets on a designated mortgage form. The machinery, plant and equipment is then mortgaged collectively as a pool of assets, and the mortgagor may continue the use of its machinery and plant, and may sell and/or replace items within the pool of assets in accordance with the ordinary course of business. The mortgagor may not dispose the entire pool of assets as such without breaching the provisions of the Norwegian Mortgage Act of 8 February 1980 (the "**Mortgage Act**"). As the mortgagor is able to dispose of assets within the ordinary course of business, a mortgagee may want to take separate mortgages in certain assets forming part of the plant, machinery and equipment of the mortgagor, if such assets are considered of particular importance to the mortgagee. Such separate mortgages can be taken as a non-possessory mortgage over cars, movable production machinery used by contractors, certain railway equipment (locomotives, etc.), certain agricultural equipment, and certain fishing equipment. Other forms of plant, machinery and equipment will need to be mortgaged and perfected by way of the mortgagee taking possession of the asset, so this is less practical if such equipment is used in the business of the mortgagor.

3.4 Can collateral security be taken over receivables? Briefly, what is the procedure? Are debtors required to be notified of the security?

There are two ways of taking security over receivables under Norwegian law. The first is the pledge of identified claims against named debtors, which the mortgagor has, or may have, in the future. These claims can be assigned pursuant to an agreement which identifies the relevant claims, and perfected by way of notification of the assignment to the debtor.

It is also possible to take collateral security over receivables in general, by way of a floating charge. This is possible for receivables that a chargor has, or may have, in the future, and which are compensation from the sale of goods or services in the business of the chargor. For these receivables, the debtors do not need to be notified for the purpose of perfection, as perfection is obtained by registration in the register of mortgaged movable assets. The debtors will of course need to be notified if and when the security is enforced.

3.5 Can collateral security be taken over cash deposited in bank accounts? Briefly, what is the procedure?

Yes, this is both possible and practical. Security is established by the entering into of a security agreement between the pledgor and the pledgee, and perfection is obtained by way of notification to the bank account. The account can remain un-blocked at the pledgor's disposal until an event of default has occurred, or the parties can agree to block the account for as long as the security is in place. In cases where the bank account is also the pledgee, security can also be established by an agreement of set-off.

3.6 Can collateral security be taken over shares in companies incorporated in your jurisdiction? Are the shares in certificated form? Can such security validly be granted under a New York or English law governed document? Briefly, what is the procedure?

Security can be taken over shares in Norwegian companies. Shares are not in certificated form. For shares in private limited liability companies, perfection is obtained by way of notification to the company whose shares are pledged. The company should then register the security in its shareholders' register, but this registration is not a perfection requirement. Security over shares in private limited liability companies is not subject to registration in any public register. For shares in a public company whose shares are registered with the VPS (a securities register), the security will need to be registered in the VPS in order to be perfected.

The appropriate choice of law for security over shares in a Norwegian company is Norwegian law. As long as the Norwegian law perfection requirement is fulfilled (notification or registration as per above), a court of law may respect New York or English law as the governing law document for such security, but this is not something we see in the current loan market.

3.7 Can security be taken over inventory? Briefly, what is the procedure?

Security can be taken over inventory as a pool of assets, pursuant to an agreement between the pledgor and the pledgee. The agreement needs to be registered in the register of mortgaged movable assets in order to obtain perfection. The security permits the pledgor to use the inventory, and to dispose of and/or exchange parts of the inventory in accordance with its ordinary course of business. Our summary under question 3.3 above regarding machinery and plant applies correspondingly to security over inventory.

3.8 Can a company grant a security interest in order to secure its obligations (i) as a borrower under a credit facility, and (ii) as a guarantor of the obligations of other borrowers and/or guarantors of obligations under a credit facility (see below for questions relating to the giving of guarantees and financial assistance)?

Yes, a Norwegian company can grant a security interest for its own obligations as borrower, and a security interest and/or guarantee for the obligations of other borrowers. We refer also to our reply under question 2.1 above.

3.9 What are the notarisation, registration, stamp duty and other fees (whether related to property value or otherwise) in relation to security over different types of assets?

No such fees are relevant in Norway, save for registration fees for certain security (ref. above). None of these registration fees correlate in any way to the value of assets being secured, and the fees are not significant.

3.10 Do the filing, notification or registration requirements in relation to security over different types of assets involve a significant amount of time or expense?

The various filings/registrations will generally be completed within a matter of hours or days, and, in our view, do not involve a significant amount of expenses, ref. above.

3.11 Are any regulatory or similar consents required with respect to the creation of security?

In general, no. If security is granted by a company which engages in regulated activity, or the asset itself is used in regulatory activity, regulatory restrictions and consents may be relevant.

3.12 If the borrowings to be secured are under a revolving credit facility, are there any special priority or other concerns?

There are no such special priorities or concerns to be considered, and, unless otherwise agreed between the parties, the security will not be affected by the continuous utilisation and re-payment under such facility.

3.13 Are there particular documentary or execution requirements (notarisation, execution under power of attorney, counterparts, deeds)?

There are no such relevant requirements for the creation of any security. For security perfected by way of registration, the registration forms may need to be signed by one or two witnesses, and the register may need proof of authorisation of the signatory before registering and perfecting the security.

4 Financial Assistance

4.1 Are there prohibitions or restrictions on the ability of a company to guarantee and/or give security to support borrowings incurred to finance or refinance the direct or indirect acquisition of: (a) shares of the company; (b) shares of any company which directly or indirectly owns shares in the company; or (c) shares in a sister subsidiary?

(a) Shares of the company

Yes, restrictions apply. The relevant NLC states that a private limited liability company may only guarantee or provide security to the extent the same is available as permitted distribution from the company. Any financial assistance shall be provided on customary business terms, and sufficient security shall be provided for the claim for repayment if the guarantee is honoured and/or the security enforced. Financial assistance can only be provided for shares which are fully paid-up. There are also certain procedural requirements (credit assessment, preparation of statement from the board directors, approval by general meeting, etc.) which need to be complied with. For public limited liability companies, the same restrictions and requirements apply, and the statement from the board of directors has to be filed with the Norwegian Register of Business Enterprises. Consequently, it is not practical for a company to support borrowings incurred to finance or refinance the acquisition of its shares.

(b) Shares of any company which directly or indirectly owns shares in the company

The same rules as set out above also applies for shares of a parent company.

(c) Shares in a sister subsidiary

No financial assistance restrictions apply.

5 Syndicated Lending/Agency/Trustee/Transfers

5.1 Will your jurisdiction recognise the role of an agent or trustee and allow the agent or trustee (rather than each lender acting separately) to enforce the loan documentation and collateral security and to apply the proceeds from the collateral to the claims of all the lenders?

There is no Norwegian legislation that permits an agent or a trustee to enforce loan documentation or security in its own name. However, the Norwegian Supreme Court has recognised the right of a bond trustee to enforce the loan documentation and security/guarantee in a case where the bond documentation clearly assumed this, and where the court found that there was a sufficient practical need for the trustee to have these rights. The concept has not been tested for agents in bank loans, but it is likely that the same concept will apply if the other merits of such case are similar. It is, however, difficult to say something certain about the extent of the Supreme Court's decision in this case, so lenders may want to join legal proceedings as claimants in order to be certain that the court will accept the lawsuit.

5.2 If an agent or trustee is not recognised in your jurisdiction, is an alternative mechanism available to achieve the effect referred to above which would allow one party to enforce claims on behalf of all the lenders so that individual lenders do not need to enforce their security separately?

This is not applicable, please see question 5.1 above.

5.3 Assume a loan is made to a company organised under the laws of your jurisdiction and guaranteed by a guarantor organised under the laws of your jurisdiction. If such loan is transferred by Lender A to Lender B, are there any special requirements necessary to make the loan and guarantee enforceable by Lender B?

Provided that the transfer of the loan is permitted pursuant to the underlying loan agreement, the only requirement in order for the loan and guarantee to be enforceable by Lender B is that the borrower and guarantor is notified of the transfer.

6 Withholding, Stamp and Other Taxes; Notarial and Other Costs

6.1 Are there any requirements to deduct or withhold tax from (a) interest payable on loans made to domestic or foreign lenders, or (b) the proceeds of a claim under a guarantee or the proceeds of enforcing security?

As of today, there is no withholding tax in Norway. Politicians have notified that withholding tax may be implemented in the future, but it is uncertain whether this will ever be implemented, and if so, in which form.

6.2 What tax incentives or other incentives are provided preferentially to foreign lenders? What taxes apply to foreign lenders with respect to their loans, mortgages or other security documents, either for the purposes of effectiveness or registration?

There are no preferentially or punitive taxes for foreign lenders.

6.3 Will any income of a foreign lender become taxable in your jurisdiction solely because of a loan to or guarantee and/or grant of security from a company in your jurisdiction?

No, a foreign lender will not be deemed tax resident (or otherwise taxable) in Norway solely due to a loan or a guarantee/security.

6.4 Will there be any other significant costs which would be incurred by foreign lenders in the grant of such loan/guarantee/security, such as notarial fees, etc.?

From a Norwegian law point of view, the granting of a loan or the signing of a loan agreement will not require any signatures to be notarised and consequently not trigger any notarial fees. If the loan document is to be filed abroad (for instance, as an attachment to foreign law security), the lenders may need to notarise and legalise their signatures, but the notarial cost will then be incurred in the foreign lender's jurisdiction on that jurisdiction's notarial rates.

6.5 Are there any adverse consequences to a company that is a borrower (such as under thin capitalisation principles) if some or all of the lenders are organised under the laws of a jurisdiction other than your own? Please disregard withholding tax concerns for purposes of this question.

There are no such adverse consequences.

7 Judicial Enforcement

7.1 Will the courts in your jurisdiction recognise a governing law in a contract that is the law of another jurisdiction (a "foreign governing law")? Will courts in your jurisdiction enforce a contract that has a foreign governing law?

As a general principle, Norwegian courts will recognise the parties' choice of a foreign law as the governing law of contract, insofar as such governing law does not contravene with Norwegian fundamental legal principles ("*ordre public*"), or relates to an area where Norwegian law is mandatory, which is typically relevant for legislation relating to consumer protection. There are, however, exceptions for matters relating to bankruptcy; for instance, the validity and effectiveness of a pledge/charge/assignment, and hardening periods relating thereto. In these cases, Norwegian courts may not apply the choice of law which has been agreed between the parties, but instead apply Norwegian law and Norwegian rules when considering the effectiveness of such document. If a Norwegian court does apply foreign law, the judgment made on this basis will be enforceable by Norwegian courts.

7.2 Will the courts in your jurisdiction recognise and enforce a judgment given against a company in New York courts or English courts (a "foreign judgment") without re-examination of the merits of the case?

Norwegian courts may enforce foreign judgments either on the basis of 1) a convention or agreement between Norway and the relevant foreign state, or 2) on the basis of a written agreement between the parties to the dispute where the parties have agreed that the foreign court has jurisdiction over the claim (with certain exceptions applying for consumer contracts). Norwegian courts will recognise and enforce a judgment given by English courts on the basis of the 2007 Lugano Convention. For judgments by New York courts, Norwegian courts will recognise and enforce the judgment if New York jurisdiction has been agreed between the parties, as set out in alternative 2) above; subject, however, to the "*ordre public*" exception mentioned in question 7.1 above.

7.3 Assuming a company is in payment default under a loan agreement or a guarantee agreement and has no legal defence to payment, approximately how long would it take for a foreign lender to (a) assuming the answer to question 7.1 is yes, file a suit against the company in a court in your jurisdiction, obtain a judgment, and enforce the judgment against the assets of the company, and (b) assuming the answer to question 7.2 is yes, enforce a foreign judgment in a court in your jurisdiction against the assets of the company?

If there is no legal defence to the payment, we assume that the hearing itself will not take more than one day. The timing for scheduling the hearing will depend on the workload of the court, which varies from court to court. In the district court of Oslo, which is the largest district court in Norway, it currently takes approximately six months from the service of first process until the hearing is scheduled. The court should then decide on the case within one month following the hearing, and the defendant has one month to appeal the judgment before it is final and enforceable. The enforceable judgment can then be filed with the local enforcement authorities, who will attach a distraint on relevant asset(s) of the debtor, a process which can take up to several months (again depending on the workload of the enforcement authorities). Timing for realisation of the asset varies significantly depending on the asset (real estate, ship, amounts credited to a bank account) and again the workload of the enforcement authorities, but one should expect at least a few months for this step as well.

If the claim is un-disputed, the creditor may also send a statement to the debtor, describing the basis for the claim and its amount. If the debtor does not object to this statement, the statement will have the same status as an enforceable judgment. If the claim is documented by way of a debenture (Nw: *gjeldsbrev*), which satisfy certain formal requirements set out by law, such debenture can be enforced directly without having to obtain a judgment.

If the foreign judgment qualifies for direct enforcement, this will have the same status as an enforceable Norwegian judgment. The timing for enforcing the foreign judgment will therefore be similar to enforcing a Norwegian judgment, with a few months to attach the distraint on the asset, and a few additional months for the realisation.

7.4 With respect to enforcing collateral security, are there any significant restrictions which may impact the timing and value of enforcement, such as (a) a requirement for a public auction, or (b) regulatory consents?

Collateral security shall be enforced in a way that generates the highest revenue. This can include realisation by way of an auction, if and when the enforcement authorities considers this to provide the highest revenue, but it can also include handing the asset over to the pledgee for a set price. For enforcement of real estate, the district court will need to consent to the sale, which can delay the process for months, and which may affect the value of the real estate. Regulatory consents are generally not required. However, if the relevant asset is subject to a regulatory consent (i.e. the property is used for regulated activity), consent by the relevant authority may also need to be obtained.

For some assets, Norwegian law permits simplified enforcement. According to the Norwegian Act on Financial Collateral (implementing EU directive 2002/47/EF) (the "**Financial Collateral Act**"), parties to a security agreement can agree on the method of enforcement, which can include, *inter alia*, transfer of ownership from the pledgor to the pledgee without the involvement of any enforcement authorities. For the purpose of this act, financial collateral will include cash deposits, financial instruments (shares, bonds, etc.) and debt receivables, but will not include, for instance, real estate.

7.5 Do restrictions apply to foreign lenders in the event of (a) filing suit against a company in your jurisdiction, or (b) foreclosure on collateral security?

A foreign plaintiff may be required to provide collateral for its potential liability for legal costs. No such requirement applies for foreclosure of collateral security.

7.6 Do the bankruptcy, reorganisation or similar laws in your jurisdiction provide for any kind of moratorium on enforcement of lender claims? If so, does the moratorium apply to the enforcement of collateral security?

The Norwegian Bankruptcy Act has the concept of a moratorium, but it is not widely used in complicated debt structures. A moratorium will not affect the security of creditors, to the extent the claim is covered by the estimated value of the collateral, which value is set by the debt committee responsible for the moratorium. The secured creditor can challenge the valuation through the courts. When a moratorium is present, a secured creditor cannot commence separate enforcement proceedings against the debtor, save for enforcement pursuant to the Financial Collateral Act (see question 7.4 above).

7.7 Will the courts in your jurisdiction recognise and enforce an arbitral award given against the company without re-examination of the merits?

Yes, an arbitral award granted pursuant to the rules of the Norwegian Arbitration Act of 14 May 2004 will be recognised and enforced against a company without re-examination of the merits. The same applies for foreign arbitral awards which pursuant to the New York Convention on Recognition and Enforcement of Foreign Arbitral Awards can be enforced without re-examination of the merits.

8 Bankruptcy Proceedings

8.1 How does a bankruptcy proceeding in respect of a company affect the ability of a lender to enforce its rights as a secured party over the collateral security?

A secured lender cannot enforce its rights to any collateral for as long as bankruptcy proceedings are ongoing, as the bankruptcy estate has the sole right to realise assets of the company. This does not apply to collateral which has been established pursuant to the rules of the Financial Collateral Act, see question 7.4 above, where the secured lender can seize the asset directly from the pledgor and where the pledgor is subject to bankruptcy proceedings. The bankruptcy estate may choose to transfer the collateral to the pledgee if it can be assumed that the claim of the pledgee exceeds the value of the collateral. The bankruptcy estate will then set a value of the collateral by which the pledgee's claim will be reduced.

8.2 Are there any preference periods, clawback rights or other preferential creditors' rights (e.g., tax debts, employees' claims) with respect to the security?

The bankruptcy estate can use clawback in certain cases where security has been granted during relevant hardening periods that are not expired at the time bankruptcy proceedings are opened. Hardening periods apply where security is granted for a debt which was incurred before security was provided (in which case the hardening period is three months), irrespective of whether the preferred creditor was in good faith or not. A less practical hardening period applies for security where the pledgee has acted in bad faith and contributed to the weakening of the financial position of the debtor (in which case the hardening period can be up to 10 years).

Certain creditors have preferential rights in a bankruptcy situation, but these are only preferred over other unsecured claims, and do not affect collateral security. However, the bankruptcy estate has a preferred security right in any assets which are subject to collateral, limited to 5% of the value of each of the collateral assets, but not to exceed 700 times the court fee (currently totalling NOK 791,000). Proceeds realised from this security may only be used to cover any necessary costs associated with the bankruptcy estate.

8.3 Are there any entities that are excluded from bankruptcy proceedings and, if so, what is the applicable legislation?

Norwegian banks, credit institutions, insurance companies and pension companies are, according to the Norwegian Financial Institutions Act of 10 April 2015 (the "**Financial Institutions Act**"), excluded from bankruptcy proceedings. Instead, these institutions will be taken under public administration, with a view to ensuring a sufficient financial basis for the continued operation of the institution, a sale of whole or parts of the institution to another similar institution, or its liquidation.

Norwegian municipalities (Nw*: kommuner, fylkeskommuner*) are, according to the Norwegian Municipalities Act of 25 September 1992, excluded from bankruptcy proceedings. Instead, the municipality may be taken under public administration until the financial status is sufficiently sound for control to be handed back to the local authorities.

8.4 Are there any processes other than court proceedings that are available to a creditor to seize the assets of a company in an enforcement?

As mentioned under question 7.4 above, security established pursuant to the Norwegian Financial Collateral Act can be enforced outside of court in such manner as the parties have agreed.

9 Jurisdiction and Waiver of Immunity

9.1 Is a party's submission to a foreign jurisdiction legally binding and enforceable under the laws of your jurisdiction?

Yes, the submission by a Norwegian company to a foreign jurisdiction will generally be legally binding and enforceable under Norwegian law. Exceptions can be found in consumer protection legislation, in which case the submission to a jurisdiction other than Norway may be set aside by Norwegian courts.

9.2 Is a party's waiver of sovereign immunity legally binding and enforceable under the laws of your jurisdiction?

If a foreign party has waived its sovereign immunity, the waiver of such will be binding on Norwegian courts to the extent such waiver is permitted and enforceable pursuant to the laws of the relevant party's jurisdiction, and pursuant to international law.

10 Licensing

10.1 What are the licensing and other eligibility requirements in your jurisdiction for lenders to a company in your jurisdiction, if any? Are these licensing and eligibility requirements different for a "foreign" lender (i.e. a lender that is not located in your jurisdiction)? In connection with any such requirements, is a distinction made under the laws of your jurisdiction between a lender that is a bank *versus* a lender that is a non-bank? If there are such requirements in your jurisdiction, what are the consequences for a lender that has not satisfied such requirements but has nonetheless made a loan to a company in your jurisdiction? What are the licensing and other eligibility requirements in your jurisdiction for an agent under a syndicated facility for lenders to a company in your jurisdiction?

Lending is a licensed activity in Norway, and may not be undertaken unless the lender holds a licence as a bank, credit institution or finance institution. An exception applies for lending done on a non-recurring basis. Although the scope of this exception is unclear, it is narrow, and anything more than one loan may require a licence.

Lenders incorporated in Norway will need to fulfil certain requirements set out in the Norwegian Financial Institutions Act in order to obtain a licence. These requirements relate to capitalisation, ownership, management/operation, etc., and the lender will be subject to supervision by the Norwegian Financial Supervisory Authority. Lenders holding a relevant licence in another EU/EEC state, may provide lending services in Norway on the basis of their home country licence, and be subject to supervision by their local financial supervisory authority. Foreign lenders outside of the EU/EEC may provide lending services in Norway provided that they obtain an authorisation (as opposed to a full licence) from the Norwegian financial authorities. The authorisation will permit for the same activities that the entity performs in its home state, and is granted on the condition that the company is subject to satisfactory supervision in their home state, and that such foreign supervisory authority cooperates with Norwegian financial authorities. There are also certain other formal requirements that needs to be complied with.

An institution providing lending services without the sufficient licence or authorisation, may be liable for fines, or, in certain serious circumstances, persons associated with the institution may risk imprisonment of up to one year.

There is no licence requirement for acting as agent under a syndicated facility, unless the agent also performs other services in relation to that syndicate (lending, payment services, etc.) which are licensed.

11 Other Matters

11.1 Are there any other material considerations which should be taken into account by lenders when participating in financings in your jurisdiction?

No, there are not.

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Ragnhild Steigberg is a finance lawyer with extensive experience with bank loans and bond issues. She assists lenders, borrowers and arrangers in bilateral and syndicated facilities and bond issues with a main focus on real estate financing, shipping/offshore and acquisition financing. Ragnhild also has extensive experience with complicated debt restructurings and insolvency matters, and advises financial institutions on regulatory matters.

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Chapter 62

Pakistan

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Zara Tariq

1 Overview

1.1 What are the main trends/significant developments in the lending markets in your jurisdiction?

Pakistan's lending market is diverse and includes lending by foreign and local banks/financial institutions; depending on the requirements of the lending institution, such lending ranges from conventional financing to Islamic financing. Recently, due to the entry by the Government of Pakistan and the Government of China, into the Agreement on the China-Pakistan Economic Corridor, various Chinese banks/financial institutions have agreed to provide finance to, *inter alia*, infrastructure-related projects. Further, we understand that the State of Pakistan (the "**SBP**") has intimated to local banks that any power project with a foreign element has to obtain a portion of its financing from a foreign entity.

1.2 What are some significant lending transactions that have taken place in your jurisdiction in recent years?

In recent years, a number of Chinese banks/financial institutions have provided finance to power projects, such as the Suki Kinari and Karot hydropower projects, the UEP wind power project, the Quaid-e-Azam solar power project and coal-based mine and power projects. In addition, lending has also been provided to local businesses by international financial institutions including International Finance Corporation, Overseas Private Investment Corporation and *Agence Française de Développement*.

2 Guarantees

2.1 Can a company guarantee borrowings of one or more other members of its corporate group (see below for questions relating to fraudulent transfer/financial assistance)?

Yes; however, Section 199(1) of the Companies Act, 2017 (the "**Act**") requires a special resolution (a resolution made by at least three-fourths of the members of a company) for a company to make any "investment", i.e. loans and guarantees, in any of its associated companies. Such special resolution shall indicate the nature, period, amount of investment and terms and conditions thereto. The Act defines "associated companies" as including two or more companies which are under common management/control or a subsidiary of another.

2.2 Are there enforceability or other concerns (such as director liability) if only a disproportionately small (or no) benefit to the guaranteeing/securing company can be shown?

Section 199(2) of the Act provides, *inter alia*, that return on any investment made by a company in an associated company shall not be less than the borrowing cost of the investing company and shall be recovered on a regular basis in accordance with the terms of the agreement, failing which the directors shall be personally liable to make the payment.

2.3 Is lack of corporate power an issue?

Yes. Unless the constitutional documents of a company provide otherwise, in order for a company to issue a guarantee, it must have the requisite corporate power to do so; the absence of which may render such an action void or the document unenforceable.

2.4 Are any governmental or other consents or filings, or other formalities (such as shareholder approval), required?

Yes. See question 2.1.

2.5 Are net worth, solvency or similar limitations imposed on the amount of a guarantee?

See question 2.2 above. Further, Section 199(4) of the Act provides that a special resolution will be required for an increase in the amount or any change in the nature of investment or terms and conditions thereto.

Further, Regulation R-7 of the Prudential Regulations issued by the SBP states that all guarantees issued by banks/development financial institutions shall be fully secured except in particular cases, including bid bonds issued for consultancy firms/contractors of goods and services and issuance of performance bonds and guarantees for local construction companies/contractors where the limit may be waived up to 50%, provided that the bank/development financial institution holds at least 20% of the guaranteed amount in the form of liquid assets as security.

2.6 Are there any exchange control or similar obstacles to enforcement of a guarantee?

See questions 2.2 and 2.5.

3 Collateral Security

3.1 What types of collateral are available to secure lending obligations?

The most common forms of collateral available to secure lending obligations are: (i) assignment of rights and interests under project documents and in respect of movable property (including receivables and insurance proceeds); (ii) charge over accounts and deposits therein; (iii) mortgage over immovable property; (iv) hypothecation and charge over movable property; and (v) pledge of shares.

3.2 Is it possible to give asset security by means of a general security agreement or is an agreement required in relation to each type of asset? Briefly, what is the procedure?

Yes, it is possible to give asset security under a general security agreement; however, certain types of security (such as security over immovable property) are usually carved out of the general security agreement and granted under specific security agreements (governed by Pakistan law or otherwise) due to reasons of registration, stamp duty, location of the asset, governing law of the underlying contracts, etc.

If the security created by a company is such that it is compulsorily registrable under Section 100 of the Act, then particulars of such security (along with the necessary documents) have to be filed with the Security and Exchange Commission of Pakistan within 30 days of creation of security.

3.3 Can collateral security be taken over real property (land), plant, machinery and equipment? Briefly, what is the procedure?

Yes, security can be created over real property (land) pursuant to a registered mortgage (wherein a mortgage deed is entered into between the parties, which is registered with the land registrar) or an equitable mortgage (wherein the original title deeds relating to the land are deposited with the trustee/lender and evidenced by a memorandum of deposit of title deeds).

Security over plant, machinery and equipment is usually created pursuant to a letter of hypothecation, wherein a fixed charge is created over the present and future tangible fixed assets of the company and a floating charge is created over, *inter alia*, present and future undertakings and current assets of the company.

See also question 3.2 for the requirement to register particulars of security.

3.4 Can collateral security be taken over receivables? Briefly, what is the procedure? Are debtors required to be notified of the security?

Yes, security can be created over receivables, usually pursuant to a general security agreement (described in question 3.2). See also question 3.2 for the requirement to register particulars of security.

As the debtor typically creates security, it will have notice of the same.

3.5 Can collateral security be taken over cash deposited in bank accounts? Briefly, what is the procedure?

Yes, security can be taken over cash deposited in bank accounts by virtue of a charge over the accounts and deposits therein.

Also see question 3.2 for the requirement to register particulars of security.

3.6 Can collateral security be taken over shares in companies incorporated in your jurisdiction? Are the shares in certificated form? Can such security validly be granted under a New York or English law governed document? Briefly, what is the procedure?

Yes, security can be created in respect of shares of a company incorporated in Pakistan; in the case of physical/certificated shares, the shareholders of the company deposit original share certificates and blank transfer deeds with the trustee/lender with the intent to create a pledge thereon, and in the case of scripless shares (recorded and maintained with the Central Depository Company), the procedure stipulated by the Central Depository Company and under applicable law in respect of a pledge of shares shall be complied with. The terms on which a pledge of shares is created and held, can be validly recorded under a New York or English law-governed document, although it is common for a Pakistan law-governed share pledge agreement to be entered into, as ultimately enforcement would occur in the courts of Pakistan.

See also question 3.2 for the requirement to register particulars of security.

3.7 Can security be taken over inventory? Briefly, what is the procedure?

Yes, security can be taken over inventory pursuant to a floating charge, the terms whereof are stated in a general security agreement or a letter of hypothecation.

See also question 3.2 for the requirement to register particulars of security.

3.8 Can a company grant a security interest in order to secure its obligations (i) as a borrower under a credit facility, and (ii) as a guarantor of the obligations of other borrowers and/or guarantors of obligations under a credit facility (see below for questions relating to the giving of guarantees and financial assistance)?

Yes; however, with regard to (ii), the responses to questions 2.1 and 2.2 should be noted.

3.9 What are the notarisation, registration, stamp duty and other fees (whether related to property value or otherwise) in relation to security over different types of assets?

Stamp duty in Pakistan is a provincial subject and the rates of stamp duty vary from jurisdiction to jurisdiction. The relevant nexus for the attraction of stamp duty under Pakistan law is the place of execution of an instrument, rather than the jurisdiction of incorporation of a party to an agreement. Pursuant to the Stamp Act, 1899 (the "**Stamp Act**"), in certain provinces, the stamp duty applicable to finance documents pertaining to interest-based financing is *ad valorem*; therefore, in such cases, finance documents are executed and retained outside Pakistan. In other provinces where stamp duty is not *ad valorem*, finance documents are executed at the rate of stamp duty set out in the schedule to the Stamp Act as applicable in the province in which such instrument is executed.

See also question 3.13.

With respect to registration, Section 17 of the Registration Act, 1908, sets out instruments which relate to property and are compulsorily registrable with the relevant registrar. The fees for registration of such instruments are stipulated in the registration table prepared by the Government.

3.10 Do the filing, notification or registration requirements in relation to security over different types of assets involve a significant amount of time or expense?

Filings, notification and registration in Pakistan do not involve a considerable amount of time, as the time within which security over different types of assets has to be filed, registered and perfected is stipulated under applicable law, and hence has to be complied with. However, where registration pertaining to land is concerned, the process can be time-consuming and cumbersome.

In relation to expenses, see question 3.9.

3.11 Are any regulatory or similar consents required with respect to the creation of security?

If land is procured under the Land Acquisition Act, 1984, a consent may have to be procured under Section 43-A, wherein the approval of the Provincial Government is required for any transfer of land (by way of sale, mortgage, gift, lease or otherwise) acquired under the aforesaid Act. Further, whether any other consents relating to security over land are required may vary depending on the land documents.

In order to create pledge or hypothecation over securities in favour of a non-resident, special permission of the SBP has to be procured prior to such security being created.

3.12 If the borrowings to be secured are under a revolving credit facility, are there any special priority or other concerns?

In addition to any requirements of the bank/financial institution providing the revolving credit facility, the Prudential Regulations for Consumer Financing stipulate that, in the case of revolving finance, "at least 15% of the maximum utilisation of the loan during the year should be cleaned up by the borrower for a minimum period of one week", failing which the loan will be appropriately classified. However, banks/DFIs who require customers to repay a minimum amount each month, will be considered to be in compliance with the foregoing condition, subject to the condition that the aggregate monthly instalments exceed 15% of the clean-up requirement.

Furthermore, the Prudential Regulations for Agriculture Financing specify certain restrictions regarding adjustment and segregation of loans under a revolving credit facility.

With reference to small and medium enterprises, the Prudential Regulations relating thereto provide that banks/DFIs will obtain a declaration from small enterprises, confirming that the loan proceeds have been utilised for the purpose stipulated by it when applying for the loan.

Further, revolving letters of credit relating to imports require approval of the SBP.

3.13 Are there particular documentary or execution requirements (notarisation, execution under power of attorney, counterparts, deeds)?

Article 17(2) of the Qanun-e-Shahadat Order, 1984, states that: "*In matters pertaining to financial or future obligations, if reduced to writing, the instrument shall be attested by two men, or one man and two women, so that one may remind the other, if necessary, and evidence shall be led accordingly*"; hence, every document that relates to financial or future obligations has to be witnessed in the manner set out above. If a document is executed in counterparts, then every signature of a party to a document should be witnessed as above.

Section 17 of the Stamp Act provides that all instruments chargeable with duty and executed by any person in Pakistan must be stamped before or at the time of execution. If an instrument chargeable with duty is executed out of Pakistan, and relates to any property situate in Pakistan or to any matter or thing done or to be done in Pakistan and is received in Pakistan, it must be stamped within three (3) months after it has first been received in Pakistan.

There is, however, an exception created under Section 18(4) of the Financial Institutions (Recovery of Finances) Ordinance, 2001 (the "**FIO**") (the FIO applies to all financial institutions based in Pakistan and/or outside Pakistan lending to Pakistani companies or individuals), enabling financial institutions to enforce documents where stamping or witnessing of such documents is deficient.

With respect to notarisation, power of attorney is required to be notarised and/or consularised by the relevant person, once it is executed.

4 Financial Assistance

4.1 Are there prohibitions or restrictions on the ability of a company to guarantee and/or give security to support borrowings incurred to finance or refinance the direct or indirect acquisition of: (a) shares of the company; (b) shares of any company which directly or indirectly owns shares in the company; or (c) shares in a sister subsidiary?

(a) Yes. Section 86(1) of the Act provides that only a listed company has the power to buy its own shares.

(b) Yes. Section 86(2) of the Act states that no public company or a private company being a subsidiary of a public company shall give financial assistance, whether directly or indirectly, for the purpose of, or in connection with, a purchase or subscription made or to be made by any person of any shares in the company or its holding company.

(c) Yes. See the response to (b) above.

5 Syndicated Lending/Agency/Trustee/Transfers

5.1 Will your jurisdiction recognise the role of an agent or trustee and allow the agent or trustee (rather than each lender acting separately) to enforce the loan documentation and collateral security and to apply the proceeds from the collateral to the claims of all the lenders?

Yes. In the event of a default, the trustee/agent has the option to enforce security by exercising its rights under the security documents without court intervention (see (i) below) or filing recovery proceedings under the FIO (see (ii) below) or filing summary proceedings under the Civil Procedure Code, 1908 (the "**Code**") (see (iii) below).

(i) Enforcement under the security documents: A trustee/agent may, on behalf of the lenders, enforce the security by exercising the power of sale (or power of attorney) granted to it under the security documents, without instituting legal proceedings; however, it is often the case that the company will be able to obtain an injunction against such sale, on one pretext or another; therefore, in practice, initiating court proceedings is the preferred (and often the only) method of enforcement.

(ii) Applicability of the FIO: Under the FIO, proceedings may be brought by a "financial institution" against a "customer". Under Section 9(1) of the FIO, a financial institution may institute a suit in the banking court by "*presenting a plaint which shall be verified on oath by a Branch Manager or such other officer of the financial institution as may be duly authorised in this behalf by power of attorney or otherwise*".

Section 2(a) of the FIO defines a "customer" as "*a person to whom finance has been extended by a financial institution and includes a person on whose behalf a guarantee or letter of credit has been issued by a financial institution as well as a surety or an indemnifier*" and a "financial institution" as: "*(i) any company whether incorporated within or outside Pakistan which transacts the business of banking or any associated or ancillary business in Pakistan through its branches within or outside Pakistan...*". While the FIO does not define the "business of banking", section 7 of the Banking Companies Ordinance, 1962 sets out various forms of business in which banking companies may engage; therefore as long as the trustee/agent are engaged in the activities described in section 7, i.e. are conducting business which is ancillary to or associated with the business of banking in Pakistan, they are likely to be considered financial institutions under the FIO.

(iii) Summary procedure under the Code: The agent/lenders can institute summary proceedings under Order XXXVII of the Code.

5.2 If an agent or trustee is not recognised in your jurisdiction, is an alternative mechanism available to achieve the effect referred to above which would allow one party to enforce claims on behalf of all the lenders so that individual lenders do not need to enforce their security separately?

This is not applicable in Pakistan.

5.3 Assume a loan is made to a company organised under the laws of your jurisdiction and guaranteed by a guarantor organised under the laws of your jurisdiction. If such loan is transferred by Lender A to Lender B, are there any special requirements necessary to make the loan and guarantee enforceable by Lender B?

Depending on the circumstances of the case, prior approval of the SBP may be required to grant any loans or overdrafts in foreign currencies, pursuant to paragraph 20 of Chapter XIX of the FEM. Additionally, paragraph 11 of Chapter XIX of the FEM, stipulates that foreign currency private loan agreements are required to be registered with the SBP through the authorised dealer within 30 days from the date of the agreement.

Prior approval of the SBP is also required if loans registered with the SBP are transferred and the new loan agreement must be registered with the SBP. If a loan agreement has not been registered with the SBP (usually in the case of local loans), then intimation/registration to the SBP is not necessary.

6 Withholding, Stamp and Other Taxes; Notarial and Other Costs

6.1 Are there any requirements to deduct or withhold tax from (a) interest payable on loans made to domestic or foreign lenders, or (b) the proceeds of a claim under a guarantee or the proceeds of enforcing security?

The Income Tax Ordinance, 2001 (the "**ITO**") prescribes that tax must be payable by lenders (local or foreign), unless specifically exempted, in respect of interest and fees. No tax is payable on enforcement proceeds in Pakistan.

6.2 What tax incentives or other incentives are provided preferentially to foreign lenders? What taxes apply to foreign lenders with respect to their loans, mortgages or other security documents, either for the purposes of effectiveness or registration?

The tax incentives provided to foreign lenders include: (i) inter-governmental treaties, such as agreements for avoidance of double taxation and prevention of fiscal evasion, entered into between Pakistan and other countries; (ii) specific statutes that recognise and provide benefits (including tax benefits) to financial institutions such as International Finance Corporation and Asian Development Bank, pursuant to the International Finance Act, 1956 and the Asian Development Bank Ordinance, 1971, respectively; and (iii) Part 1 of the Second Schedule of the ITO wherein, *inter alia*, any income derived from the institutions stated thereunder is exempt from income tax in Pakistan.

See questions 3.9 and 3.13 with respect to other fees (including stamp tax).

6.3 Will any income of a foreign lender become taxable in your jurisdiction solely because of a loan to or guarantee and/or grant of security from a company in your jurisdiction?

Yes. Unless specifically exempted under statute or otherwise, section 152(2) of the ITO (read with Division II, Part III of the First

Schedule of the ITO) shall apply, which provides that any person paying an amount to a non-resident person shall deduct tax at the rate of 20% from the gross amount paid. Section 81 of the ITO defines a "non-resident person" as a person who is not a resident of Pakistan for that tax year.

6.4 Will there be any other significant costs which would be incurred by foreign lenders in the grant of such loan/guarantee/security, such as notarial fees, etc.?

No; it is a commercial decision to be taken by the parties as to whom should bear costs arising in a transaction. Security documents, however, may attract *ad valorem* stamp duty, and usually such liability would be on the borrower, notwithstanding that the security documents may be executed outside Pakistan without payment of stamp duty.

6.5 Are there any adverse consequences to a company that is a borrower (such as under thin capitalisation principles) if some or all of the lenders are organised under the laws of a jurisdiction other than your own? Please disregard withholding tax concerns for purposes of this question.

No, there are no such adverse consequences.

7 Judicial Enforcement

7.1 Will the courts in your jurisdiction recognise a governing law in a contract that is the law of another jurisdiction (a "foreign governing law")? Will courts in your jurisdiction enforce a contract that has a foreign governing law?

Yes, a foreign governing law clause in a contract will be valid under Pakistan law and will be recognised and given effect to by the courts in Pakistan, but only to the extent that such law is proved to the satisfaction of the court, which satisfaction is within the discretion of the court and not considered contrary to the public policy of Pakistan.

7.2 Will the courts in your jurisdiction recognise and enforce a judgment given against a company in New York courts or English courts (a "foreign judgment") without re-examination of the merits of the case?

A money judgment obtained in the High Court of Justice in England (not being a sum payable in respect of taxes or other charges of a like nature or in respect of a fine or other penalty) will be recognised and enforced under Section 44A of the Code as if it were a decree of a District Court in Pakistan, without re-examination of issues of fact.

Section 13 of the Code provides that any judgment for a sum of money obtained in a foreign court with concurrent jurisdiction is conclusive as to any matters thereby adjudicated between the parties to such judgment unless:

(a) it has not been pronounced by a court of competent jurisdiction;

(b) it has not been given on the merits of the case;

(c) it appears on the face of the proceedings to be founded on an incorrect view of International Law or a refusal to recognise the law of Pakistan in cases in which such law is applicable;

(d) the proceedings in which the judgment was obtained are opposed to natural justice;

(e) it has been obtained by fraud; or

(f) it sustains a claim founded on a breach of any law in force in Pakistan.

A foreign judgment obtained in a foreign court (other than a judgment obtained in the English Courts as set out above) will be enforceable in Pakistan by bringing a separate suit on the basis of the foreign judgment as a cause of action and execution may only take place once a Pakistani judgment has been obtained on such a suit.

7.3 Assuming a company is in payment default under a loan agreement or a guarantee agreement and has no legal defence to payment, approximately how long would it take for a foreign lender to (a) assuming the answer to question 7.1 is yes, file a suit against the company in a court in your jurisdiction, obtain a judgment, and enforce the judgment against the assets of the company, and (b) assuming the answer to question 7.2 is yes, enforce a foreign judgment in a court in your jurisdiction against the assets of the company?

(a) It would take approximately five to 10 years for a foreign lender to file a suit against the company in the courts of Pakistan, obtain a judgment and enforce the same. However, this period could increase if counsel for the company adopts dilatory tactics.

(b) It would take approximately a year to enforce a foreign judgment obtained in the English courts and approximately five to 10 years to enforce a foreign judgment if it is a judgment of any other court. If enforcement proceedings are instituted under the FIO, the period may be reduced to no more than eight years, since the FIO permits enforcement under summary procedure.

7.4 With respect to enforcing collateral security, are there any significant restrictions which may impact the timing and value of enforcement, such as (a) a requirement for a public auction, or (b) regulatory consents?

Under the FIO and the Code, there is a requirement for a public auction with respect to collateral security. Regulatory consents are usually obtained prior to security being created in order to ensure that, at the time of enforcement of security, no further approvals are required.

7.5 Do restrictions apply to foreign lenders in the event of (a) filing suit against a company in your jurisdiction, or (b) foreclosure on collateral security?

No restrictions apply.

7.6 Do the bankruptcy, reorganisation or similar laws in your jurisdiction provide for any kind of moratorium on enforcement of lender claims? If so, does the moratorium apply to the enforcement of collateral security?

There are no provisions for moratoriums on enforcement of lender claims in Pakistan.

7.7 Will the courts in your jurisdiction recognise and enforce an arbitral award given against the company without re-examination of the merits?

Yes. An arbitral award obtained against the company would be enforceable by the courts in Pakistan, without re-litigation of the matters thereby adjudicated, in accordance with the Recognition and Enforcement (Arbitration Agreements and Foreign Arbitral Awards) Act, 2011.

8 Bankruptcy Proceedings

8.1 How does a bankruptcy proceeding in respect of a company affect the ability of a lender to enforce its rights as a secured party over the collateral security?

Section 389 of the Act states that, in the case of a winding up of an insolvent company, the same rules shall prevail and be observed with regard to the rights of secured and unsecured creditors and to debts provable, as are in force for the time being under the law of insolvency with respect to the estates of persons adjudged insolvent.

A secured creditor is defined under the Provincial Insolvency Act, 1920 as "*a person holding a mortgage, charge or lien on the property of the debtor or any part thereof as a security for a debt due to him from the debtor*". A secured creditor is, therefore, free to deal with and realise its security for the repayment of the debt. The protection afforded to secured creditors in winding up proceedings is elaborated in *United Bank Limited v PICIC* (1992 SCMR 1731), wherein it was held that the scheme of the Act is such that a secured creditor cannot claim any preferential treatment in distribution of the assets of the insolvent and instead has an independent right to realise or relinquish the security.

Therefore, a secured creditor is not a part of the category of unsecured creditors and would be entitled to enforce the security created in its favour, separately and independently of any insolvency proceedings.

8.2 Are there any preference periods, clawback rights or other preferential creditors' rights (e.g., tax debts, employees' claims) with respect to the security?

Section 61 of Provincial Insolvency Act, 1920 specifies that all debts due to the Government or to any local authority will have priority over other debts upon distribution of the property of the insolvent. A similar provision is present under Section 390 of the Act, pursuant to which, in the event of winding up, priority has been given to the revenue, taxes, cesses and rates due from a company to the Federal or Provincial Government or a local authority, and specified payments to be made to employees and workers of a company.

Under Section 391 of the Act, every transfer made after the commencement of winding up shall be void. Transfers made one year prior to the presentation of the winding up shall be void if the transfer is not in the ordinary course of business or in favour of a purchaser or encumbrancer in good faith and for valuable consideration.

8.3 Are there any entities that are excluded from bankruptcy proceedings and, if so, what is the applicable legislation?

Certain statutory corporations are excluded from bankruptcy proceedings, e.g. no provision of law related to the winding up of companies and corporations was applicable to the Pakistan International Airlines Corporation prior to it being converted into a public limited company, and such entity could not be wound up, save by order of the Federal Government.

8.4 Are there any processes other than court proceedings that are available to a creditor to seize the assets of a company in an enforcement?

Under Section 15 of the FIO (as amended by the Financial Institutions (Recovery of Finances) Amendment Act, 2016), a financial institution may, without the intervention of any court, sell mortgaged property or any part thereof by public auction and appropriate the proceeds thereof.

9 Jurisdiction and Waiver of Immunity

9.1 Is a party's submission to a foreign jurisdiction legally binding and enforceable under the laws of your jurisdiction?

Yes, a party's submission to a foreign jurisdiction is legally binding and enforceable.

9.2 Is a party's waiver of sovereign immunity legally binding and enforceable under the laws of your jurisdiction?

Yes, a party's waiver of sovereign immunity is legally binding and enforceable.

10 Licensing

10.1 What are the licensing and other eligibility requirements in your jurisdiction for lenders to a company in your jurisdiction, if any? Are these licensing and eligibility requirements different for a "foreign" lender (i.e. a lender that is not located in your jurisdiction)? In connection with any such requirements, is a distinction made under the laws of your jurisdiction between a lender that is a bank *versus* a lender that is a non-bank? If there are such requirements in your jurisdiction, what are the consequences for a lender that has not satisfied such requirements but has nonetheless made a loan to a company in your jurisdiction? What are the licensing and other eligibility requirements in your jurisdiction for an agent under a syndicated facility for lenders to a company in your jurisdiction?

There are no licensing requirements for lending from a company or a private individual.

If the lender is a local bank or a non-banking finance company ("NBFC"), such entities must be licensed by the SBP or the Securities and Exchange Commission of Pakistan, respectively. A distinction is created under applicable law between a bank and a NBFC. A banking company is a company carrying on the business of banking; the term "banking" has been defined in the Banking Companies Ordinance, 1962 as "*accepting, for the purpose of lending or investment, of deposits of money from the public, repayable on demand or otherwise, and withdrawable by cheque, draft, order or otherwise*". An NBFC is defined under the Non-Banking Finance Companies (Establishment and Regulation) Rules, 2003 as a non-banking finance company carrying out any one or more forms of business, including, *inter alia*, Investment Finance Services, and Asset Management Services.

If a local lender is engaged in the business of banking or is carrying on a form of business which may be categorised as a business carried out by a NBFC and it has not been licensed, then the company and its representatives/employees may be subject to a fine and/or imprisonment.

There are no eligibility requirements for an agent under a syndicated facility, as long as it does not carry on any banking business (for which it requires a licence).

The SBP has prohibited borrowing from abroad without its previous general or special permission and has given general permission to private sector entrepreneurs to obtain foreign currency loans from, *inter alia*, banks/financial institutions abroad and from parent companies of multinationals. A foreign lender lending to a local entity without such permission risks not being repaid by the company.

11 Other Matters

11.1 Are there any other material considerations which should be taken into account by lenders when participating in financings in your jurisdiction?

A material consideration when participating in financings relating to power projects in Pakistan is the issue of circular debt, i.e. it is often the case that the power purchaser is unable to make payments to the power generation companies due to non-payment by the distribution companies (the distribution companies being unable to make payments due to non-payment by consumers). Ultimately, this cycle of non-payment impacts repayments to the lenders of a project; however, to a certain extent this risk is mitigated by the Government of Pakistan providing an indemnity and a sovereign guarantee to the company.

A foreign lender must be aware that foreign exchange laws in Pakistan regulate the remittance of foreign currency outside Pakistan and, as such, repayment of foreign loans will require approval of the SBP, which may cause delays and therefore must be taken into consideration when anticipating a timeline for repayment.

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Kabraji & Talibuddin Advocates and Legal Counsellors

Kabraji & Talibuddin was formed in 1997 by the two name partners, who have between them over 60 years of legal experience in Pakistan and elsewhere. Kairas Kabraji is recognised as one of the country's leading corporate and commercial lawyers and Salman Talibuddin is a leading member of the Karachi Bar and has acted in major international commercial arbitrations and presently holds the position of Additional Attorney General for Pakistan at Karachi. Between 2012 and 2017, Danish Shah, Syed Ali Bin Maaz and Maheen Faruqui were admitted to the partnership.

The firm undertakes all forms of corporate and commercial work, focusing on project financing in the private sector, aircraft leasing, banking and finance and mergers and acquisitions. The firm's portfolio of clients includes foreign and local banks, multinationals, financial institutions and individuals, to whom advice and assistance is provided on all contentious and non-contentious matters, both domestic and trans-border.

Portugal

PLMJ

Gonçalo dos Reis Martins

1 Overview

1.1 What are the main trends/significant developments in the lending markets in your jurisdiction?

Further to the successful exit of the financial assistance programme in 2014, the Portuguese economy has been growing at an increasing pace. Such growth has fuelled a significant rise in unsecured consumer lending, as well as large-scale property finance transactions. The increase in the M&A industry has also led to an increase in acquisition finance.

1.2 What are some significant lending transactions that have taken place in your jurisdiction in recent years?

The landmark lending transactions in 2017 have been: (i) the EUR 350 million loan to Bridgepoint for financing of the acquisition of Portuguese-based SAPEC group; and (ii) the EUR 250 million bridge loan to REN – Redes Energéticas Nacionais, SGPS, S.A. for the acquisition of EDP Gás, SGPS, S.A.

2 Guarantees

2.1 Can a company guarantee borrowings of one or more other members of its corporate group (see below for questions relating to fraudulent transfer/financial assistance)?

As a general rule, the corporate powers of a company are restricted to those rights and obligations which are necessary or convenient for accomplishing the purpose of the company (which, generally, is to make a profit).

In accordance with Article 6(3) of the Portuguese Companies Code, there is a legal presumption that the granting of guarantees in respect of obligations of other entities is contrary to the purpose of companies, unless there is a justifiable self-interest of the company in providing the guarantee or the company in question is in a group or controlling relationship with such entity.

Such justifiable self-interest of the company is evident in the provision of downstream guarantees, but is less evident in the provision of upstream and cross-stream guarantees. In the case of upstream and cross-stream guarantees it is advisable for the relevant resolutions to be passed justifying the self-interest of the company, which may be an indirect one, in providing the guarantee.

2.2 Are there enforceability or other concerns (such as director liability) if only a disproportionately small (or no) benefit to the guaranteeing/securing company can be shown?

In such situations, it is likely that there is no justifiable self-interest to the company in providing the guarantee/security and unless the company is in a group or controlling relationship with the entity whose obligations it guarantees/secures, the provision of the guarantee/security may be considered to be null and void.

Furthermore, in the absence of benefit or the existence of only a disproportionately small benefit to the company, the provision of the guarantee/security may be terminated in the context of an insolvency proceeding relating to the company if the guarantee/security is provided during the 12-month period prior to the declaration of insolvency.

The provision of the guarantee or security with disproportionately small (or no) benefit to the company may give rise to the breach of duties of directors towards the company and, therefore, liability.

2.3 Is lack of corporate power an issue?

Yes, please see question 2.1 above.

2.4 Are any governmental or other consents or filings, or other formalities (such as shareholder approval), required?

Except for certain state-owned and other public sector companies, unless there is a restriction contained in the articles of association of the company, in principle, no governmental approvals, consents, filings or other formalities are required by law, for a guarantee provided by a Portuguese company to be enforceable.

However, it is common practice for there to be a requirement for either shareholder approval or board approval for the granting of the guarantee. Usually, such approval will contain an express reference to the benefit to the company from the provision of the guarantee (even if such benefit is an indirect one) or to the controlling or group relationship (if any) with the entity benefiting from the provision of the guarantee.

2.5 Are net worth, solvency or similar limitations imposed on the amount of a guarantee?

No, but please see question 2.2 above as to corporate benefit.

2.6 Are there any exchange control or similar obstacles to enforcement of a guarantee?

No exchange controls or other obstacles exist in Portugal regarding the enforcement of a guarantee.

3 Collateral Security

3.1 What types of collateral are available to secure lending obligations?

There are various types of collateral available to secure lending obligations, such as:

(i) mortgage over real estate property, aircrafts, vessels, cars and industrial units (e.g. factories);

(ii) pledge over movable assets not referred to in (i) above;

(iii) pledge over a business (including inventory) – only possible if the pledgee is a credit institution;

(iv) pledge of rights (including credits and receivables);

(v) financial pledge – a pledge of cash or securities in favour of a credit institution; and

(vi) escrow of income deriving from real estate, aircrafts, vessels or cars.

3.2 Is it possible to give asset security by means of a general security agreement or is an agreement required in relation to each type of asset? Briefly, what is the procedure?

In accordance with Portuguese law, the provision of generic security (i.e. over the assets of a given entity generically) is considered null and void because of lack of determination of the specific assets that become subject to the security.

It is therefore necessary that a security agreement identifies, to the greatest extent possible, the assets which are subject to the security created by such agreement. At least, the security agreement must contain certain criteria which would allow the identification of the secured assets at a given time.

The use of one single agreement or separate agreements will depend on the type of security being granted, as mortgages and escrow of income must be granted by public deed, whereas the pledges may be granted by means of private agreements.

3.3 Can collateral security be taken over real property (land), plant, machinery and equipment? Briefly, what is the procedure?

Yes, collateral security may be taken over such assets by means of a deed of mortgage.

A mortgage over a plant will include the real estate property and all the machinery and equipment thereof which is identified in a schedule to the deed.

3.4 Can collateral security be taken over receivables? Briefly, what is the procedure? Are debtors required to be notified of the security?

Yes, collateral security by means of a pledge over receivables may be taken. A written agreement is required, as well as notification of the creation of the pledge to the debtors, so that the pledge may be enforced against such persons.

3.5 Can collateral security be taken over cash deposited in bank accounts? Briefly, what is the procedure?

Yes. There are two types of pledge that can be taken over cash deposited in bank accounts: a pledge created under the Portuguese Civil Code; and a financial pledge.

A Portuguese Civil Code pledge is the most common form of pledge. The financial pledge, which may be created if the pledgee is a bank, provides more flexibility to the pledgor upon enforcement.

In any event, formalities include the execution of an agreement and notice to the bank where the cash is deposited (if the custody bank is not the pledgee). The acknowledgment of the pledge by the bank is not required, but is useful so as to ensure swift enforcement.

3.6 Can collateral security be taken over shares in companies incorporated in your jurisdiction? Are the shares in certificated form? Can such security validly be granted under a New York or English law governed document? Briefly, what is the procedure?

Yes, collateral security may be taken over shares in companies incorporated in Portugal as a pledge of shares.

Shares may be either in certificated form or in book-entry form. Yes, provided that any formalities required under Portuguese law for the validity and effectiveness of the pledge are complied with. The procedure will depend on the type of company in question.

If the company is a private limited liability company (*sociedade por quotas*), registration of the pledge over the shares at the Commercial Registry is required.

If the company is a public limited liability company (*sociedade anónima*), a pledge of shares of such type of company requires, if the shares are in certificate form, the annotation of the creation of the pledge on each share certificate and registration of the pledge in the books of the issuer. The creation of the pledge over book-entry shares is made by annotation of the creation of the pledge in the securities account in which the shares are deposited and registration in the books of the issuer.

3.7 Can security be taken over inventory? Briefly, what is the procedure?

Security over inventory is possible if such security is granted in favour of a credit institution. The procedure includes the execution of a written agreement. Upon default or the occurrence of other circumstances as set out in the pledge agreement, it is customary for the pledgee or security agent to give an enforcement notice to the pledgor crystallising the stock. Alternatively, parties may agree in the provision of regular notices detailing the pledged stock.

3.8 Can a company grant a security interest in order to secure its obligations (i) as a borrower under a credit facility, and (ii) as a guarantor of the obligations of other borrowers and/or guarantors of obligations under a credit facility (see below for questions relating to the giving of guarantees and financial assistance)?

Yes, but please see the restrictions on the provision of guarantees in question 2.1 above, which are also applicable in relation to the provision of security interest by companies.

3.9 What are the notarisation, registration, stamp duty and other fees (whether related to property value or otherwise) in relation to security over different types of assets?

The costs for the creation of security are, generally, as follows:

(i) notarial fees (only applicable where the execution of a public deed is required): approximately EUR 280 per deed;

(ii) registration fees: EUR 225 per property asset, if registration is requested by the notary; and

(iii) stamp duty (please see below on the applicability of stamp duty):

(a) 0.04 per cent, per month over the secured amount, in the case of security granted for a period of less than one year;

(b) 0.5 per cent, over the secured amount for security granted for a period of one year or more and less than five years; and

(c) 0.6 per cent, over the secured amount for security granted for a period of five years or more.

3.10 Do the filing, notification or registration requirements in relation to security over different types of assets involve a significant amount of time or expense?

In principle, there should be no timing issues. Filings, notifications and registrations are made in a matter of a few days.

As regards expenses, these can be a considerable amount in the event that stamp duty is due on the granting of guarantees or the creation of security.

3.11 Are any regulatory or similar consents required with respect to the creation of security?

No regulatory or similar consents apply, except for assets held by state-owned entities or shares of concessionaires of public services, which must be assessed on a case-by-case basis.

3.12 If the borrowings to be secured are under a revolving credit facility, are there any special priority or other concerns?

No, there are not. In any case, please note that the creditors benefitting from *in rem security* have a privileged status in accordance with the Portuguese Insolvency Code. The fact that the credit facility is a revolving one does not affect priority or raise other concerns.

3.13 Are there particular documentary or execution requirements (notarisation, execution under power of attorney, counterparts, deeds)?

Yes, the creation of security over real estate requires the execution of a deed, usually made before a notary. In such case, the powers of attorney, if any, must also be granted before a public notary (and bear the apostille of The Hague Convention or legalised in accordance with the relevant rules, if executed outside of Portugal). The execution of a deed in Portugal before a notary requires the parties (whether Portuguese or foreign entities) to have a legal entity and tax identification number. The provision of such number is also required for the registration of a security interest in favour of a given entity.

4 Financial Assistance

4.1 Are there prohibitions or restrictions on the ability of a company to guarantee and/or give security to support borrowings incurred to finance or refinance the direct or indirect acquisition of: (a) shares of the company; (b) shares of any company which directly or indirectly owns shares in the company; or (c) shares in a sister subsidiary?

(a) Shares of the company

Yes, this is expressly forbidden in accordance with Article 322 of the Portuguese Companies Code. Few exceptions are available. The violation of this prohibition may lead to criminal liability of the directors/managers of such company and the agreement, guarantee or security interest may be declared null and void.

(b) Shares of any company which directly or indirectly owns shares in the company

No express prohibition exists, but it is generally understood as applicable. Also, please note that the corporate powers of the company may be restricted in respect of granting of guarantees or security – please see question 2.1 above.

(c) Shares in a sister subsidiary

No express prohibition exists, but please note that the corporate powers of the company may be restricted in respect of granting of guarantees or security – please see question 2.1 above.

5 Syndicated Lending/Agency/Trustee/Transfers

5.1 Will your jurisdiction recognise the role of an agent or trustee and allow the agent or trustee (rather than each lender acting separately) to enforce the loan documentation and collateral security and to apply the proceeds from the collateral to the claims of all the lenders?

The role of the agent acting on behalf of the secured creditors will be recognised in Portugal, provided that the agent is also a secured creditor, which is usually the case. This requirement derives from the fact that, under Portuguese law, only an entity which is a creditor may request the registration of the security in its own name. In such circumstances, and besides the fact that the agent is also named as secured creditor in the documentation, the documentation shall foresee that the agent will also be acting as a representative of the other creditors in enforcing the security.

The role of the trustee is not recognised in Portugal, except for the specific legal regime applicable only in the context of the Madeira International Business Centre (*Zona Franca da Madeira*).

5.2 If an agent or trustee is not recognised in your jurisdiction, is an alternative mechanism available to achieve the effect referred to above which would allow one party to enforce claims on behalf of all the lenders so that individual lenders do not need to enforce their security separately?

This is not applicable.

5.3 Assume a loan is made to a company organised under the laws of your jurisdiction and guaranteed by a guarantor organised under the laws of your jurisdiction. If such loan is transferred by Lender A to Lender B, are there any special requirements necessary to make the loan and guarantee enforceable by Lender B?

Yes, notice to the borrower and guarantor of the assignment is required, as well as registration of the security (if subject to registration) with the relevant registry (land registry, commercial registry, car registry, financial intermediary or company books, as applicable).

In addition, please note that the assignment of security against a company which is in an insolvency proceeding will, from a practical perspective, also require the notification to the court of the assignment so that the new creditor can be recognised in the insolvency proceeding.

However, please note that there might be situations in which the guarantee may not be assigned. For example, if the parties have restricted the ability of the guarantor to assign, or if the guarantee has been provided *intuitu personae* (i.e. the nature of the guarantee is not separable from the person or the borrower).

6 Withholding, Stamp and Other Taxes; Notarial and Other Costs

6.1 Are there any requirements to deduct or withhold tax from (a) interest payable on loans made to domestic or foreign lenders, or (b) the proceeds of a claim under a guarantee or the proceeds of enforcing security?

Payments of interest by a Portuguese corporate to a foreign lender will be subject to withholding tax, currently at a rate of 25 per cent, or such other reduced withholding tax rate as determined in the applicable Double Tax Treaty. The proceeds of a claim under a guarantee or the proceeds of enforcing security are not subject to withholding tax.

6.2 What tax incentives or other incentives are provided preferentially to foreign lenders? What taxes apply to foreign lenders with respect to their loans, mortgages or other security documents, either for the purposes of effectiveness or registration?

In general, there are no tax incentives to foreign lenders in the context of bank lending transactions, in contrast to the general tax exemption applicable to foreign bondholders.

However, the following specific tax incentives may apply:

(i) full or partial tax exemption in respect of interest paid by public sector entities to foreign lenders (for instance, *Schuldschein* loans); and

(ii) full tax exemption on interest paid by entities operating in the Madeira International Business Centre to foreign entities.

A loan to a Portuguese entity or a guarantee provided by a Portuguese entity will, in principle, attract stamp duty at the rates specified in question 3.9 above. However, please note that non-payment of stamp duty will not have an impact of the effectiveness of the loan or security or the valid registration of security.

6.3 Will any income of a foreign lender become taxable in your jurisdiction solely because of a loan to or guarantee and/or grant of security from a company in your jurisdiction?

The income of a foreign lender deriving from payments of interest will become taxable in Portugal by virtue of the borrower being considered tax resident in Portugal. Please note that, as mentioned in question 6.1 above, there will be withholding tax on the payments of interest in such situation.

6.4 Will there be any other significant costs which would be incurred by foreign lenders in the grant of such loan/guarantee/security, such as notarial fees, etc.?

There are other costs, such as notarial fees and land registry fees, for the registration of a mortgage over real estate. These will not be significant unless the security is granted over several properties. The cost of registration of a mortgage is EUR 225 per property, if the registration is submitted by a notary.

6.5 Are there any adverse consequences to a company that is a borrower (such as under thin capitalisation principles) if some or all of the lenders are organised under the laws of a jurisdiction other than your own? Please disregard withholding tax concerns for purposes of this question.

No specific adverse consequences (other than described above as to withholding tax) will arise by virtue of the lenders being incorporated outside of Portugal.

7 Judicial Enforcement

7.1 Will the courts in your jurisdiction recognise a governing law in a contract that is the law of another jurisdiction (a "foreign governing law")? Will courts in your jurisdiction enforce a contract that has a foreign governing law?

In accordance with the general principle set out in the Portuguese Civil Code, the parties to an agreement may elect the law governing the agreement, provided that such election corresponds to a serious interest of the parties or is the law of a jurisdiction which has a connection with the agreement and is legitimate in the context of the principles of private international law.

Furthermore, under the Rome I Regulation (Regulation (EC) No. 593/2008 of 17 June), the choice of foreign law is valid and will be recognised and enforceable in Portugal, unless there is a mandatory provision in the Rome I Regulation that determines the competence of Portuguese law.

7.2 Will the courts in your jurisdiction recognise and enforce a judgment given against a company in New York courts or English courts (a "foreign judgment") without re-examination of the merits of the case?

Any final judgment obtained in a competent jurisdiction in respect of any sums payable in connection with the agreements would be enforced by the courts of Portugal under the conditions set out in the (recast) Brussels Regulation (Regulation (EU) No. 1215/2012 of 20 December 2012) or the Lugano Convention of 16 September 1988 or, if and when such instruments are not applicable, would be enforced by the courts of Portugal without re-examination of the merits of the case provided that:

(a) there are no doubts about the authenticity or substance of the document in which the judgment is given, and the judgment is final and conclusive;
(b) any conditions imposed by the law of the country in which it was given, which are conditions to its enforcement in the Portuguese courts, have been complied with;
(c) it was issued by a foreign court, the jurisdiction of which had not been claimed fraudulently and does not pertain to matters subject to the exclusive competence of the Portuguese courts;
(d) it would not be adjudged *res judicata* by the Portuguese courts;
(e) the defendant was duly served for the action in accordance with the law of the country in which the judgment was issued and that the principles of the right to a fair trial (*principio do contraditório*) and equal treatment of the parties have been complied with; and
(f) it does not contravene the principles of Portuguese public order.

7.3 Assuming a company is in payment default under a loan agreement or a guarantee agreement and has no legal defence to payment, approximately how long would it take for a foreign lender to (a) assuming the answer to question 7.1 is yes, file a suit against the company in a court in your jurisdiction, obtain a judgment, and enforce the judgment against the assets of the company, and (b) assuming the answer to question 7.2 is yes, enforce a foreign judgment in a court in your jurisdiction against the assets of the company?

In general, filing a suit in Portugal, obtaining a judgment and enforcing it may take, on average, 30 months. Enforcing a foreign judgment in Portugal against the assets of the company could take 12 months. In both scenarios, the timeframe for enforcement of the court decision will depend on how long it takes to identify the assets to be seized.

7.4 With respect to enforcing collateral security, are there any significant restrictions which may impact the timing and value of enforcement, such as (a) a requirement for a public auction, or (b) regulatory consents?

Yes, timing of the enforcement may be affected in the event that there is a public auction of the assets or in the event that such auctions are not successful, if, for instance, no offers higher than the reserve amount are received.

Regulatory consents may also impose a significant delay in the conclusion of the enforcement in the event that the sale of the enforced assets to the acquirer is subject to obtaining regulatory consents, in the context of competition laws or sectorial regulation (sale of qualified shareholdings in financial institutions, defence industries, and public services concessionaires).

7.5 Do restrictions apply to foreign lenders in the event of (a) filing suit against a company in your jurisdiction, or (b) foreclosure on collateral security?

No, in principle, no such restrictions will apply.

7.6 Do the bankruptcy, reorganisation or similar laws in your jurisdiction provide for any kind of moratorium on enforcement of lender claims? If so, does the moratorium apply to the enforcement of collateral security?

Yes, in accordance with the Portuguese Insolvency Code, the commencement of an insolvency proceeding or a *procedimento de revitalização* (similar to a Chapter 11 procedure) will imply a moratorium on the enforcement of collateral security against the insolvent or quasi-insolvent borrower or guarantor.

7.7 Will the courts in your jurisdiction recognise and enforce an arbitral award given against the company without re-examination of the merits?

The Portuguese Republic is a party to the New York Arbitration Convention and therefore any arbitral awards given in another contracting state will be recognised without re-examination of the merits of the claim.

In relation to arbitral awards given in a state which is not a party to the New York Arbitration Convention, or any other convention to which the Portuguese state is a party, the enforcement of an arbitral award in Portugal is subject to the recognition of such award by a court of competent jurisdiction in Portugal, irrespective of the nationality of the parties.

8 Bankruptcy Proceedings

8.1 How does a bankruptcy proceeding in respect of a company affect the ability of a lender to enforce its rights as a secured party over the collateral security?

Yes, in accordance with the Portuguese Insolvency Code, the commencement of an insolvency proceeding or a *procedimento de revitalização* (similar to a Chapter 11 procedure) will suspend all enforcement proceedings against the company.

8.2 Are there any preference periods, clawback rights or other preferential creditors' rights (e.g., tax debts, employees' claims) with respect to the security?

Under the Portuguese Insolvency Code there is a two-year suspect period during which any acts that are "prejudicial" to the insolvent entity and are carried out in bad faith will be set aside.

In addition, the Portuguese Insolvency Code sets out the specific situations in which certain acts may be set aside, including, *inter alia*:

(i) any acts carried out within two years prior to the commencement of the insolvency proceedings without there having been consideration thereof;
(ii) the provision of security for existing obligations by the insolvent entity within six months prior to the commencement of the insolvency proceedings;
(iii) the provision of guarantees by the insolvent entity in respect of debts of third parties within six months prior to the commencement of the insolvency proceedings where there is no benefit (vested interest) to the insolvent entity; or
(iv) the provision of security by the insolvent entity in respect of new transactions within 60 days prior to the commencement of the insolvency proceedings.

Under the Portuguese Civil Code, there is also a concept of *impugnação pauliana* pursuant to which an action may be brought by a creditor to set aside a transaction that results in the decrease of the bankrupt company assets and in circumstances in which there was no consideration, given certain requirements are met.

Preferential creditor's rights exist under Portuguese law such as court fees, tax debts and employees claims.

8.3 Are there any entities that are excluded from bankruptcy proceedings and, if so, what is the applicable legislation?

Yes, the Portuguese Republic and certain public sector entities are excluded from Portuguese insolvency laws, and there is no applicable legislation governing the insolvency of such entities.

8.4 Are there any processes other than court proceedings that are available to a creditor to seize the assets of a company in an enforcement?

In accordance with (i) the Portuguese Civil Code, (ii) the Portuguese Commercial Code, (iii) the regime of the financial pledge, or (iv) the regime of the banking pledge, it is possible that the enforcement of a pledge is conducted in an out-of-court proceeding.

In the case of a pledge created under the rules of the Portuguese Civil Code, the parties may agree to an out-of-court sale of the pledged assets. Please note, however, that in this situation, the pledged assets will, in principle, be in the possession of the pledgee or a custodian appointed by the parties.

In the case of a financial pledge, the Commercial Code pledge, or a banking pledge, the assets may not be in the possession of the pledgee. If the assets are in the possession of the pledgee or an agent appointed by the pledgee, the pledgee may appropriate the assets, but must return to the pledgor any excess amounts.

9 Jurisdiction and Waiver of Immunity

9.1 Is a party's submission to a foreign jurisdiction legally binding and enforceable under the laws of your jurisdiction?

Yes, please see the answer to question 7.2 above.

9.2 Is a party's waiver of sovereign immunity legally binding and enforceable under the laws of your jurisdiction?

In the event that an entity benefits from sovereign immunity, the waiver of the benefit of such immunity will be valid. However, it should be noted that the assets of such entity which are in the public domain (*domínio público*) or used for the purpose of pursuing a public service may not be seized and the entity may not waive immunity over such assets, unless there is a specific law approved for such purpose.

10 Licensing

10.1 What are the licensing and other eligibility requirements in your jurisdiction for lenders to a company in your jurisdiction, if any? Are these licensing and eligibility requirements different for a "foreign" lender (i.e. a lender that is not located in your jurisdiction)? In connection with any such requirements, is a distinction made under the laws of your jurisdiction between a lender that is a bank *versus* a lender that is a non-bank? If there are such requirements in your jurisdiction, what are the consequences for a lender that has not satisfied such requirements but has nonetheless made a loan to a company in your jurisdiction? What are the licensing and other eligibility requirements in your jurisdiction for an agent under a syndicated facility for lenders to a company in your jurisdiction?

Under the General Framework of Credit Institutions and Financial Companies (as approved by Decree-Law No. 298/92 of 31 December), only licensed entities may carry out lending activity in Portugal on a professional basis. The provision of loans to Portuguese entities on a professional and regular basis will trigger a licensing requirement in Portugal. However, if a foreign entity provides loans to Portuguese entities on a single or very infrequent basis, no licensing requirement will apply as the foreign lender may be deemed not to be carrying out activity in Portugal, which assumes a repetition of acts or transactions in Portugal.

EEA entities benefit from passporting rights under the Capital Requirements Directive.

So far as the agent is concerned, no specific licensing requirement applies, although if the agent is a licensed entity in, or passported into, Portugal, then this will mitigate the risk of triggering a licensing requirement in Portugal for the lenders.

11 Other Matters

11.1 Are there any other material considerations which should be taken into account by lenders when participating in financings in your jurisdiction?

We believe that the questions above fairly address the main material issues that arise generally in the context of lending transactions.

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Gonçalo dos Reis Martins has gained comprehensive experience over the last 15 years in advising leading international and domestic investment and retail banks, other financial institutions and asset managers in a wide range of transactions, including syndicated loans for Portuguese blue-chip corporates, asset finance transactions for the oil industry, project finance, direct lending, multi-jurisdictional supply chain finance transactions and Islamic finance work. He has also been involved in the development of the contractual framework, for offering sby banks of new technology-based products for retail clients, as well as in the engagement of Portuguese banks by Fintech companies.

Before joining PLMJ he worked in another leading Portuguese law firm and valuable international experience, having been seconded to the Capital Markets department of Simmons & Simmons and Morgan Stanley's Legal Department (Fixed Income Division), both in London.

Gonçalo earned his Law degree from the Law School of Universidade Nova de Lisboa in 2002, where he also lectured. He is also entitled to practise under English law, being a member of the Law Society of England and Wales since 2007.

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PLMJ is one of Portugal's leading law firms and a key reference in the country's legal sector because of its dynamism, capacity for innovation and quality of service. PLMJ is a full-service firm that focuses on specialisation and offers a complete range of legal services.

The PLMJ Finance team acts in all areas of banking, finance and capital markets.

In the banking and finance segments, the team regularly deals with domestic and cross-border operations in the areas of corporate finance, real estate financing, leveraged and acquisition finance, asset finance, project finance, structured finance, factoring and trade finance.

The PLMJ Finance team comprises four partners, 12 associates and three trainees.

Puerto Rico

Ferraiuoli LLC

José Fernando Rovira-Rullán

1 Overview

1.1 What are the main trends/significant developments in the lending markets in your jurisdiction?

Commercial and consumer lending has seen a reduction over the past decade due to the general economic downturn. Activity in the lending markets continues, albeit at lower volumes and somewhat driven by opportunity funds that have acquired loans in bulk from local banks.

Local lending alternatives are limited as a result of (A) the assisted closure by the Puerto Rico Office of the Commissioner of Financial Institutions ("PROCFI") and the United States Federal Deposit Insurance Corporation ("FDIC") of three local banks during the second quarter of calendar year 2010, (B) the sale of the Puerto Rico operation of a multinational Spanish banking group during the fourth quarter of calendar year 2012, and (C) the assisted closure by the PROCFI and the FDIC of a fourth local bank during the first quarter of calendar year 2015.

It is noteworthy, however, that several well-capitalised opportunity funds and emerging financial institutions have commenced operations in Puerto Rico in recent years.

More recently, Puerto Rico suffered catastrophic damage due to the passing of Hurricane María, the full extent of which is not yet known, particularly, the effect on our national income (resulting from the expected changes in consumption, investment, trade and aid) relative to Puerto Rico's pre-disaster trend.

1.2 What are some significant lending transactions that have taken place in your jurisdiction in recent years?

On March 21, 2013, the Luis Muñoz Marín International Airport Public-Private Partnership Transaction came to a successful completion with the project's financial closing. The local component of the financial closing took place in Ferraiuoli and secured crucial funding for the Highstar Capital and Grupo Aeroportuario del Sureste-led Aerostar Airport Holdings, LLC. Ferraiuoli's multi-disciplinary practice was involved in all aspects of the financial transaction, which included: (A) the re-financing of a portion of the leasehold fee and certain other costs and expenditures through the issuance and sale of senior secured notes in the aggregate principal amount of $350 million; and (B) the financing of certain other costs and expenditures through a senior secured term loan commitment in the aggregate principal amount $50 million and a revolving facility in the aggregate principal amount of $10 million.

On September 22, 2011, the Abertis and Goldman Sachs Infrastructure-led Autopistas Metropolitanas de Puerto Rico closed a significant financing for the 40-year PR-22 and PR-5 real toll concession. The $1.136 billion financing is split between (A) a $750 million club loan with a seven-year bullet maturity, and (B) $386 million in equity. The aforementioned financing was also conducted within the parameters of the Puerto Rico Public-Private Partnerships Act.

While multiple other significant lending transactions have taken place in Puerto Rico in recent years, the above-referenced transactions are probably the most significant and ground-breaking deals completed to date.

2 Guarantees

2.1 Can a company guarantee borrowings of one or more other members of its corporate group (see below for questions relating to fraudulent transfer/financial assistance)?

Except otherwise restricted or limited in the company's governance documents, a company can guarantee borrowings of one or more other members of its corporate group. There is no statutory legal restriction or limitation in this respect.

2.2 Are there enforceability or other concerns (such as director liability) if only a disproportionately small (or no) benefit to the guaranteeing/securing company can be shown?

No. The guarantee will be effective and enforceable against the company if approved by the company in accordance with the company's governance documents.

2.3 Is lack of corporate power an issue?

Yes. The company needs to act and remain in good standing and in compliance with its charter and its internal governance documents. A guarantee authorised with insufficient corporate power could potentially render the same ineffective and unenforceable.

2.4 Are any governmental or other consents or filings, or other formalities (such as shareholder approval), required?

The effectiveness and enforceability of a guarantee issued by a non-public corporation is generally not contingent to the consent or approval of, or the filing or registration with, any Puerto Rico governmental authority. Note, however, that any requirements of this nature need to be nonetheless examined on a case-by-case basis insofar as the same may vary depending on the type of legal entity issuing the guarantee and its internal governance mechanisms. An opinion is generally obtained at closing from counsel to the loan parties confirming that neither the execution and delivery the guarantee, nor the consummation of the transactions contemplated thereunder, requires the consent or approval of, or any filing or registration with, any governmental authority except for those consents, acknowledgments and approvals which have been obtained and those notices which have been given on or prior to closing.

As stated in question 2.2 above, a guarantee will generally be effective and enforceable against the company if approved in accordance with the company's governance documents.

2.5 Are net worth, solvency or similar limitations imposed on the amount of a guarantee?

There are no statutory limitations imposed on the amount of a guarantee by reason of the net worth, solvency or similar criteria of the guarantor.

2.6 Are there any exchange control or similar obstacles to enforcement of a guarantee?

There are no statutory exchange control or similar obstacles to the effectiveness and enforcement of a guarantee.

3 Collateral Security

3.1 What types of collateral are available to secure lending obligations?

There are infinite types of collateral, as virtually anything can be used for such purpose as long as it is acceptable to the secured party. The most common types of collateral include real estate, equipment, inventory, accounts receivable, contracts, general intangibles and fixtures.

3.2 Is it possible to give asset security by means of a general security agreement or is an agreement required in relation to each type of asset? Briefly, what is the procedure?

The manner in which to perfect a lien or security interest varies depending on asset type.

In the context of personal property, a modified version of the United States Uniform Commercial Code Revised Article 9 governs. While most personal property collateral could be covered under a single blanket-lien Security Agreement, it is advisable when dealing with certain types of collateral, such as deposit accounts and life insurance, to prepare separate asset-specific Security Agreements.

In the context of real property, the execution of a Deed of Mortgage before a licensed Puerto Rico notary public, together with compliance with numerous substantive and procedural formalities and its recordation in the Puerto Rico Registry of the Property, is mandatory for the creation of a mortgage lien. On December 8, 2015, the Governor of Puerto Rico signed into law Act No. 210 adopting Puerto Rico's new Registry of the Property Act.

3.3 Can collateral security be taken over real property (land), plant, machinery and equipment? Briefly, what is the procedure?

In the context of personal property, such as machinery and equipment, a modified version of United States Uniform Commercial Code Revised Article 9 governs, which generally requires the execution of a Security Agreement and the filing of a UCC-1 Financing Statement at the applicable filing office.

In the context of real property, it is obligatory to create a mortgage lien via the execution of a Deed of Mortgage before a licensed Puerto Rico notary public, together with compliance with numerous substantive and procedural formalities and its recordation in the Puerto Rico Registry of the Property. On December 8, 2015, the Governor of Puerto Rico signed into law Act No. 210 adopting Puerto Rico's new Registry of the Property Act.

3.4 Can collateral security be taken over receivables? Briefly, what is the procedure? Are debtors required to be notified of the security?

Collateral security can be taken over account receivables by the execution of a Security Agreement and the filing of a UCC-1 Financing Statement at the applicable filing office. Account debtors only need to be notified of the granting of the security interest at the time of the enforcement of the same.

3.5 Can collateral security be taken over cash deposited in bank accounts? Briefly, what is the procedure?

Collateral security can be taken over cash deposited in a bank account by the execution of a Security Agreement and an acknowledgment of control of deposit issued by the depositary bank, usually in the form of an Account Control Agreement.

3.6 Can collateral security be taken over shares in companies incorporated in your jurisdiction? Are the shares in certificated form? Can such security validly be granted under a New York or English law governed document? Briefly, what is the procedure?

Collateral security can be taken over shares in certificated form in companies incorporated in Puerto Rico by the execution of a Security Agreement and the delivery of control over the pledged shares. A secured party obtains control over a certificated security which is delivered to the secured party in bearer or registered form and, if in registered form, is either endorsed to the secured party or in blank or is registered in the name of the secured party in the books of the issuer.

Collateral security can also be taken over uncertificated shares in companies incorporated in Puerto Rico by the execution of a Security Agreement and (A) the filing of a UCC-1 Financing Statement at the applicable filing office, or (B) by exercising control over the uncertificated shares. The secured party obtains control either by becoming the entitlement holder or, as has increasingly become common practice, by entering into an Account Control Agreement with both the securities intermediary and the debtor pursuant to which the securities intermediary agrees that it will comply with all entitlement orders given to it by the secured party without further consent from or action by the debtor. It is important to reference that control takes precedence over the filing. Thus, if a secured party obtains a perfected security interest in the uncertificated shares by control after the debtor has already granted a security interest which was perfected by filing, the later security interest, perfected by control, will have priority over the earlier (filed) security interest.

Likewise, if any of the above operations are to be governed under foreign law, in such case the parties would need to comply with both the laws applicable to Puerto Rico and the laws of the foreign jurisdiction in question.

3.7 Can security be taken over inventory? Briefly, what is the procedure?

Collateral security can be taken over inventory by the execution of a Security Agreement and the filing of a UCC-1 Financing Statement in the applicable filing office.

3.8 Can a company grant a security interest in order to secure its obligations (i) as a borrower under a credit facility, and (ii) as a guarantor of the obligations of other borrowers and/or guarantors of obligations under a credit facility (see below for questions relating to the giving of guarantees and financial assistance)?

Subject to proper corporate approval in accordance with the company's governance documents, a company can grant a security interest in order to secure its obligations under the scenarios contemplated above.

3.9 What are the notarisation, registration, stamp duty and other fees (whether related to property value or otherwise) in relation to security over different types of assets?

The answer to this question varies depending on the type of collateral subject of the security.

In the context of personal property collateral capable of being perfected by the filing of a UCC-1 Financing Statement, the filing of the same with the Commercial Transactions Registry of the Puerto Rico Department of State ("PRDOS") costs at present $25.00 per each registration.

On the other hand, in the context of real property collateral, perfecting a security interest in real property entails the payment of (A) internal revenue and notarial tax stamps, (B) legal assistance stamps, (C) recordation and filing vouchers, and (D) a notarial tariff, all of which are of a statutory nature and calculated based on the value of the transaction.

In general terms, internal revenue and notarial tax stamps, legal assistance stamps and recordation and filing vouchers can be estimated in the aggregate at roughly 0.56% of the value of the transaction. Likewise and subject to certain additional restrictions and thresholds, the notarial tariff can be negotiated by agreement between the parties and the notary public, but the same can never be more than 1% or less than 0.50% of the value of the transaction, and can never be less than $250.00.

Moreover, loan and security documentation notarised by a licensed Puerto Rico notary public also entails the payment of $5 internal revenue stamp per document.

3.10 Do the filing, notification or registration requirements in relation to security over different types of assets involve a significant amount of time or expense?

In general terms, the creation of a security interest on personal property does not involve a significant amount of time or expense. The creation of a mortgage on real estate can be more costly, depending on the complexity of the title and the amount of the mortgage. Please refer to our response in question 3.9 above as to the costs and expenses of security over personal property collateral *vis-à-vis* real property collateral.

3.11 Are any regulatory or similar consents required with respect to the creation of security?

In general terms, only debtor consent is necessary for the creation of a lien or a security interest. Note, however, that certain types of collateral, such as (A) receivables payable by an agency of the local or federal government, (B) airplanes and vessels, and (C) dairy produce quotas, among a few others, may require compliance with certain specific filing, notice and/or consent requirements.

3.12 If the borrowings to be secured are under a revolving credit facility, are there any special priority or other concerns?

No special priority or other concerns arise solely by reason of the borrowing to be secured being a revolving credit facility.

3.13 Are there particular documentary or execution requirements (notarisation, execution under power of attorney, counterparts, deeds)?

All types of documents, both private and public, generally require execution before a licensed Puerto Rico notary public. In the case of mortgages, these need to be executed in deed form before a licensed Puerto Rico notary public and following numerous substantive and procedural formalities, such as the filing in the Registry of the Property, in order for it to be effectively constituted.

4 Financial Assistance

4.1 Are there prohibitions or restrictions on the ability of a company to guarantee and/or give security to support borrowings incurred to finance or refinance the direct or indirect acquisition of: (a) shares of the company; (b) shares of any company which directly or indirectly owns shares in the company; or (c) shares in a sister subsidiary?

(a) Shares of the company

Except if the company's organisational and/or governance documents dictate otherwise, there are no statutory prohibitions or restrictions on the ability of a company to guarantee and/or give security to support borrowings incurred to finance or refinance the direct or indirect acquisition of shares of the company.

(b) Shares of any company which directly or indirectly owns shares in the company

Except if the company's organisational and/or governance documents dictate otherwise, there are no statutory prohibitions or restrictions on the ability of a company to guarantee and/or give security to support borrowings incurred to finance or refinance the direct or indirect acquisition of shares of any company which directly or indirectly owns shares in the company.

(c) Shares in a sister subsidiary

Except if the company's organisational and/or governance documents dictate otherwise, there are no statutory

Puerto Rico

prohibitions or restrictions on the ability of a company to guarantee and/or give security to support borrowings incurred to finance or refinance the direct or indirect acquisition of shares of any company which directly or indirectly owns shares in a sister subsidiary.

5 Syndicated Lending/Agency/Trustee/Transfers

5.1 Will your jurisdiction recognise the role of an agent or trustee and allow the agent or trustee (rather than each lender acting separately) to enforce the loan documentation and collateral security and to apply the proceeds from the collateral to the claims of all the lenders?

Yes. In syndicated credit facilities, which are fairly common in Puerto Rico in the context of larger credit facilities, an administrative and collateral agent usually acts on behalf and for the benefit of all participating lenders.

5.2 If an agent or trustee is not recognised in your jurisdiction, is an alternative mechanism available to achieve the effect referred to above which would allow one party to enforce claims on behalf of all the lenders so that individual lenders do not need to enforce their security separately?

While certain jurisdictions of the United States of America recognise the concept of a security trust, that is not the case in Puerto Rico.

5.3 Assume a loan is made to a company organised under the laws of your jurisdiction and guaranteed by a guarantor organised under the laws of your jurisdiction. If such loan is transferred by Lender A to Lender B, are there any special requirements necessary to make the loan and guarantee enforceable by Lender B?

Puerto Rico loan documentation generally includes specific assignment provisions that enable the original lender to transfer the loan to a third party. Besides compliance with any transfer requirements provided in the applicable loan documentation and the completion of any necessary endorsements, there are no special statutory requirements necessary to make the loan and guarantee enforceable by the transferee.

6 Withholding, Stamp and Other Taxes; Notarial and Other Costs

6.1 Are there any requirements to deduct or withhold tax from (a) interest payable on loans made to domestic or foreign lenders, or (b) the proceeds of a claim under a guarantee or the proceeds of enforcing security?

Interest payments to domestic lenders are not subject to any Puerto Rico withholding requirements. Interest payments to foreign lenders are not subject to any Puerto Rico withholding requirements unless the borrower and the lender are related parties, in which case the interest payments are subject to a 29% withholding tax.

The above rules would also apply to the portion of a claim under a guarantee or security interest that consists of accrued but unpaid interest. The portion of the claim representing principal would not be subject to any Puerto Rico withholding requirements.

6.2 What tax incentives or other incentives are provided preferentially to foreign lenders? What taxes apply to foreign lenders with respect to their loans, mortgages or other security documents, either for the purposes of effectiveness or registration?

Foreign lenders are not subject to Puerto Rico income taxes on their interest income unless: (A) the loan is attributable to a Puerto Rico office or place of business; or (B) the lender and the borrower are related parties.

6.3 Will any income of a foreign lender become taxable in your jurisdiction solely because of a loan to or guarantee and/or grant of security from a company in your jurisdiction?

Income generated by a foreign lender is not taxable in Puerto Rico solely because of a loan to or guarantee and/or grant of security from a company in Puerto Rico.

6.4 Will there be any other significant costs which would be incurred by foreign lenders in the grant of such loan/guarantee/security, such as notarial fees, etc.?

Income generated by a foreign lender is not taxable in Puerto Rico solely because of a loan to or guarantee and/or grant of security from a company in Puerto Rico.

6.5 Are there any adverse consequences to a company that is a borrower (such as under thin capitalisation principles) if some or all of the lenders are organised under the laws of a jurisdiction other than your own? Please disregard withholding tax concerns for purposes of this question.

There are no adverse consequences to a borrower company by reason of one or more lenders being organised under the laws of a jurisdiction other than Puerto Rico.

7 Judicial Enforcement

7.1 Will the courts in your jurisdiction recognise a governing law in a contract that is the law of another jurisdiction (a "foreign governing law")? Will courts in your jurisdiction enforce a contract that has a foreign governing law?

Puerto Rico courts generally find choice of law clauses valid. However, the choice of law clause must meet the following two requirements: (A) the chosen state has a substantial relationship to the parties or the transaction and there is a reasonable basis for the parties' choice; or (B) application of the law of the chosen state would not be contrary to a fundamental policy of a state which has a materially greater interest than the chosen state in the determination of the particular issue.

7.2 Will the courts in your jurisdiction recognise and enforce a judgment given against a company in New York courts or English courts (a "foreign judgment") without re-examination of the merits of the case?

The United States Congress has mandated that federal courts grant full faith and credit to the judgments of all states, territories and possessions of the United States, including Puerto Rico. The method by which a judgment of another state is recognised and enforced, is determined by the local law of the enforcing state. However, foreign or state court judgments do not automatically operate in Puerto Rico. In order to be recognised and enforced, exequatur proceedings are necessary. Under Puerto Rico law, local courts must give full faith and credit to judgments from Courts in the United States when the following standards apply: (A) that the judgment has been issued by a state court with jurisdiction over the person and the subject matter; (B) that the state court that issued the judgment observed due process of law; and (C) that the judgment has not been obtained by fraud. The court must give full faith and credit to state court judgments when the exequatur proceedings factors are met.

In cases involving judgments by non-United States jurisdictions, a more complex test applies. In the absence of treaty or special legislation, foreign judgments may be validated in Puerto Rico only if (A) the foreign judgment was issued by a court with jurisdiction over the person and the subject matter, (B) the judgment was entered by a competent court, (C) due process of law was observed, (D) the justice system under which the judgment was rendered is characterised by its impartiality and absence of prejudice against foreigners, (E) the judgment is not contrary to Puerto Rico public policy or of the selected forum, and (F) the judgment was not procured by fraud.

7.3 Assuming a company is in payment default under a loan agreement or a guarantee agreement and has no legal defence to payment, approximately how long would it take for a foreign lender to (a) assuming the answer to question 7.1 is yes, file a suit against the company in a court in your jurisdiction, obtain a judgment, and enforce the judgment against the assets of the company, and (b) assuming the answer to question 7.2 is yes, enforce a foreign judgment in a court in your jurisdiction against the assets of the company?

In general terms, a complaint where the defendant has no defence (and none are raised) can be resolved, and a judgment obtained and enforced, in a period of five to nine months. In order for a foreign judgment to be enforced, the interested party must commence exequatur proceedings in a court in Puerto Rico. Such proceedings can take anywhere from four to six months, without taking into account the time to obtain real property through the public sale process (depending the municipality, another two months).

7.4 With respect to enforcing collateral security, are there any significant restrictions which may impact the timing and value of enforcement, such as (a) a requirement for a public auction, or (b) regulatory consents?

Real property that is duly registered and serves as collateral security must be sold at a public auction in Puerto Rico which significantly impacts the timing and value of enforcement. No regulatory consent is needed for enforcing collateral security. However, in cases where the collateral security is a residential property that is the principal dwelling of the debtor, creditor and debtor must participate in mandatory mediation.

7.5 Do restrictions apply to foreign lenders in the event of (a) filing suit against a company in your jurisdiction, or (b) foreclosure on collateral security?

Subject to certain exceptions and in order to file suit in local Puerto Rico courts (non-federal), a foreign corporation or a claimant who does not reside in Puerto Rico must pay a non-resident bond of at least $1,000.00. Court proceedings are stayed until the non-resident bond is submitted.

7.6 Do the bankruptcy, reorganisation or similar laws in your jurisdiction provide for any kind of moratorium on enforcement of lender claims? If so, does the moratorium apply to the enforcement of collateral security?

The United States Bankruptcy Code ("Bankruptcy Code") has full force and effect in Puerto Rico, except for Chapter 9. Puerto Rico is considered a state for all purposes of the Bankruptcy Code, except for who may be a debtor under Chapter 9. The Bankruptcy Code creates a forced moratorium on the creditor's right to enforce and execute his security interest. Upon the filing of a bankruptcy petition, the lender needs to seek authorisation from the bankruptcy court to exercise any right to enforce a collateral security. Please refer to our response in question 8.1 below for further insight as to the ability of a lender to enforce its rights as a secured party over the collateral security.

7.7 Will the courts in your jurisdiction recognise and enforce an arbitral award given against the company without re-examination of the merits?

Puerto Rico courts have adopted the standard of judicial restraint not to interfere with arbitration awards except when the parties agreed that the award must be issued according to law, in which case the court may correct errors of law in regard to the applicable law. In such a case, judicial review of arbitration awards in Puerto Rico is akin to judicial review of administrative decisions. Despite such judicial restraint a Puerto Rico courts may entertain a challenge of the award based on: (A) fraud; (B) misconduct; (C) due process violations; (D) violation of public policy; (E) lack of jurisdiction; and (F) because the award does not resolve all issues submitted for resolution.

8 Bankruptcy Proceedings

8.1 How does a bankruptcy proceeding in respect of a company affect the ability of a lender to enforce its rights as a secured party over the collateral security?

The automatic stay contemplated under Section 362 of the Bankruptcy Code prohibits, although not on an absolute basis, any creditor from taking aggressive action against the debtor after the filing of a bankruptcy petition. In order for a secured creditor to enforce its rights, it must file a "motion for relief from the stay" in order to get permission to take various actions against the collateral held by the bankruptcy debtor. In general terms, a secured creditor is entitled to relief from the stay only if it can successfully evidence: (A) good cause, including lack of adequate protection for the secured creditor; or that (B) the debtor does not have equity in the property and it is not necessary for an effective Chapter 11 reorganisation under the Bankruptcy Code.

8.2 Are there any preference periods, clawback rights or other preferential creditors' rights (e.g., tax debts, employees' claims) with respect to the security?

The power to avoid preferential transfers under section 547 of the Bankruptcy Code serves two broad purposes: (A) it prevents creditors from exerting undue pressure on struggling debtors; and (B) it discourages a debtor from engaging in unusual acts that either favour certain creditors or otherwise hasten the debtor's bankruptcy. To prevent this result, the Bankruptcy Code exempts certain transfers made within the ordinary course of the debtor's and creditor's business.

To prove the "ordinary course of business defence" the creditor must show that the preference payments were made in the "ordinary course of business" between the creditor and the debtor. Typically, this is done by showing that the same were: (A) not the result of any overt collection activity on the part of the creditor; and (B) were made in a similar amount of time and under similar terms and conditions as previous, non-preference period payments made by the debtor to the creditor. Alternatively, if the payments were not made in the ordinary course of business between the parties, the creditor can show that the preference payments were made on terms and conditions prevalent in the respective industry. All payments that are shown to have been made in the ordinary course of business are not avoidable as preferences and need not be repaid.

The Bankruptcy Code establishes a 90-day period prior to the filing of a bankruptcy petitions as a preferential transfer period. In certain cases, such term can be extended to two years under the Bankruptcy Code and further extended according to available remedies in the state law.

The Bankruptcy Code also establishes different types of priority claims such as: domestic support obligations; extensions of credit in an involuntary bankruptcy case; wages/salaries/commissions; contributions to employee benefit plans; claims of certain farmers and fishermen; deposits by individuals; taxes and debt owed to governments; commitments to maintain capital of an insured depository institution; and claims for death or injury while the debtor was intoxicated. These priority claims are also subject to "the ordinary course of business defence". Therefore, in order to be avoided as preferential transfers, the transactions would have occurred during the preference period and outside the normal relations of the creditor and the debtor.

8.3 Are there any entities that are excluded from bankruptcy proceedings and, if so, what is the applicable legislation?

The Bankruptcy Code precludes certain entities from qualifying as debtors in bankruptcy proceedings. Entities from highly regulated industries such as domestic insurance companies, banks, savings banks, cooperative banks, savings and loan associations, building and loan associations, homestead associations, credit unions, or industrial banks or similar institutions have other federal statutes which control their restructuring; for these companies, the Federal Deposit Insurance Act controls. It is still uncertain, since neither the Bankruptcy Code nor the Federal Courts have expressly determined so, whether Series LLC's are also excluded from entering any bankruptcy relief proceeding.

8.4 Are there any processes other than court proceedings that are available to a creditor to seize the assets of a company in an enforcement?

A bankruptcy proceeding with an automatic stay order in effect precludes the creditor from seizing the debtor's assets. However, if the bankruptcy case is dismissed or the stay is lifted, the creditor can pursue the execution of its collateral. If the collateral is abandoned by the bankruptcy trustee, the creditor would also have certain rights over the collateral. It will depend on the chapter in which the bankruptcy case is filed and on the rights of the creditor under other applicable laws.

Moreover, depending upon the nature of the collateral and the provisions of the collateral documents, creditors may be permitted to exercise self-help remedies, some contemplated under Puerto Rico's modified version of the United States Uniform Commercial Code.

9 Jurisdiction and Waiver of Immunity

9.1 Is a party's submission to a foreign jurisdiction legally binding and enforceable under the laws of your jurisdiction?

It is well established that forum selection clauses are *prima facie* valid and should be enforced unless enforcement is shown by the resisting party to be 'unreasonable' under the circumstances. More specifically, a forum selection clause should be enforced unless the resisting party can show that enforcement would be unreasonable and unjust, or that the clause was invalid for such reasons as fraud or overreaching or that enforcement would contravene a strong public policy of the forum in which suit is brought, whether declared by statute or by judicial decision.

9.2 Is a party's waiver of sovereign immunity legally binding and enforceable under the laws of your jurisdiction?

Puerto Rico can waive its immunity in three ways: (A) by a clear declaration that it intends to submit itself to the jurisdiction of a federal court; (B) by consent to or participation in a federal programme for which waiver of immunity is an express condition; or (C) by affirmative conduct in litigation. However, Puerto Rico's waiver of sovereign immunity in its own courts is not a waiver of the Eleventh Amendment immunity in the federal courts.

10 Licensing

10.1 What are the licensing and other eligibility requirements in your jurisdiction for lenders to a company in your jurisdiction, if any? Are these licensing and eligibility requirements different for a "foreign" lender (i.e. a lender that is not located in your jurisdiction)? In connection with any such requirements, is a distinction made under the laws of your jurisdiction between a lender that is a bank *versus* a lender that is a non-bank? If there are such requirements in your jurisdiction, what are the consequences for a lender that has not satisfied such requirements but has nonetheless made a loan to a company in your jurisdiction? What are the licensing and other eligibility requirements in your jurisdiction for an agent under a syndicated facility for lenders to a company in your jurisdiction?

The laws of the Commonwealth of Puerto Rico require that individuals and companies be authorised before engaging in any financial business on its jurisdiction. The licensing requirements will vary depending on the business of each lender. If a lender intends to become involved in any *consumer* lending activities within the jurisdiction of Puerto Rico, such lender must first obtain an authorisation from the PROCFI. To the extent that such lender is qualified as a national association under a United States federal charter, the process for obtaining such an authorisation from PROCFI should be fairly simple and expedient. As part of the aforementioned process, such lender will likely be required by PROCFI to become authorised to do business in Puerto Rico at the Corporations Registry of the PRDOS.

If a lender intends to become involved in any *commercial* lending activities within the jurisdiction of the Commonwealth of Puerto Rico, the licensing requirements are more lax. Depending on the nature and volume of the transactions proposed to be transacted within Puerto Rico's territorial boundaries, authorisation from PROCFI and registration with the PRDOS may not be required.

The PROCFI grants licences under the following categories: Credit Repair Agencies; Brokerage Institutions; Commercial Banks; Casinos; Check Cashers; Financial Intermediaries; Pawn Shops; Instalment Sales and Credit Cards; International Banking Entities; International Financial Institutions; Investment Advisors; Leasing Companies; Money Transmitters; Mortgage Institutions; Mortgage Brokers; Small Loan Companies; Mortgage Loan Originators; and Trust Companies.

Except for Credit Unions, which are licensed, supervised and insured by the *Corporación Pública para la Supervisión y Seguro de Cooperativas de Puerto Rico* ("COSSEC"), and individuals and companies engaged in the insurance business that fall under the jurisdiction of the Insurance Commissioner of Puerto Rico, the remaining group must either obtain a licence or be registered with the PROCIF.

11 Other Matters

11.1 Are there any other material considerations which should be taken into account by lenders when participating in financings in your jurisdiction?

The answers provided above properly address the main material considerations for lending transactions governed under Puerto Rico law.

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Mr. Rovira-Rullán is a Capital Member of Ferraiuoli, Chair of its Commercial Lending Practice Group, Chair of its Conflict Committee and member of its Compensation Committee. Prior to joining Ferraiuoli, Mr. Rovira-Rullán worked for Puerto Rico's Thirteenth (13th) Legislative Assembly as Special Advisor to the Director of the Office of Legislative Services where he collaborated closely with lawmakers and other executive personnel and was actively involved in the legislative process.

Mr. Rovira-Rullán's principal areas of practice include commercial lending, financial restructuring, real estate, corporate governance and general corporate law. As a transactional attorney, Mr. Rovira-Rullán principally concentrates his practice in the representation of foreign and domestic commercial lenders, real estate developers and other business entities.

Throughout his career, Mr. Rovira-Rullán has been actively involved in all aspects of the commercial lending, real estate and corporate practice. Representative clients include local and cross-border lending institutions, real estate developers, commercial real estate management companies and global commodity trading firms.

Ferraiuoli LLC
Looking Forward

From the very beginning, *Ferraiuoli* was founded as an alternative to business as usual. We recognised that in order to become one of Puerto Rico's leading law firms, we had to partner with our clients and provide them with smart, cost-efficient, business-savvy legal advice. Our clients run the gamut from local entrepreneurs to multi-national Fortune 500 companies. They are innovators in technology, energy, finance and health care. They are in the business of looking forward. And so are we.

Ferraiuoli has received international recognition in the legal field by *Chambers & Partners*, a London-based legal directory firm that publishes, on an annual basis, the leading directories of the legal profession identifying the world's top lawyers and law firms. In its 2018 Latin America and Global editions, Chambers ranked *Ferraiuoli* as a leader in Corporate, Intellectual Property, Labour and Employment, Real Estate, and Tax and several firm attorneys were named "Leaders in their Fields" by the publication. *Ferraiuoli* has further been honoured as one of Puerto Rico's outstanding firms by *Chambers & Partners* as it was shortlisted as one of the candidates for Puerto Rico's Law Firm of the Year for the years 2011–2017.

Romania

Valentin Trofin

Trofin & Asociații

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1 Overview

1.1 What are the main trends/significant developments in the lending markets in your jurisdiction?

We have noticed an increase in commercial real estate properties financing in 2017 compared to 2016. Investments in Romanian commercial real estate properties reached about EUR 1 billion in 2017, up 10% compared to the previous year (EUR 890 million).

The number of transactions increased in Romania, with the average deal size standing at about USD 28.5 million. Bucharest accounted for some 36% of the total investment volume, less than in 2016. The retail transactions (43%) dominate the market volumes, while industrial, hotels and office accounted for over 22%, 18% and 17% respectively.

1.2 What are some significant lending transactions that have taken place in your jurisdiction in recent years?

European Investment Bank financing in Romania came to a total of EUR 1.3 billion in 2017. The total lending of the EIB Group (the European Investment Bank and the European Investment Fund) in Romania in 2017 was EUR 1.87 billion for infrastructure EUR 972 million, small and medium-sized enterprises EUR 624 million, environment EUR 265 million, innovation and skills EUR 6 million. The European Fund for Strategic Investments (EFSI) is an initiative to help overcome the current investment gap in the EU.

Other sources for financing in Romania are syndicated loans. The Romanian syndicated loan market is estimated at EUR 1 billion. For example, in June 2017, UNICREDIT BANK and BRD-GROUPE SOCIETE GENERALE provided A&D Pharma Group with a syndicated loan for a value of EUR 177 million.

2 Guarantees

2.1 Can a company guarantee borrowings of one or more other members of its corporate group (see below for questions relating to fraudulent transfer/financial assistance)?

A company may guarantee the borrowings of other members of its group if the guarantor has a certain commercial benefit deriving from the guarantee.

The most important restriction provided by Romanian law on this matter is that the guaranteeing operation should not represent a financial assistance transaction.

The assessment of the commercial benefit is not subject to any particular criteria. Thus, the guarantor's directors shall carefully asses each case, considering the ratio between risks undertaken and the potential benefits that might be obtained by the guarantor, and also the general financial situation of the borrower, the general and specific terms of transaction and the group relationship.

2.2 Are there enforceability or other concerns (such as director liability) if only a disproportionately small (or no) benefit to the guaranteeing/securing company can be shown?

According to Romanian law, financial assistance is prohibited. This interdiction is stipulated specifically only for joint stock companies, but there are opinions arguing that it should also be applied to limited liability companies also.

Secondly, as shown in question 2.1, a guarantor should have a certain interest in relation to any guarantee granted to support borrowings of another corporation.

Also, the Romanian Company Law sets that joint stock companies cannot guarantee the borrowings of their directors and the borrowings of companies where directors or their spouses or relatives are directors or shareholders of more than 20% of the share capital.

If one of these rules is breached, the guarantee will be declared null and void and can attract criminal liability of the directors in specific cases.

Another requirement set by the law for the guarantor is to possess and maintain sufficient assets in order to cover the secured liabilities, except where the creditor required that the guarantor was a particular person.

2.3 Is lack of corporate power an issue?

Generally, in order to be able to grant loans, a company must have included in the scope of activity, and appropriately authorised, the carrying out of lending activities.

However, in order not to fall within the scope of normative acts applicable in the field of financial-banking activities issued by the National Bank of Romania, the borrowing company will have to prove the necessity, the opportunity and the efficiency of such a lending operation, in the case of affiliated companies, that is, when the loan is granted within the company group members.

2.4 Are any governmental or other consents or filings, or other formalities (such as shareholder approval), required?

In principle, there are no such consents. Still, in the case of joint stock companies, the Board of Directors or the Directorate will be able to conclude legal acts in the name of and on behalf of the company by which to establish security interests over the company's assets whose value exceeds half of the book value of all the company's assets at the date of conclusion of the legal act, only with the prior approval of the general meeting of the shareholders.

In addition, when making any payments equal to or greater than EUR 50,000 or equivalent to non-residents, residents of credit institutions have an obligation to fill in a form provided by the credit institution used for the payment or by the payment authority. Also, credit institutions may use forms according to their own requirements in order to make any payments to non-residents with a value of less than EUR 50,000 or equivalent at the date of payment.

2.5 Are net worth, solvency or similar limitations imposed on the amount of a guarantee?

In general, no (except for approvals for the guarantees referred to in question 2.4).

2.6 Are there any exchange control or similar obstacles to enforcement of a guarantee?

In principle, no. Yet, in case of foreign lenders, the borrower can be restricted or limited from paying due amounts and the lender can be restricted from exercising its rights against a borrower. This safeguard measure may be imposed by the National Bank of Romania, according to the regulation on foreign exchange regime.

3 Collateral Security

3.1 What types of collateral are available to secure lending obligations?

The New Civil Code provides the following types of collateral available in order to secure lending: pledge; and immoveable mortgage.

3.2 Is it possible to give asset security by means of a general security agreement or is an agreement required in relation to each type of asset? Briefly, what is the procedure?

An agreement in relation to each type of assets is not required, only a distinction between movable and immovable property and shares.

Firstly, a general pledge agreement may be concluded that can cover most types of asset, such as bank accounts, stocks, inventory, receivables, intellectual property, intangible assets and universalities, or it can be divided into many agreements for each type of asset.

Secondly, in order to take a collateral security over the real estate of the borrower an immoveable mortgage agreement is usually used which may include the rent and the insurance pertaining to the real estate.

Thirdly, the share mortgage agreement is used when the lending transaction is secured by the shareholders of the borrower company with their own shares.

3.3 Can collateral security be taken over real property (land), plant, machinery and equipment? Briefly, what is the procedure?

Yes, collateral security can be taken over land, plant, machinery and equipment.

In case of the land, an immoveable mortgage agreement will be concluded. The agreement will be authenticated by a public notary and registered in the Land Book. If some moveable assets are accessories to the real estate, the agreement will also be registered in the Electronic Archive.

The plant, machinery and equipment are usually brought as security by means of pledge agreement. This does not require the authentication by a public notary, but only a deed that describes the assets in a sufficiently precise way. The description is sufficiently precise, even if the asset is not individualised insofar as it reasonably allows it to be identified.

3.4 Can collateral security be taken over receivables? Briefly, what is the procedure? Are debtors required to be notified of the security?

Under Romanian law, collateral security can be taken over receivables by way of pledge. The pledge may have as its object either one or more receivable or a universality of receivables.

The debtor of the pledge debt must be notified in writing, with the notification coming into effect as of the date on which the debtor received the communication. On the other hand, the effects of the notification are not conditional to the debtor's effective receipt of the notification; according to the law, the pledge lender is only obliged to inform the debtor about establishing the pledge.

The pledge on a receivable that is also guaranteed with a moveable or immovable mortgage must be registered with the Electronic Archive or the Land Book.

The pledge of a receivable confers upon the creditor, when the conditions for the commencement of forced execution are met, the right to take over the title of the claim, to demand and obtain the payment or, at his choice, to sell the claim and to take the price, all within the guaranteed amount.

3.5 Can collateral security be taken over cash deposited in bank accounts? Briefly, what is the procedure?

Collateral security can be taken over cash deposits in bank accounts, according to Romanian law. In this case, the bank account must be individually identified in the mortgage agreement.

The publicity of a mortgage on the bank accounts opened at a credit institution is made by registering the mortgage into the archive or can be satisfied by checking the account.

In order to ensure priority, the lender should hold control over the mortgaged bank account.

A creditor acquires control over an account if (i) the mortgage lender is the actual credit institution where the account is opened, (ii) the creator, credit institution and creditor agree in writing that the credit institution, without requiring the consent of the mortgage constituent, will follow the instructions by which the creditor has the amounts in the account, or (iii) the mortgage creditor becomes the account holder.

3.6 Can collateral security be taken over shares in companies incorporated in your jurisdiction? Are the shares in certificated form? Can such security validly be granted under a New York or English law governed document? Briefly, what is the procedure?

Collateral security may be taken over shares in companies incorporated in Romania usually by means of pledge.

The pledge on the shares shall be made by means of a private signature, showing the amount of the debt, the value and the category of the guarantee shares, and, in the case of registered or bearer nominatives issued in the material form, also by mentioning the pledge by title, signed by the creditor and the shareholder or their trustees.

The pledge shall be registered in the register of shareholders held by the board of directors, respectively by the directorate, or, as the case may be, by the independent company keeping the shareholder register. The pledge creditor will receive the proof of registration.

The pledge becomes opposed to third parties and acquires a rank in order of preference of the creditors as of the date of registration in the Electronic Archive of the Real Securities Guarantees.

Even if the legal basis of the constitution, transfer, restraint or extinction of the collateral security was constituted by the application of another law, the pledge will be subject to the law of the place where the asset is situated. The validity, the publicity and the effects of the mortgage or pledge will be subject to Romanian law, therefore being necessary to conclude one of the mortgage agreements shown above.

3.7 Can security be taken over inventory? Briefly, what is the procedure?

Under Romanian law, a general pledge agreement may be concluded over inventory. This agreement is not subject to the authentication of the public notary, but the assets must be descripted in a sufficiently precise way. As shown above, the description is sufficiently precise, even if the asset is not individualised insofar as it reasonably allows it to be identified.

The description can be made by drawing up a list of mortgaged movable assets, by determining the category to which they belong, by indicating the quantity, by setting a determination formula and by any other means that reasonably allows the identification of the mortgaged movable asset.

3.8 Can a company grant a security interest in order to secure its obligations (i) as a borrower under a credit facility, and (ii) as a guarantor of the obligations of other borrowers and/or guarantors of obligations under a credit facility (see below for questions relating to the giving of guarantees and financial assistance)?

There is no such prohibition under Romanian law, therefore a company may grant a security interest in order to secure its obligations under a credit facility, both as a borrower and as a guarantor of the obligations of other borrowers and/or guarantors of obligations.

3.9 What are the notarisation, registration, stamp duty and other fees (whether related to property value or otherwise) in relation to security over different types of assets?

As a general rule, in the Romanian procedure related to granting security over different type of assets, there are is no stamp duty or other similar fee.

The only fees payable are the ones associated with: the registration of the mortgages in the Electronic Archive or other public register; the authentication of the immovable mortgage agreement by a public notary; and the authorised translations of the finance documents; as well as the registration of such an agreement in the Land Book.

3.10 Do the filing, notification or registration requirements in relation to security over different types of assets involve a significant amount of time or expense?

Generally, the notification and the registration of securities does not involve a significant amount of time. In order to register a deed or a court decision in the Land Registry or the Electronic Archive it usually takes a few days and the authentication of an immoveable mortgage agreement by a public notary usually takes a few hours. The fees payable in order to register the security is calculated proportionally with the value of the guaranteed asset, but is not a high-cost procedure.

3.11 Are any regulatory or similar consents required with respect to the creation of security?

In order to create a security, the articles of association of the company should mention the approval levels for a facility or a board decision on this matter can be issued.

As set out above for joint stock companies, if the security exceeds half of the book value of the company's assets at the date of conclusion of the legal act, the security may be granted only with prior approval of the general meeting of the shareholders.

3.12 If the borrowings to be secured are under a revolving credit facility, are there any special priority or other concerns?

There is no special priority in case of borrowings under a revolving credit facility. The guarantee structure is flexible, including mortgage guarantees on equipment, machinery and real estate.

3.13 Are there particular documentary or execution requirements (notarisation, execution under power of attorney, counterparts, deeds)?

See our answers above.

4 Financial Assistance

4.1 Are there prohibitions or restrictions on the ability of a company to guarantee and/or give security to support borrowings incurred to finance or refinance the direct or indirect acquisition of: (a) shares of the company; (b) shares of any company which directly or indirectly owns shares in the company; or (c) shares in a sister subsidiary?

(a) Shares of the company

According to the law, a company is allowed to acquire its own shares, either directly or through a person acting in his own name but on behalf of the company concerned, subject to the following conditions:

i) the approval of the acquisition of own shares is granted by the extraordinary general meeting of the shareholders, that shall determine the conditions of this acquisition, in particular the maximum number of shares to be acquired, the duration of the authorisation (that it may not exceed 18 months from the date of publication of the decision in the Official Gazette of Romania, Part IV), and, in the case of an acquisition by onerous title, their minimum and maximum value;

ii) the nominal value of own shares acquired by the company, including those already in its portfolio, may not exceed 10% of the subscribed share capital;

iii) the transaction may only deal with fully paid shares; and

iv) payment of the shares thus acquired shall be made only from the distributable profit or from the company's available reserves, entered in the last approved annual financial statement, except for the legal reserves.

If own shares are acquired for distribution to the employees of the company, the shares thus acquired must be distributed within 12 months from the acquisition date.

(b) Shares of any company which directly or indirectly owns shares in the company

The law provides that the subscription, acquisition or holding of shares in a joint-stock company by another company where the joint-stock company directly or indirectly holds the majority of the voting rights or whose decisions may be significantly influenced by the joint-stock company is considered to be carried out by the joint-stock company itself.

The provisions mentioned above shall also apply when the company through which the underwriting, acquisition or holding of such shares is performed is governed by the law of another State.

Moreover, a company may not make advances or loans or provide collateral security for the subscription or acquisition of its own shares by a third party. This provision shall not apply to transactions in current operations of credit institutions and other financial institutions.

Conclusion: in this situation, it is considered that the acquisition is carried out by the joint-stock company itself, thus the provisions under situation (a) are applicable, namely a company may not provide any financial assistance in the form of a loan, guarantee or security interest for the acquisition of its own shares as these ways of acquisition are not compliant with the four cumulative conditions provided above.

Moreover, loans or collateral security to a third party is expressly forbidden.

(c) Shares in a sister subsidiary

There is no financial assistance prohibition as such, but this type of transaction remains subject to the corporate benefit rules described above.

5 Syndicated Lending/Agency/Trustee/ Transfers

5.1 Will your jurisdiction recognise the role of an agent or trustee and allow the agent or trustee (rather than each lender acting separately) to enforce the loan documentation and collateral security and to apply the proceeds from the collateral to the claims of all the lenders?

According to the provisions governing the mandate contract, the trustee can make conservation and administration acts (general mandate) and also disposition acts (special mandate – expressly empowered). Also, the mandate extends to all acts necessary for its execution, even if not expressly stated.

Moreover, according to the law, the administrators of a company are allowed to do all the operations required to carry out the object of the company's activity, except for the restrictions shown in the Articles of Incorporation.

The acts of disposition regarding the assets of a company may be concluded pursuant to the powers conferred to the legal representatives of the company, as the case may be, by law, by the Articles of Incorporation or by the decisions of the company's statutory bodies adopted in accordance with the provisions of the law and of the company's Articles of Incorporation. A special power of attorney in authentic form for this purpose is not necessary, even if the acts of disposition have to be concluded in authentic form.

The obligations and liability of administrators are governed by the provisions of the mandate contract and those specifically provided for by the law.

5.2 If an agent or trustee is not recognised in your jurisdiction, is an alternative mechanism available to achieve the effect referred to above which would allow one party to enforce claims on behalf of all the lenders so that individual lenders do not need to enforce their security separately?

See answer at question 5.1 above.

5.3 Assume a loan is made to a company organised under the laws of your jurisdiction and guaranteed by a guarantor organised under the laws of your jurisdiction. If such loan is transferred by Lender A to Lender B, are there any special requirements necessary to make the loan and guarantee enforceable by Lender B?

The receivables assignment involves the transfer of one or more receivables from the primary creditor (acting as assignor) to a new creditor (acting as assignee) by means of a bipartite agreement, generally concluded between the creditors, while the assigned debtor is not even notified about this agreement. The consent of the debtor is required only when, as the occasion requires, the debt is essentially linked to the person of the creditor.

The receivables assignment transfers all the rights of the assignor relating to the assigned receivables and also the securities and all related accessories of the debt to the assignee. However, the assignor cannot transfer, without the consent of the pledger, the possession of the pledged asset to the assignee.

There are no special requirements necessary to make the loan and guarantee enforceable by the lender that took over the loan from the primary lender. However, the forms of publicity regarding the guarantees of the loans must be complied with.

6 Withholding, Stamp and Other Taxes; Notarial and Other Costs

6.1 Are there any requirements to deduct or withhold tax from (a) interest payable on loans made to domestic or foreign lenders, or (b) the proceeds of a claim under a guarantee or the proceeds of enforcing security?

Revenue in the form of interest paid by the borrower to a foreign lender is 16% and will be withheld by the borrower from the moment when the interest is paid. The abovementioned tax may be different where double tax treaty or EU regulation is applicable.

Where a lender is enforcing a security against a debtor (borower or guarantor) he is not liable for any tax on proceeds of such a claim, except where the lender is a natural person.

6.2 What tax incentives or other incentives are provided preferentially to foreign lenders? What taxes apply to foreign lenders with respect to their loans, mortgages or other security documents, either for the purposes of effectiveness or registration?

There are no tax incentives preferentially provided to foreign lenders.

With an *immovable mortgage*, the fee to be paid for its registration with the Land Book is composed of a fixed tax of RON 100 and a tax of 0.1% of the value of the secured receivable, acc. to Annex no. 1, point 2.3.3. of Order no. 39/2009 on the approval of tariffs for the services provided by the National Agency of Cadastre and Real Estate Advertising and its subordinated Units and authorisation fee for those who carry out specialised works of cadastre, geodesy and cartography.

With a *movable mortgage*, charges for signing the credit Agreement and the related guarantee in Electronic Archive for Secured Transactions are borne by customers.

Fees for guarantee notices were initially established in 2000, by art. 24 of GO 89/2000. The amount of taxes is updated by Government decision, depending on the official rate of inflation.

Thus, at present, the level of fees charged by Electronic Archive for Secured Transactions is of RON 67 for submitting an opinion.

6.3 Will any income of a foreign lender become taxable in your jurisdiction solely because of a loan to or guarantee and/or grant of security from a company in your jurisdiction?

A foreign lender in receipt of Romanian-source interest income would be liable to Romanian income tax, 222 and 223 (1) (b) of Romanian Fiscal Code except where double tax treaty or other EU regulations are applicable.

6.4 Will there be any other significant costs which would be incurred by foreign lenders in the grant of such loan/guarantee/security, such as notarial fees, etc.?

Except the cost for registration of the collateral security mentioned at question 6.2 above to create a valid mortgage over real estate, the agreement must be notarised, and notary fees can be quite significant, varying depending on the value of the secured amounts and the mechanism used for establishing the security. Where the loan agreement is not considered under its applicable law as being an executory title, the enforcement of the mortgages over real estate may raise problems.

The lenders will not be subject to such costs, whereas, according to the practice of the Romanian market, these costs are born by the borrower, nevertheless it is advisable that parties to reach to an agreement regarding the allocation of such costs.

6.5 Are there any adverse consequences to a company that is a borrower (such as under thin capitalisation principles) if some or all of the lenders are organised under the laws of a jurisdiction other than your own? Please disregard withholding tax concerns for purposes of this question.

No. However, on January 1st 2018, the applicable rules for deductibility of expenses were completely changed.

7 Judicial Enforcement

7.1 Will the courts in your jurisdiction recognise a governing law in a contract that is the law of another jurisdiction (a "foreign governing law")? Will courts in your jurisdiction enforce a contract that has a foreign governing law?

The Romanian Courts recognise the foreign law of a contract, but the internal legislation may raise some debates, in connection with this issue. In accordance with the Romanian Civil Procedural Code, in a case which has an extraneity element, the Court will apply the Romanian procedural regulation ("*forum regit processum*"), as a principle in accordance with art. 1088 Civil procedural Code. Nowadays, the majority of foreign civil international legislation is built in accordance with this principle, without admitting any waiver.

However, the qualification of an issue as being governed by the procedural rules or by substantial rules will be made in accordance with the internal legislation, excepting the legal entities that have no correspondence with Romanian bodies. Thus, the quality of the parties, the object and the scope of the claim will be set in accordance with the law that governs the merits of the dispute. The evidence and the evidence power of the document will be made in accordance with the law applicable to the Contract, whenever the law of the parties allows this.

In consequence, the Parties may choose any substantial law of the Agreement, but if they choose to commence legal proceedings in front of Romanian Courts, the Romanian Procedural laws will be applied. In the latest situation, the substantial law of the Agreement shall be used, excepting the aforementioned features.

Regarding a contract that has a foreign governing law, in accordance with EU Regulation no. 593/2008, on the Law applicable to Contractual obligations (Rome I) courts in Romania generally enforce such contracts, if these have jurisdiction for claims under such contract.

7.2 Will the courts in your jurisdiction recognise and enforce a judgment given against a company in New York courts or English courts (a "foreign judgment") without re-examination of the merits of the case?

In this case, a distinction between the English Courts and the Courts in USA (namely New York Courts) should be made. In accordance with the EU Council Regulation no. 1215/2012, on jurisdiction, enforcement of judgment in civil and commercial matters ("Regulation Brussels I recast), a ruling rendered in an EU Member State shall be recognised without any special proceedings in any other EU Member States, unless the recognition is challenged.

However, in accordance with art. 45 from the aforementioned Regulation, on the application of any interested party, the recognition of a judgment shall be refused: taking into consideration a few conditions stressed by this legal provision.

Regulation no. 1215 does not apply to judgments rendered by the NY Courts. In accordance with the Romanian Civil Procedural Code, foreign judgments are fully recognised in Romania (i) if they refer to the personal status of the citizens of the state where they were ruled, or (ii) if they were ruled in a third State first recognised in the state of citizenship of each party or, if recognition have been rendered on the basis of the law determined as applicable under the Romanian private international law, are not contrary to the public order of Romanian private international law and the right to defence has been fulfilled. The rulings other than the ones mentioned in the first paragraph, may be recognised in Romania in order to benefit of "*res judicata*" (claim preclusion), if the following conditions are met cumulatively: a) the judgment is final according to the law of the state where it was rendered; b) the court which ruled it had, under the law of the State of residence, jurisdiction to hold the proceedings without, however, being based exclusively on the defendant's presence or property not directly related to the dispute in the State in which that court is situated; or c) there is reciprocity regarding the effects of foreign judgments between Romania and the state of the court that ruled the judgment.

Also, if the judgment has been given in the absence of the party who has lost the case, it must also declare that the party concerned has been served in good time both with the summons for the substantive debate and with the referral of the court and that it was given the opportunity to defend itself and to appeal the decision.

Unless some prior conditions are met, the Court will not rule on the merits of the foreign ruling and will not proceed on amending it.

7.3 Assuming a company is in payment default under a loan agreement or a guarantee agreement and has no legal defence to payment, approximately how long would it take for a foreign lender to (a) assuming the answer to question 7.1 is yes, file a suit against the company in a court in your jurisdiction, obtain a judgment, and enforce the judgment against the assets of the company, and (b) assuming the answer to question 7.2 is yes, enforce a foreign judgment in a court in your jurisdiction against the assets of the company?

Firstly, we should make a distinction depending of the enforceable character of the agreement under discussion. If the contract is governed by Romanian law and the enforceable character is recognised, a claim submission won't be necessary and the contract shall be enforced in accordance with the Romanian Civil Procedural Code (as it will be stressed below). If the contract is governed by foreign law, an application in court shall be necessary, in order to obtain a ruling and afterwards enforce it.

A foreign company may submit an application in front of the Romanian Courts in order to obtain a favourable ruling against a debtor which is in payment default. This application may take six months to one year, depending on the circumstances of the case, considering that the debtor has no legal defence.

After the ruling becomes definitive and all the appeals are ruled, a foreign lender will follow the enforcement procedure in front of a bailiff. This procedure may also take three months to one year depending on the assets that are executed. A seizure on the bank accounts may solve the debt recovery earlier than the execution of a real estate or mobile goods (that require a more complex procedure).

For example, in case of real estate enforcement, the bailiff will organise a public auction in order to sell the asset and recover the enforced amounts. The Creditor may choose to adjudicate the real estate on behalf of its receivable, if its economic reasons are in this respect.

Regarding the mobile goods, depending on their specifications, their enforcement requires the presence of the Police authorities in accordance with art. 659 Romanian Civil Procedural Code. Also, the enforcement of such assets will be considered as being performed, only after the bailiff identifies the goods, which is rather difficult. The possession document gives the creditor the right over those assets.

We should stress that if the foreign lender holds a letter of guarantee (even issued by a foreign bank) against the Romanian debtor, this instrument shall be enforced immediately by the bank at the first demand of the creditor, in accordance with the Paris Publication no. 758, related to the execution of such autonomous instruments. The only requirement in this respect is to indicate to the bank the contractual provision that was breached by the Romanian company.

7.4 With respect to enforcing collateral security, are there any significant restrictions which may impact the timing and value of enforcement, such as (a) a requirement for a public auction, or (b) regulatory consents?

Regarding the enforcement of collateral securities, as mentioned above, this stage requires a procedure in front of a bailiff. After the registration of the enforcement submission, the bailiff shall request court approval for initiating the enforcement procedure. This approval is provided by art. 666 Romanian Civil Procedural Code. After the Courts grants this approval (the approval is based on form condition verifications), the executor will start the enforcement procedure: identify the debtor's assets (which are located in the bailiff's territorial division), transmit seizure letters to all the banks and try to identify if the debtor has mobile assets or real estate assets in the Land Book and with City Hall. Also, the bailiff may request Trade Registry information about the debtor's involvement in other companies, in order to seize these assets, also.

As mentioned at question 7.3, the real estate execution requires the organisation of a public auction, in accordance with the provisions of art. 846 Romanian Civil Procedural Code. The real estate selling advertisement will be published at the bailiff's office, at the City Hall where the asset is located and also at the executional Court. This advertisement is usually published in national newspapers, in order to insure an entire advertisement of the auction.

7.5 Do restrictions apply to foreign lenders in the event of (a) filing suit against a company in your jurisdiction, or (b) foreclosure on collateral security?

There are no specific restrictions applying to foreign lenders in case of submitting a court application against a company or foreclosure on collateral security.

It should, however, be noted that foreigners who submit claims in Romania should set a procedural headquarter in Romania for the communication of procedural documents (usually the lawyer's office). If they do not comply with this legal requirement, the Romanian Courts will communicate the procedural documentation by post and the post receipt submission will be considered the evidence of a legal summoning procedure.

Also, all foreign documentation submitted before the Romanian courts will be translated into Romanian language by an authorised translator.

7.6 Do the bankruptcy, reorganisation or similar laws in your jurisdiction provide for any kind of moratorium on enforcement of lender claims? If so, does the moratorium apply to the enforcement of collateral security?

According to the Romanian legislation from the date of the opening of the bankruptcy, reorganisation or similar proceedings, all judicial or extrajudicial claims against the insolvent/bankrupt debtor or any enforced execution proceedings are legally suspended. The main debt and all the penalties (contractual ones or legal interest) should be capitalised only by registering on the table of creditors. In this respect, the interested creditors may submit a registration petition to the judicial administrator/liquidator and in front of the insolvency court. This submission will show the amount of the receivable, its contractual and legal grounds. The judicial administrator/liquidator shall admit or dismiss the request of registration, depending on the grounds of the receivable. However, the creditor may challenge the liquidator/judicial administrator's decision in the insolvency Court.

The Romanian Insolvency Law stresses also that no interest, increase or penalty, collectively called 'accessories' will not be added to the receivables borne before the commencement of the insolvency procedure, excepting the situation of the guaranteed creditors (that hold a mortgage), which will be registered on the definitive Table of Creditors with the market value of the guarantee. This value will be set by a valuation report and in case the value resulting from the report will be higher than the initial amount registered on the table, the favourable difference will be distributed to the guaranteed creditor. This means that the Romanian legislation gives to the guaranteed creditors additional rights others than those applicable the rest of the creditors, participating at the insolvency procedure, in order to add securities to their guaranteed receivable.

Also, in case no reorganisation plan is confirmed, all the penalties, legal interest, additional expenses, borne after the initiation of the bankruptcy procedure will be paid in accordance with the contractual documentation and the payment chart of the reorganisation plan. In case the reorganisation plan shall fail, all the accessories will be owed by the debtor until the initiation of the insolvency procedure.

7.7 Will the courts in your jurisdiction recognise and enforce an arbitral award given against the company without re-examination of the merits?

According to the Romanian Civil Procedure Code, art. 1125, a foreign arbitral award shall be enforced in Romania if the dispute is not contrary to the public policy of international private law. The procedure is provided by arts. 1124–1134, of the Romanian Procedural Code.

At the same time, the Romanian Civil Procedure Code (art. 1065) stipulates the possibility of choosing the most favourable law ("*mitior lex*"): The New York Convention; or the Romanian Civil Procedure Code.

In other terms, the grounds for dismissing the recognition or the enforcement of the awards are identical in both normative acts because the Romanian Civil Procedure Code takes over the provisions of art. 5 of the New York Convention.

According to the Civil Procedure Code, in order to enforce the foreign arbitral awards, an application approval of the execution shall be submitted to the Tribunal, attaching the said award the arbitral convention translated in Romanian and over-certified by the Consulate. There is no requirement of a prior exequatur decision, in order to address an application for declaration of enforceability. We should also stress that the aforementioned procedure is also called the exequatur procedure but this does not imply the involvement of a judicial executor (bailiff). This could have led to a confusion of terms.

Anyway, the Romanian Court shall only verify some prior procedural issues and will not argue the merits of the arbitral award.

8 Bankruptcy Proceedings

8.1 How does a bankruptcy proceeding in respect of a company affect the ability of a lender to enforce its rights as a secured party over the collateral security?

According to the Insolvency Law, from the opening date of the insolvency proceedings, all judicial, extrajudicial actions or enforcement measures for recovering any receivables against the debtor's assets are suspended.

The lenders can recover their claims, but only within the insolvency proceedings by submitting an application for receivables acceptance with the competent court and abiding by special rules provided under this procedure.

However, under the security held, the lender becomes a secured creditor and has certain preferential rights in the insolvency proceedings for the satisfaction of his claim.

8.2 Are there any preference periods, clawback rights or other preferential creditors' rights (e.g., tax debts, employees' claims) with respect to the security?

According to the insolvency law, certain claims have priority over a creditor's secured claim, in the following order:

- Taxes, stamps and any other fees incurred with respect to the sale of the respective secured asset.
- Receivables of utility services providers arising after the opening of the insolvency proceedings.
- Remuneration of the judicial administrator.
- Receivables of other secured creditors relating to the same secured asset if these arose during the insolvency proceedings.

Creditors granted with security over an asset have priority over that asset or the equivalent value of that asset, with the observance of the aforementioned limitations.

If, by selling the asset, the amounts do not cover the value of the debt, for the difference in value, the creditors have an unsecured receivable that comes in competition with other receivables, in the following order:

- Fees, stamps or any other expenses related to the insolvency procedure.
- Claims resulting from financing granted during the insolvency proceeding.
- Labour-related claims.
- Claims arising from the debtor's activity after the opening of the insolvency proceedings.
- Fiscal claims.
- Receivables representing amounts owed by the debtor to third parties under alimony obligations.
- Receivables representing amounts established by the syndic-judge for supporting the debtor and their family, if the debtor is a natural person.

- Receivables representing banking loans, with accrued expenses and interest, resulting from product delivery, services or rents.
- Other unsecured claims.
- Subordinated claims, in the following order:
  - receivables of third parties that have acquired or sub-acquired in bad faith the debtor's goods, as well as the loans provided to the legal person debtor by a shareholder holding at least 10% of the share capital or voting rights in the general meeting of shareholders or by a member of the economic interest group; and
  - receivables resulting from gratuitous acts.

Where more creditors are granted the same security interest over the same asset, the priority is determined by reference to the moment the publicity formalities were performed (that is, registration with the Land Book or with the Electronic Archive for Secured Transactions).

Therefore, on registration with the relevant public registry, the respective security interest ranks before the claims of any unsecured creditors and of the creditors holding subsequently registered security interests in respect of the same asset.

Where two or more creditors have the same priority rank, the sums are distributed proportionally by reference to the sum relating to the receivable of each such creditor.

8.3 Are there any entities that are excluded from bankruptcy proceedings and, if so, what is the applicable legislation?

According to the law, the insolvency procedure does not apply to public institutions, individuals, professionals who practice liberal professions (e.g. lawyers, doctors, architects, assistants, executors, experts, pharmacists) and to professionals who are subject to special provisions regarding their insolvency regime.

Also, the insolvency procedure is not applicable to the pre-university and university education units and institutions, as well as to the entities stipulated in art. 7 of the Government Ordinance no. 57/2002 on scientific research and technological development.

Persons performing liberal professions are liable civilly and disciplinary for the damages caused in the exercise of their profession, according to special normative acts that regulate organisation and exercise of the respective profession.

Government Emergency Ordinance no. 46/2013 on the financial crisis and the insolvency of territorial-administrative units establishes the general framework and collective procedures for covering liabilities of the administrative-territorial units in the financial crisis or in insolvency.

Also, starting with January 1st, 2018, the Insolvency Law of Individuals (personal bankruptcy) entered into force.

8.4 Are there any processes other than court proceedings that are available to a creditor to seize the assets of a company in an enforcement?

In our legal system, the only creditors who can seize the assets of a company without court intervention are public institutions, the most common situation being the seizure insured by the Public Finance Administration for the recovery of tax liabilities owed by taxpayers to the state.

However, the Civil Code provides certain alternative enforcement measures for the creditors, such as: a) the possibility to temporarily take over mortgaged assets, for administration purposes, until the claims are satisfied; and b) the possibility to appropriate the asset in order to extinguish the receivable, under certain conditions provided by the law.

Also, if the lender holds an enforcement title as defined by the Romanian Law (exchange bills, promissory notes, credit agreements under Romanian substantial law), it can easily be enforced, since the enforcement court intervention is purely a formal one, the Court having the sole obligation to endorse forced execution in a non-contentious proceeding. After the writ of execution is given, the bailiff can take any and all the necessary measures for seizing the company's assets.

9 Jurisdiction and Waiver of Immunity

9.1 Is a party's submission to a foreign jurisdiction legally binding and enforceable under the laws of your jurisdiction?

In Romania, a contractual choice of forum is generally permissible and legally binding. Certain form requirements may apply. However, the choice of forum is not valid if it leads to the abusive deprivation of the protection provided by a Romanian court to one of the parties. Also, if other courts have exclusive jurisdiction, no choice of forum is permissible.

9.2 Is a party's waiver of sovereign immunity legally binding and enforceable under the laws of your jurisdiction?

A waiver of sovereign immunity from jurisdiction is generally legally binding, on the condition that the waiver is authorised by law or by international conventions to which Romania is a party. Also, the legal entities governed by public law having economic activities in their field of activity are able to conclude arbitration agreements, unless the law or their act of incorporation provides otherwise.

10 Licensing

10.1 What are the licensing and other eligibility requirements in your jurisdiction for lenders to a company in your jurisdiction, if any? Are these licensing and eligibility requirements different for a "foreign" lender (i.e. a lender that is not located in your jurisdiction)? In connection with any such requirements, is a distinction made under the laws of your jurisdiction between a lender that is a bank *versus* a lender that is a non-bank? If there are such requirements in your jurisdiction, what are the consequences for a lender that has not satisfied such requirements but has nonetheless made a loan to a company in your jurisdiction? What are the licensing and other eligibility requirements in your jurisdiction for an agent under a syndicated facility for lenders to a company in your jurisdiction?

In Romania, a company could become a lender following the authorisation of its activity by the National Bank of Romania (NBR). An entity which carries out banking activities on a regular basis in Romania must either be duly licensed as a creditor institution or as a financing company, or non-banking financial institution.

Also, a company can grant loans to other company, occasionally, but without doing it with professional title. In this case, the Romanian law provides that these companies are not subject to the legal provisions on credit institutions.

A creditor institution must have its own funds or a level of initial share capital that cannot be less than EUR 5 million. During the operation of the creditor company, the share capital must not fall below this level, otherwise the NBR may close its activity.

In order to obtain the approval, the applicants shall submit to the NBR a plan of activity, including the types of activities to be carried out and the organisational structure and showing the ability to achieve their objectives under a prudent and healthy banking practice.

Regarding the structure of the creditor, the company must have a rigorous management framework which includes processes to identify, manage, monitor and report the risks to which it is or might be exposed, adequate internal control mechanisms, including administrative and accounting procedures, rigorous policies and remuneration practices, which promote and agree with healthy and effective risk management.

The management of the creditor shall be provided by, at least, two people with good reputations and adequate banking experience.

The licensing and eligibility requirements for creditors in Romania are also applicable to credit institutions in other countries, with the following specifications:

Credit institutions authorised and supervised by the competent authority of **a Member State** may be considered as creditors **by the establishment of branches** or **by the provision of services directly**, if those activities are covered by the authorisation granted by the competent authority of the country of origin.

A credit institution from another Member State may carry out activities directly in Romania, pursuant to European Directive no. 2013/36/EU and European Regulation no. 575/2013, if authorised by the competent authority of the Member State.

A credit institution authorised in a Member State, may set up a branch in Romania or provide services directly on the basis of the notification sent to the National Bank of Romania by the competent authority of the country of origin.

A credit institution in **a third country** can only operate in Romania by setting up a branch in Romania authorised by NBR. The initial capital of the branch may not be lower than the EUR 5 million.

In Romania, both non-banking financial institutions (NFI) and banks are regulated. The main differences are as follows:

a) NFI may grant credits but cannot attract deposits. This last activity can only be done by credit institutions.

b) NFIs are divided into two categories: NFIs registered in the Special Register of the National Bank; and those entered only in the General Register. In order to be part of the first category, non-bank financial institutions must meet certain capital criteria, the amount of credits granted, total assets.

c) In order to receive an authorisation from the NBR, a bank must prove that it has an initial minimum capital of EUR 5 million.

d) A non-bank financial institution shall have a share capital of only EUR 200,000, or EUR 3 million in the case of NFIs granting mortgages.

Non-compliance with such banking rules may lead to the criminal liability. According to the Romanian law, it constitutes an offence and it is punished by imprisonment from one to five years.

The Romanian legislation does not contain provisions on syndicated facilities.

11 Other Matters

11.1 Are there any other material considerations which should be taken into account by lenders when participating in financings in your jurisdiction?

Yes, there are any other material which should be taken into account by lenders when they are participating in financings and this is the establishment of personal insolvency for Romanian individuals.

The Personal Insolvency Law was inspired by the legislation applicable to the insolvency of natural persons in the EU and aims to offer Romanian citizens similar rights (and obligations) as the majority EU Member States recognise when their EU citizens declare insolvency.

The Personal Insolvency Law creates the legal framework for insolvency of individuals, i.e. a procedure of declaring insolvency of individuals aimed at offering possibilities to natural persons to (partially) clean their debts, under certain conditions set out by the Personal Insolvency Law. There are three different insolvency procedures, applicable depending on the particular situation of the individual:

- insolvency procedure based on a debt repayment plan (upon request of the individual);
- insolvency procedure based on asset liquidation (either at the request of the individual or of his/her creditors); and
- simplified insolvency procedure (applicable to individuals who lost over 50 per cent of their work capacity or qualify for standard retirement).

The relevant bodies which will apply the insolvency procedure for individuals are the insolvency commission (a new administrative body which will be established for the purposes of the personal insolvency of individuals), the insolvency administrator or liquidator and the courts.

While the banking industry is generally fine with the compromise solution enacted under the Personal Insolvency Law, it is still to be seen to what extent individuals will try to abuse the newly introduced benefits.

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Valentin Trofin holds a Bachelor Law Degree (1998) and a Master Degree in International Commercial Arbitration (2014), both from Law School of University of Bucharest. He also holds a Diploma in International Commercial Arbitration from Chartered Institute of Arbitrators (2014). Valentin Trofin is a Ph.D. candidate at the Doctoral Law School of Titu Maiorescu University.

Valentin Trofin was admitted to the Bucharest Bas Association (1999), The National Association of Authorized Romanian Valuers (2003) and to the Romanian National Union of the Insolvency Practitioners (2010). He was admitted to the Fellowship of Chartered Institute of Arbitrators, being a member of the European Branch's Executive Comitee. Also, he is member of International Bar Association, Society of Construction Law (UK), Romanian Society of Construction Law and founding member and Treasurer of Bucharest Arbitration Network.

Valentin Trofin is recognised as a leading practitioner in the construction industry and real estate development, mergers & acquisitions and international arbitration. Valentin Trofin's multidisciplinary qualification as a lawyer, real estate appraiser and business appraiser provides him with quick and better business understanding followed by the ability to render innovative solutions for each case.

Valentin Trofin's business acumen, passion for technicalities and details and great negotiation skills makes him as a "most needed person" for all complex cases. When he is assigned to draft a bespoke agreement, his outstanding drafting skills will deliver a well-structured agreement with a combination of plain and minimum legal language resulting in an easy to understand agreement smartly dealing with all the risks involved. These skills combined with his business understanding is long tested and in every case the results were the same: no disputes were referred to courts for resolution.

Mihaela Spiridon

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Associate, Trofin & Asociații.

Mihaela Spiridon has been an Associate with Trofin & Asociații since 2016.

Mihaela Spiridon graduated from University of Bucharest – Faculty of Law in 2014, holds a Master's Degree in Business Law from Nicolae Titulescu University and is also a speaker of English and French and was admitted to the Bucharest Bar Association in 2015.

Her work includes providing general advisory assistance regarding various business aspects and she also works as part of the internal team in an investment arbitration case handled by the International Centre for Settlement of Investment Disputes of Washington involving major privatisation, insurance/reinsurance and insolvency issues.

Since joining the team, Mihaela has been involved in a variety of transactional and non-transactional real estate and commercial matters, including legal due diligence investigations, construction projects, preparing and negotiating various agreements.

She has also been involved in drafting and negotiating finance documents and the corresponding security packages, as well as due diligence analyses in this respect. On this note, she advised a consortium of investors in relation to the potential participation on the development of a real-estate project consisting of building and selling a number of buildings. She also advised and assisted a construction company in the acquisition of a land plot of approx. 46,000 sq. m. in Romania, in view of a future office and storage development thereon.

Her experience covers land acquisitions, urbanism and construction matters, including FIDIC contracts, leasing and operational aspects for office. In addition, Mihaela is actively assisting clients on diverse corporate housekeeping operations and on general contracts and commercial legal aspects.

She also provided legal advice to economic operators acting as bidders in public procurement procedures, in connection with the submission of complaints and defence before the National Challenge Resolution Council, supplying legal assistance and representation during the settlement of complaints.

TROFIN & ASOCIAȚII
BRAINMADE LEGAL SOLUTIONS

Trofin & Asociații was founded in March 2003 as a boutique law firm specialised in construction industry and corporate law. Immediately after that, in 2004 the firm became well known for its professionalism and leading voice in construction projects and real estate development. Since then, their practice has increased and they are now experienced in mergers and acquisitions, intellectual property, employment law, real estate development, insurance claims, banking & finance, public procurement, international commercial or investment arbitration and domestic litigation.

Since 2003, Trofin & Asociații had been involved in more than 50 construction or real estate development projects with values ranging from Euro 10 million to Euro 70 million.

Since 2007, the firm was involved in many cross-border transactions especially in Turkey, Russian Federation, North Africa and Republic of Moldova. The firm has a great deal of experience in dispute resolution, including international commercial arbitration being involved in more than 30 cases of domestic and international arbitration.

Every year the firm's dispute resolution practice is involved in representing clients in more than 70 litigation and arbitration cases on average, with a peak in 2009–2012 when they were involved in more than 200 litigation and arbitration cases each year.

In 2016, the Romanian Government appointed them, as co-counsel, to represent Romania in an investment arbitration in a dispute of hundreds of millions of Euros under the rules of ICSID Washington D.C. (U.S.A.).

The lawyers in our firm have a strong academic background being frequent speakers at workshops and international conferences.

Russia

Grigory Marinichev

Morgan, Lewis & Bockius LLP

Alexey Chertov

1 Overview

1.1 What are the main trends/significant developments in the lending markets in your jurisdiction?

One of the major trends in the Russian lending market is the bailout of several major private Russian banks, including Promsvyazbank and Otkritie, which were taken over by the state.

Russian state banks, such as Sberbank, VTB and Gazprombank, are increasing their shares in the lending markets, including prepayment markets. The prepayment markets have extended well beyond the oil market to electricity, copper, aluminium, gold, coal, and other goods during recent years.

Increasing number of lending transactions are governed by Russian law. In late December 2017, the Russian State Duma passed a law specifically addressing the issues of syndication and relationships of a syndicate participants – the Federal Law No. 486 – FZ dated 31 December 2017 "On syndicate facility (loan) and on amendments to certain legislative acts of the Russian Federation" (the **Syndication Law**). The Syndication Law became effective on 1 February 2018. Importantly, the Syndication Law addresses the issues of syndication and the role of facility arrangers and facility agents (managers).

1.2 What are some significant lending transactions that have taken place in your jurisdiction in recent years?

Significant finance transactions in 2017 include, among others:

- a RUB 600 billion placement of Rosneft bonds;
- a USD 1 billion five-year pre-export financing of SUEK organised by a group of 19 international and domestic lenders;
- a USD 750 million financing of EuroChem Group AG organised by a syndicate of banks including UniCredit Bank AG, London branch, as agent; and
- a USD 850 million pre-export financing of Uralkali. Coordinating Mandated Lead Arrangers and Bookrunners of the pre-export finance facility were Commerzbank AG, Credit Agricole Corporate and Investment Bank, ING Bank N.V., Natixis, PJSC Rosbank/Societe Generale Corporate & Investment Bank, and AO UniCredit Bank.

2 Guarantees

2.1 Can a company guarantee borrowings of one or more other members of its corporate group (see below for questions relating to fraudulent transfer/financial assistance)?

Generally, there are no restrictions to provision of guarantees or sureties by a Russian company in favour of members of its group. If a guarantee or surety constitutes a "major" or "interested party" transaction, it may be subject to certain corporate consents (notifications).

2.2 Are there enforceability or other concerns (such as director liability) if only a disproportionately small (or no) benefit to the guaranteeing/securing company can be shown?

Any transaction, including a guarantee or surety, may be challenged by the company and, in certain cases, by its shareholders or members of the board if such transaction is entered into to the detriment of the company and the counterparty was aware about such circumstances.

Also, a director of a Russian company shall generally act reasonably and in good faith and in the best interest of the company. If such obligations are breached, the directors may be sued for losses caused to the company.

In case of insolvency of a company, a guarantee or surety may be challenged if such transaction is aimed at a violation of creditors' rights or constitutes a preferential transaction. Directors and controlling persons of a company may be subject to "subsidiary liability" if the insolvency occurred as a result of their actions.

2.3 Is lack of corporate power an issue?

Subject to certain exceptions, Russian companies can enter into any lawful transactions. In the meantime, the powers of a director may be limited by the company's charter. In certain cases, a guarantee or surety may require consent of (notification to) the shareholders (participants) or the board of directors if it constitutes a "major" (i.e., a transaction amounting to 25% or more of the company's assets) or an "interested party" transaction.

2.4 Are any governmental or other consents or filings, or other formalities (such as shareholder approval), required?

Generally, no governmental consents or filing are required in respect of guarantees or sureties. As described in question 2.3, a guarantee or surety may require consent of the shareholders (participants) or the board of directors if it constitutes a "major" or "interested party" transaction for the company and in other cases stipulated by the company's charter.

2.5 Are net worth, solvency or similar limitations imposed on the amount of a guarantee?

Generally, there are no such limitations. However, if the value of the transaction exceeds certain thresholds (such as 25% of the company's assets), this may be taken into consideration if the company's transaction is contested in the course of the company's insolvency.

2.6 Are there any exchange control or similar obstacles to enforcement of a guarantee?

There are generally no such obstacles other than insolvency of a company. In order for a company to make certain payments to a foreign lender in a foreign currency under the guarantee or surety, the company may be required to file with a Russian authorised bank certain documents in support of any such payment (including a transaction passport ("*паспорт сделки*")). Such filing is required to be made as a condition to a payment transfer rather than to the entry into the underlying transaction. Such requirement is of an administrative nature and does not restrict or affect the company's obligation to make payments under the guarantee or surety. Starting from 1 March 2018, in accordance with new amendments, the filing of a transaction passport with a Russian authorised bank shall no longer be required. Instead, the contract will have to be recorded with such bank.

3 Collateral Security

3.1 What types of collateral are available to secure lending obligations?

Russian law allows using various types of collateral including pledge of immovable property (mortgage), pledge of equipment, pledge of rights under bank accounts, pledge of goods in turnover, pledge over shares and participatory interest and pledge over receivables.

3.2 Is it possible to give asset security by means of a general security agreement or is an agreement required in relation to each type of asset? Briefly, what is the procedure?

Russian law generally allows extending the pledge to "all assets" of the company. The respective pledge agreement shall be made in written form. In the meantime, it is unlikely that a pledge created by such a pledge agreement would automatically extend to certain types of assets such as rights under bank accounts, immovable assets (mortgage), participatory interest in limited liability companies or shares in joint stock companies since pledges over such assets are subject to registration/notarisation or other specific formalities.

3.3 Can collateral security be taken over real property (land), plant, machinery and equipment? Briefly, what is the procedure?

Security over immovable property (land, buildings, etc.) can be taken by way of mortgage. The mortgage agreement shall be made in written form. The mortgage shall be registered in the Unified State Register of Immovable Property ("*Единый государственный реестр недвижимости*"). Security over machinery and equipment is usually taken by entering into a pledge of movables. The pledge of machinery and equipment can be notified to the register of notices on pledges maintained by the notaries. Such notification is not mandatory and is not required for a pledge to be effective. However, the notification makes the pledge public and third parties are deemed notified about such pledge. This is particularly important in case of a dispute in respect of the priority of pledges created over the same property.

3.4 Can collateral security be taken over receivables? Briefly, what is the procedure? Are debtors required to be notified of the security?

Yes, such security is usually taken by way of a pledge over receivables. The debtor shall be notified about the pledge of receivables. Consent of the debtor is generally not required unless otherwise provided by the underlying contract.

3.5 Can collateral security be taken over cash deposited in bank accounts? Briefly, what is the procedure?

Such security is usually done by way of a pledge of rights under bank accounts. The Russian Supreme Court has recently supported a view that a pledge of rights under a bank account is possible only in respect of specific pledge accounts ("*залоговые счета*"), which means that there is substantial risk that a pledge of rights in respect of an ordinary bank account may be unenforceable. It is impossible to bypass this rule by changing the status of an ordinary bank account to the specific pledge accounts. A new pledge account must be opened for this purpose. A pledge of rights under a bank account is created from the moment when the respective account bank is notified about the pledge. However, if the account bank is the pledgee, the pledge will be created from the date of the pledge agreement.

3.6 Can collateral security be taken over shares in companies incorporated in your jurisdiction? Are the shares in certificated form? Can such security validly be granted under a New York or English law governed document? Briefly, what is the procedure?

Russian law makes a distinction between shares in joint stock companies and participatory interests in limited liability companies. Both can serve as collateral and both are in a non-documentary form.

In respect of the participatory interests, a pledgor must obtain the prior consent of a majority of participants in the limited liability company if the pledge is made in favour of a third party. A participatory interest pledge agreement must be made in written form and notarised. A pledge of participatory interest is deemed to be created from the moment of its registration in the Unified State Register of Legal Entities.

In contrast with a participation interest pledge, notarisation of a share pledge is possible but not mandatory. No consent of other shareholders is required. A share pledge must be registered in the shareholders' register or a depositary.

Pledges of participatory interests and shares are usually governed by Russian law. New York and English law may also be used in practice, but enforcement of such pledges may be more complicated.

3.7 Can security be taken over inventory? Briefly, what is the procedure?

Russian law recognises the pledge of inventory (pledge of goods in turnover). The subject matter of a pledge of goods in turnover can be determined by specifying the generic features of the goods and their location (e.g. goods in certain premises).

3.8 Can a company grant a security interest in order to secure its obligations (i) as a borrower under a credit facility, and (ii) as a guarantor of the obligations of other borrowers and/or guarantors of obligations under a credit facility (see below for questions relating to the giving of guarantees and financial assistance)?

Yes, both options are possible as long as the required corporate consents (if any) are obtained.

3.9 What are the notarisation, registration, stamp duty and other fees (whether related to property value or otherwise) in relation to security over different types of assets?

Any pledge agreement shall be made in written form. Notarisation of a pledge of participatory agreement is mandatory, while notarisation of pledges of other types of assets is possible but, as a rule, not mandatory. However, out-of-court enforcement of the pledged assets by way of notarial endorsement is only possible if the agreement is notarised.

The amount of notary fees depends on the amount of the secured obligation and whether the notarisation is mandatory. If the notarisation is mandatory, the amount of the notary fee cannot exceed RUB 150,000. If the notarisation is not mandatory, this amount cannot exceed RUB 500,000.

Pledges of most assets (other than immovable property, shares, participatory interests, rights under bank accounts and pledges of other assets, transfers of rights in respect of which are subject to mandatory registration) can be notified to the register of notices on pledges maintained by the notaries. Such notification is not mandatory and is not required for the validity of a pledge. However, the notification makes the pledge public and third persons are deemed notified about such pledge. This is particularly important in case of a dispute in respect of the priority of pledges. The fees in connection with registration of such notices are nominal (RUB 600 per notice).

The fees for registration of mortgage by legal entities in the Unified State Register of Immovable Property are RUB 4,000.

No stamp duties are payable as a matter of Russian law.

3.10 Do the filing, notification or registration requirements in relation to security over different types of assets involve a significant amount of time or expense?

The statutory term for registration of a mortgage is up to five business days, but in practice sometimes takes longer.

Notarisation of a participatory interest pledge and registration of the respective pledge in the Unified State Register of Legal Entities usually takes 7–15 days. Foreign pledgors and pledgees must collect and submit to the notary a set of notarised and apostilled corporate and other documents, which often takes some additional time.

Notices regarding pledges of movable property are submitted by the notaries and can be done within 1–2 hours.

Registration and notary fees are described in more detail in question 3.9.

3.11 Are any regulatory or similar consents required with respect to the creation of security?

Regulatory or similar consents are generally not required with respect to creation of security unless the rights of third parties are involved. In certain cases, corporate consents (notifications) may be required if the pledge agreement constitutes a "major" or "interested party" transaction.

3.12 If the borrowings to be secured are under a revolving credit facility, are there any special priority or other concerns?

Russian law previously required having a detailed description of the secured obligations, which created complications in instances when collateral secured the revolving facilities. At the moment, Russian law is far more flexible in respect of the requirement to describe the secured obligations, and expressly provides that the pledge may secure future obligations, so in our view the previous priority concerns in respect of a security relating to revolving facilities is less likely to be an issue at the moment.

3.13 Are there particular documentary or execution requirements (notarisation, execution under power of attorney, counterparts, deeds)?

Please refer to question 3.9 in respect of the pledge agreements which require notarisation. Execution of contracts by means of electronic communication is allowed as long as such execution makes it possible to determine that the document is sent by the relevant party.

4 Financial Assistance

4.1 Are there prohibitions or restrictions on the ability of a company to guarantee and/or give security to support borrowings incurred to finance or refinance the direct or indirect acquisition of: (a) shares of the company; (b) shares of any company which directly or indirectly owns shares in the company; or (c) shares in a sister subsidiary?

The financial assistance restrictions like the ones which exist in Germany and certain other jurisdictions do not exist in Russia. In the meantime, such guarantee or security may in certain cases require corporate consent. Please also refer to question 2.4 for further details.

5 Syndicated Lending/Agency/Trustee/ Transfers

5.1 Will your jurisdiction recognise the role of an agent or trustee and allow the agent or trustee (rather than each lender acting separately) to enforce the loan documentation and collateral security and to apply the proceeds from the collateral to the claims of all the lenders?

Russian law does not currently recognise trustee relationship, which is common in English law. In the meantime, the Russian Civil Code now contains provisions allowing the creditors to enter into a pledge management agreement and appoint a "pledge manager" to act on behalf of several creditors in connection with the pledge. The pledge management agreement may contemplate payment of a fee to the pledge manager. The pledge manager shall act in the best interest of the creditors. The proceeds received by the pledge manager in connection with the pledge become the common property of the creditors unless the pledge management agreement provides otherwise.

The Syndication Law introduced the role of a facility agent referred to as the "facility manager". The functions of the facility manager can be carried out by a credit organisation, the state corporation Vnesheconombank, a foreign bank or an international finance organisation.

Facility managers shall run the register of the syndicate participants and record all amounts granted to the borrower. Facility managers shall act on behalf of lenders in their relationship with the borrower, mainly, collecting funds under facility, including interest amounts and other payments and providing relevant documents and information to lenders and security arrangers.

5.2 If an agent or trustee is not recognised in your jurisdiction, is an alternative mechanism available to achieve the effect referred to above which would allow one party to enforce claims on behalf of all the lenders so that individual lenders do not need to enforce their security separately?

Please refer to the answer to question 5.1.

5.3 Assume a loan is made to a company organised under the laws of your jurisdiction and guaranteed by a guarantor organised under the laws of your jurisdiction. If such loan is transferred by Lender A to Lender B, are there any special requirements necessary to make the loan and guarantee enforceable by Lender B?

Rights under loan agreements and guarantees governed by Russian law are usually transferred by way of assignment. The consent of the debtor is not required unless otherwise provided by the loan agreement or guarantee. If the consent is required by the loan agreement or guarantee but is not obtained, the assignment would still be valid but the initial creditor would be liable for breach of contract.

6 Withholding, Stamp and Other Taxes; Notarial and Other Costs

6.1 Are there any requirements to deduct or withhold tax from (a) interest payable on loans made to domestic or foreign lenders, or (b) the proceeds of a claim under a guarantee or the proceeds of enforcing security?

Interest payable on loans made by Russian lenders (lenders incorporated in Russia and foreign lenders which have permanent establishment in Russia) is generally subject to Russian income tax at a rate of 20%. The same rate applies to a foreign lender receiving their income from interest on loans at a source in Russia. In this case, taxable income is withheld by the borrower.

Proceeds under a guarantee are subject to the same rules as taxable income under loan agreements.

6.2 What tax incentives or other incentives are provided preferentially to foreign lenders? What taxes apply to foreign lenders with respect to their loans, mortgages or other security documents, either for the purposes of effectiveness or registration?

The general approach under Russian law is that foreign lenders are subject to the same rules as Russian lenders. However, international tax treaties provide certain specific tax exemptions or reductions. In order to enjoy such exemptions or reductions, the foreign lender must provide the borrower with the tax residence certificate issued by the relevant competent tax authority in that lender's jurisdiction of residence confirming that the lender is tax resident in such tax jurisdiction for the purposes of the relevant tax treaty. Such certificates are usually provided before the first payment of interest under the loan and thereafter annually until the full repayment of the loan.

6.3 Will any income of a foreign lender become taxable in your jurisdiction solely because of a loan to or guarantee and/or grant of security from a company in your jurisdiction?

Please refer to questions 6.1 and 6.2.

6.4 Will there be any other significant costs which would be incurred by foreign lenders in the grant of such loan/guarantee/security, such as notarial fees, etc.?

Notarisation of loan agreements and guarantees is not mandatory in Russia. No registration of loan agreements or guarantees is required in Russia. Notarial and other fees applicable to security are described in question 3.9.

6.5 Are there any adverse consequences to a company that is a borrower (such as under thin capitalisation principles) if some or all of the lenders are organised under the laws of a jurisdiction other than your own? Please disregard withholding tax concerns for purposes of this question.

A loan from a foreign entity can be considered as "controlled indebtedness" if such loan is provided or secured by a foreign entity (or a Russian entity controlled by such foreign entity).

If the amount of such "controlled indebtedness" exceeds the amount of a borrower's own equity by more than three times, the interest paid on such loan can only be considered as expenses subject to certain limits. The remaining interest is considered as dividends paid to a foreign entity and is subject to 15% taxation (unless an international treaty allows specific tax exemptions or reductions).

7 Judicial Enforcement

7.1 Will the courts in your jurisdiction recognise a governing law in a contract that is the law of another jurisdiction (a "foreign governing law")? Will courts in your jurisdiction enforce a contract that has a foreign governing law?

Russian courts should generally recognise (and enforce) foreign governing law, provided that such laws do not conflict with Russian public policy or specific mandatory rules ("*нормы непосредственного применения*") of the laws of the Russian Federation. The concepts of public policy and specific mandatory rules are not defined in the laws of the Russian Federation and, therefore, are open to interpretation by Russian courts. Furthermore, a Russian court will apply foreign law as the law of the contract only provided that such Russian court has properly established the content of the relevant foreign law in relation to the issues considered by it. If a Russian court is not in a position to establish the content of foreign law within a reasonable period of time, it is entitled to apply the laws of the Russian Federation. In any event, the laws of the Russian Federation will apply as to the matters of evidence and procedure.

7.2 Will the courts in your jurisdiction recognise and enforce a judgment given against a company in New York courts or English courts (a "foreign judgment") without re-examination of the merits of the case?

Judgments of foreign courts may be enforced in the Russian Federation only if there is a treaty between the Russian Federation and the relevant foreign jurisdiction on the mutual recognition and enforcement of court judgments or, in the absence of such a treaty, on the basis of reciprocity. As of today, no such treaty is currently in force and no formal legal procedures for reciprocal enforcement of court judgments exist between the Russian Federation and England or Russian Federation and the United States of America, which means that the risk that judgment of an English or a New York court could not be recognised and enforced in Russia is substantial.

We are aware of some cases in which judgments of foreign courts were successfully recognised and enforced in Russia (the claimant usually provided evidence, including an expert opinion, that, under similar circumstances, a judgment of a Russian court would be enforceable in the respective foreign jurisdiction), but we are also aware of a number of cases in which enforcement of foreign court judgments was denied by Russian courts.

7.3 Assuming a company is in payment default under a loan agreement or a guarantee agreement and has no legal defence to payment, approximately how long would it take for a foreign lender to (a) assuming the answer to question 7.1 is yes, file a suit against the company in a court in your jurisdiction, obtain a judgment, and enforce the judgment against the assets of the company, and (b) assuming the answer to question 7.2 is yes, enforce a foreign judgment in a court in your jurisdiction against the assets of the company?

In general, a claim under a loan would normally be enforced in Russia upon a court order.

(a) Obtaining a final and binding judgment of the arbitrazh (commercial) court of first instance usually takes three to four months. The proceeding at the court of appeal usually takes from two to three months. Enforcement of a Russian court judgment should normally be completed within two months from the day of the commencement of the enforcement proceedings, although sometimes it takes much longer due to various delays.

(b) Enforcement of a foreign judgment should technically be completed within one month, but may in practice take several months.

A bad faith debtor may substantially delay the court or enforcement proceedings by means of raising various objections in respect of the substance of foreign law as well as various procedural objections.

Under Russian law it is also possible to collect debt through an out-of-court procedure under a notary's executory endorsement made on a copy of the loan agreement. An out-of-court order of debt collection may be exercised in case the loan agreement specifically provide for such enforcement option. The lender must notify the borrower at least 14 days prior to the intended collection of debt. In the absence of established court practice it is unclear whether the out-of-court procedure can also be used by foreign banks.

7.4 With respect to enforcing collateral security, are there any significant restrictions which may impact the timing and value of enforcement, such as (a) a requirement for a public auction, or (b) regulatory consents?

Enforcement in respect of most types of pledges assets is possible both in court and out of court. In most cases, out-of-court enforcement of the pledged assets requires notarial endorsement and such endorsement is only allowed if the pledge agreement is notarised.

Out-of-court enforcement may be exercised by the following methods: public auction; private auction; retention; and private sale without an auction. Out-of-court enforcement and the particular method of enforcement shall be provided by the pledge agreement. The methods of the court enforcement are public auction, retention and private sale without an auction. Acquisition of shares in certain companies through an enforcement procedure may require certain antimonopoly and similar consents.

7.5 Do restrictions apply to foreign lenders in the event of (a) filing suit against a company in your jurisdiction, or (b) foreclosure on collateral security?

Foreign creditors should generally be treated in the same way as Russian creditors in terms of filings of suits and enforcement of the collateral security. All documents filed to the Russian arbitrazh (commercial) courts must be in Russian; any documentation in any other language must be translated into Russian, notarised and apostilled, unless originally made in Russian.

7.6 Do the bankruptcy, reorganisation or similar laws in your jurisdiction provide for any kind of moratorium on enforcement of lender claims? If so, does the moratorium apply to the enforcement of collateral security?

There is a general moratorium on enforcement of lenders monetary claims since introduction of the supervision procedure (first insolvency stage). Creditors are not entitled to enforce collateral security during the supervision procedure. During the financial rehabilitation and external management procedures (further insolvency stages), secured creditors are generally entitled to enforce their security.

If a secured creditor opts for enforcement of security during the financial rehabilitation or external management procedure, it must file an application to the court. Enforcement is possible only if there is risk of loss or substantial devaluation of the security. If the debtor proves that enforcement of the security will make restoration of the debtor's solvency impossible, the court can reject the creditor's enforcement application. In such case, a secured creditor obtains full voting rights at the creditors' meetings during that bankruptcy stage. Unless enforced during the previous stages, the collateral security should generally be sold during the final bankruptcy stage (liquidation).

During bankruptcy proceedings, the company's pledged property can only be sold at an auction and any provisions in the security documents concerning the out-of-court enforcement of a pledge do not apply.

7.7 Will the courts in your jurisdiction recognise and enforce an arbitral award given against the company without re-examination of the merits?

A foreign arbitral award needs to be recognised and enforced in Russia, and the creditor must obtain an executory writ for the execution of an arbitral award. The decisions of international arbitration tribunals are generally enforceable in Russia subject to compliance with the provisions of the 1958 New York Convention and the requirements of Russian procedural legislation. The process of recognising and enforcing a foreign arbitral award must be made without re-examining in substance or re-litigating the underlying dispute. In practice, however, due to the absence of clearly established practice in this regard, Russian courts sometimes refuse to enforce foreign arbitral awards without substantiating such a decision with a sufficient legal explanation.

8 Bankruptcy Proceedings

8.1 How does a bankruptcy proceeding in respect of a company affect the ability of a lender to enforce its rights as a secured party over the collateral security?

Please refer to question 7.6.

8.2 Are there any preference periods, clawback rights or other preferential creditors' rights (e.g., tax debts, employees' claims) with respect to the security?

The proceeds obtained from the sale of pledged property are applied as follows:

(a) 80% (in the event of the pledge securing a loan agreement) or 70% (in all other cases) of the proceeds (in an amount not exceeding the aggregate amount of principal and interest) is allocated to satisfy the claim of the relevant secured creditor;

(b) 15% (in the event of the pledge securing a loan agreement) or 20% (in all other cases) is allocated to satisfy "first priority" and "second priority" claims if the unencumbered property of the company is insufficient to satisfy these claims; and

(c) the remaining amounts are allocated to the cost of court and bankruptcy proceedings.

Russian insolvency laws provide that certain transactions qualifying as "suspicious" or "preferential transaction" may be contested in the course of insolvency.

"Suspicious" transactions are those entered into with the intention to infringe creditors' rights and entered into by the company within the three-year period preceding the commencement of the insolvency proceedings.

A so-called "preferential transaction" is a transaction entered into with a creditor or another person that results or may result in the preferential satisfaction of a claim of one of the creditors in comparison to claims of other creditors.

"Preferential transactions" may be challenged if they are entered into within the one-month period preceding the initiation of insolvency proceedings. However, the hardening period is extended to six months if a "preferential transaction" is entered into with a person who was aware of the debtor's inability to meet its obligations or that the amount of the debtor's obligations exceeded the value of the debtor's assets. A related party is automatically deemed to have such knowledge.

The concept of "preferential transactions" captures prepayment under the existing agreements, set-offs, transfer of the debtors' property, granting security for an existing debt and other arrangements which can be frequently seen in the course of a debt restructuring. Therefore, the risk of challenge in insolvency should be carefully considered by the creditors prior to agreeing any restructuring arrangement with a company.

8.3 Are there any entities that are excluded from bankruptcy proceedings and, if so, what is the applicable legislation?

According to the Russian Civil Code, certain entities such as political parties, religious organisations, public enterprises and most state corporations are excluded from bankruptcy proceedings. Liquidation of such entities is usually subject to the Civil Code and special laws.

8.4 Are there any processes other than court proceedings that are available to a creditor to seize the assets of a company in an enforcement?

During bankruptcy proceedings, the assets of the company can be enforced only within the insolvency proceedings. Any provisions in the security documents concerning the out-of-court enforcement of a pledge do not apply.

9 Jurisdiction and Waiver of Immunity

9.1 Is a party's submission to a foreign jurisdiction legally binding and enforceable under the laws of your jurisdiction?

Submission by parties of a contract to a foreign jurisdiction should generally be binding and enforceable if at least one party is a foreign entity and the subject matter of the contract is not subject to the exclusive jurisdiction of Russian courts.

9.2 Is a party's waiver of sovereign immunity legally binding and enforceable under the laws of your jurisdiction?

The concept of waiver of sovereign immunity is not developed in Russia.

10 Licensing

10.1 What are the licensing and other eligibility requirements in your jurisdiction for lenders to a company in your jurisdiction, if any? Are these licensing and eligibility requirements different for a "foreign" lender (i.e. a lender that is not located in your jurisdiction)? In connection with any such requirements, is a distinction made under the laws of your jurisdiction between a lender that is a bank *versus* a lender that is a non-bank? If there are such requirements in your jurisdiction, what are the consequences for a lender that has not satisfied such requirements but has nonetheless made a loan to a company in your jurisdiction? What are the licensing and other eligibility requirements in your jurisdiction for an agent under a syndicated facility for lenders to a company in your jurisdiction?

Russian law provides different legal regimes with respect to loan agreements and facility agreements. Only banks (including foreign ones) may enter into a facility agreement, while loan agreements may be made by any legal entity.

In order to carry on business, all banks incorporated in Russia must receive the Central Bank of Russia's licence. No licence is required to be obtained by a foreign bank to make a loan to a Russian company.

In terms of a cross-border transaction, it should be noted that:

(a) the borrowings under a foreign currency loan can be credited to a Russian borrower's offshore account with a bank located in a state which is a member of the Organization for Economic Co-operation and Development (OECD) or the Financial Action Task Force (FATF), provided that (1) a lender is an agent of a foreign government or located in an OECD or FATF jurisdiction, and (2) the maturity of a loan exceeds two years; and

(b) a Russian company, for the purposes of effecting any payment exceeding $50,000 to a non-resident, shall open a deal passport with an authorised bank.

11 Other Matters

11.1 Are there any other material considerations which should be taken into account by lenders when participating in financings in your jurisdiction?

One of the most important considerations which should be addressed at the financing stage is the necessity to obtain a pledge or mortgage from a Russian company as collateral, which is beneficial not only because it entitles a creditor to receive satisfaction of its claim from the proceeds of the sale of the pledged or mortgaged property, but also because the status of a secured creditor gives a creditor substantial comfort during insolvency proceedings.

Further considerations which must be taken into account are the requirement to obtain corporate consents and, in respect of state-owned companies, the procurement regulations.

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Chapter 67

Serbia


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1 Overview

1.1 What are the main trends/significant developments in the lending markets in your jurisdiction?

In 2017 there was a growth in corporate lending in the Serbian market. The loan demand of companies continued to rise primarily due to investment financing and, to a lesser extent, financing of current assets and debt restructuring. Past monetary policy easing by the National Bank of Serbia, Serbia's decreased risk premium, increased competition within the banking sector, rising economic activity and low interest rates in the euro zone contributed to a further rise of lending in 2017. Growth of lending continued even though a record number of NPLs was written off, reducing the share of NPLs in total loans to 12.2% in September 2017, which was the lowest value of this ratio since January 2009.

1.2 What are some significant lending transactions that have taken place in your jurisdiction in recent years?

Major energy and infrastructure projects in Serbia have been marked by continuing involvement of IFIs. In the field of NPL acquisitions, major transactions involved various acquisitions of corporate NPLs.

2 Guarantees

2.1 Can a company guarantee borrowings of one or more other members of its corporate group (see below for questions relating to fraudulent transfer/financial assistance)?

In the case where all the companies are resident companies, there are no limitations for guaranteeing borrowings.

A resident company may guarantee borrowings only of the subsidiary non-resident company.

2.2 Are there enforceability or other concerns (such as director liability) if only a disproportionately small (or no) benefit to the guaranteeing/securing company can be shown?

Pursuant to Serbian law, directors have a fiduciary obligation towards their companies. In the case of non-compliance with such obligation, a company may bring a legal action against its director for indemnification of damages.

Also, in the event that the guarantor has creditors which cannot collect their matured claims, such creditors may, under the Serbian Law on Contracts and Torts, seek the annulment of the guarantee in court proceedings. In the course of proceedings, the creditors would argue that they were deprived of assets against which the claim could have been collected, due to issuance of the guarantee which is disproportionately low or has no benefit for the guarantor.

2.3 Is lack of corporate power an issue?

Limitations of a representative's powers may not be relied upon against third parties. There is an assumption that a legal representative of a company has the necessary authority to conclude all lawful legal transactions (including the issuing of warranties and other types of guarantees), and third parties cannot suffer consequences if a representative breaches its authority. Shareholders also have the right to void such transactions. In those cases, a legal representative is liable for damages suffered by the company as a result of the breach of authority, but any rights acquired by *bona fide* third parties on the basis of a voided transactions or its execution shall continue in full force and effect.

2.4 Are any governmental or other consents or filings, or other formalities (such as shareholder approval), required?

Regarding governmental filings, each foreign credit and/or loan including any means of guarantee provided for the foreign loans and their amendments must be reported to the NBS by the borrower within 10 days from the execution of the respective agreement or its amendments.

Regarding the shareholders' approval, the prior or subsequent approval of the ¾ majority of shareholders is required only in the case of disposal of high-value assets. If the approval is not obtained, the company itself or the shareholder holding a minimum 5% of the share capital, may file a legal action for the annulment of the issued guarantees or sureties by the guarantor, only under the condition that the counterparty was and had to be aware of the breach at the time of receiving the guarantee.

2.5 Are net worth, solvency or similar limitations imposed on the amount of a guarantee?

There are no set limitations.

2.6 Are there any exchange control or similar obstacles to enforcement of a guarantee?

There are no exchange control restrictions presenting an obstacle to the enforcement of a guarantee, provided that the guarantee was duly reported to the NBS.

In order to enforce the guarantee, any non-resident shall obtain a PIB (Tax Identification Number) and open a Serbian non-resident bank account. Before transferring of funds, a non-resident would have to convert the funds into foreign currency and submit evidence that all tax obligations have been fully settled.

3 Collateral Security

3.1 What types of collateral are available to secure lending obligations?

Lending obligations may be secured with either one of the following collaterals:

- pledge over movable assets;
- pledge over receivables;
- mortgage over immovable property;
- pledge over IP rights;
- pledge over securities;
- pledge over company's shares or stocks;
- pledge over bank accounts;
- cash deposit account agreement; or
- an assignment of receivables agreement.

3.2 Is it possible to give asset security by means of a general security agreement or is an agreement required in relation to each type of asset? Briefly, what is the procedure?

No, it is not.

3.3 Can collateral security be taken over real property (land), plant, machinery and equipment? Briefly, what is the procedure?

Yes. Both mortgage over land and plants and pledge over equipment and machines are established upon registration in the competent registers.

The only exception applies to aircrafts and vessels which are subject to special regime and registered in specialised registers.

3.4 Can collateral security be taken over receivables? Briefly, what is the procedure? Are debtors required to be notified of the security?

Yes. A pledge may be created over receivables and is established upon registration in the pledge registry.

Notification of debtors is not a perfection criterion, but is necessary for enforcement.

An assignment of receivables is created by an agreement executed between the lender and security provider which becomes fully perfected upon the notification of debtors, provided that the assignment was duly reported to the NBS.

3.5 Can collateral security be taken over cash deposited in bank accounts? Briefly, what is the procedure?

Yes. The cash deposited into bank accounts may either be pledged or deposited on a separate special purpose account.

The pledge over cash deposited into bank accounts is established upon registration in the pledge registry and only up to the amount identified at the time of the establishment of this security.

Cash is deposited into a separate special purpose account based on the tripartite agreement executed between bank, security provider and lender. The advantage of this security is, *inter alia,* direct enforcement by the lender in case of default under a credit/loan agreement.

3.6 Can collateral security be taken over shares in companies incorporated in your jurisdiction? Are the shares in certificated form? Can such security validly be granted under a New York or English law governed document? Briefly, what is the procedure?

A pledge may be established over shares or stocks depending on the corporate form of the company.

The pledge over stocks is established upon registration in the securities register. Pledged stocks are kept on the separate ownership sub-accounts.

The pledge over shares is established upon registration in the pledge registry.

The pledge over shares or stocks cannot be validly granted under any foreign law.

3.7 Can security be taken over inventory? Briefly, what is the procedure?

Yes. A pledge over inventory is established upon registration in the pledge registry.

3.8 Can a company grant a security interest in order to secure its obligations (i) as a borrower under a credit facility, and (ii) as a guarantor of the obligations of other borrowers and/or guarantors of obligations under a credit facility (see below for questions relating to the giving of guarantees and financial assistance)?

In the case a resident company is a borrower under a credit agreement executed with a non-resident, the borrower is free to secure the claim from the credit agreement by providing any of the above collaterals.

The resident company may guarantee borrowings and therefore provide all collaterals listed above, only of the subsidiary non-resident company.

3.9 What are the notarisation, registration, stamp duty and other fees (whether related to property value or otherwise) in relation to security over different types of assets?

The registration fees differ from the type of asset and may depend on the value of principal receivable (e.g. mortgage or pledge) or may be determined in a fixed amount (e.g. pledge over stocks).

Notarisation fees cannot be calculated precisely in advance. They may vary and depend on several factors such as value of mortgaged property, value of receivables, number of counterparts requested by the parties, etc.

3.10 Do the filing, notification or registration requirements in relation to security over different types of assets involve a significant amount of time or expense?

The deadlines for registration of security over different type of assets are prescribed by law. For example, a pledge is registered within five days from the day of submission of registration application, while mortgage is registered within seven days. However, some deadlines may be significantly prolonged.

3.11 Are any regulatory or similar consents required with respect to the creation of security?

Besides the perfection requirements described above, collaterals established by a resident company in favour of a non-resident creditor or as a guarantee for another non-resident borrower, must be reported to the NBS.

The constitutional documents of the company may also prescribe the shareholders' or other consents or approvals. Other potential requirements may only be estimated on a case-to-case basis.

3.12 If the borrowings to be secured are under a revolving credit facility, are there any special priority or other concerns?

No specific concerns relate to the borrowings secured under a revolving credit facility, except the mandatory reporting to NBS and mandatory repayment terms.

3.13 Are there particular documentary or execution requirements (notarisation, execution under power of attorney, counterparts, deeds)?

In general, written form of the security agreements is the only requirement unless otherwise prescribed by law (e.g. certified signatures on share pledge agreement or solemnised mortgage agreement/executed in the form of notarial deed).

If the security agreement is executed by a proxy, the power of attorney must follow the form of the agreement (e.g. power of attorney must be issued in the form of notarial deed for execution of the mortgage agreement in subject form).

4 Financial Assistance

4.1 Are there prohibitions or restrictions on the ability of a company to guarantee and/or give security to support borrowings incurred to finance or refinance the direct or indirect acquisition of: (a) shares of the company; (b) shares of any company which directly or indirectly owns shares in the company; or (c) shares in a sister subsidiary?

Regarding shares of any company which directly or indirectly owns shares in the company, joint stock or limited liability company may not directly or indirectly provide any sort of financial support to its members, employees or third parties for the acquisition of equity interests in the company, including in particular loans, guarantees, sureties, collateral, etc. Any of these transactions would be considered null and void, exposing the company to a fine ranging between RSD 100,000 and RSD 1,000,000.

Regarding shares in a sister subsidiary, providing this financial support to anyone acquiring equity in such companies is not strictly forbidden.

5 Syndicated Lending/Agency/Trustee/Transfers

5.1 Will your jurisdiction recognise the role of an agent or trustee and allow the agent or trustee (rather than each lender acting separately) to enforce the loan documentation and collateral security and to apply the proceeds from the collateral to the claims of all the lenders?

An agent or trustee, as existing in English law, is not recognised by Serbian law.

5.2 If an agent or trustee is not recognised in your jurisdiction, is an alternative mechanism available to achieve the effect referred to above which would allow one party to enforce claims on behalf of all the lenders so that individual lenders do not need to enforce their security separately?

Serbian law recognises an institution of a "security agent" only regarding the pledge of movable assets and the immovable property mortgage.

The Serbian Law on Pledges on Registered Movable Property prescribes that one or more pledgees/lenders may designate one of the lenders or a third party, i.e. the security agent, to undertake all legal actions in order to protect and settle the pledged receivable. In this case, the security agent shall have the rights of a pledgee in relation to the pledger and the name of the security agent shall be registered in the pledge registry instead of all of the pledgees/lenders.

As per the mortgage over immovable property, the Mortgage Law also prescribes that one or more mortgage lenders may designate one of the lenders or a third party to undertake all legal actions in order to protect and settle receivables secured by a mortgage.

5.3 Assume a loan is made to a company organised under the laws of your jurisdiction and guaranteed by a guarantor organised under the laws of your jurisdiction. If such loan is transferred by Lender A to Lender B, are there any special requirements necessary to make the loan and guarantee enforceable by Lender B?

The loan transfer, i.e. assignment of receivables, is possible when the banks and/or resident legal entities and/or non-resident legal entities are transferring claims and debts of residents that arise only from foreign credit operations.

A resident can, under current or capital transactions, make the collection from, or a payment to, another non-resident and not from/to a non-resident towards which the resident has a debt or a claim, provided this is permitted by the FOREX law. The assignment may be performed only on the basis of an agreement concluded by all parties or a statement of the resident confirming he is duly informed about the transfer, provided that the assignment was duly reported to the NBS.

6 Withholding, Stamp and Other Taxes; Notarial and Other Costs

6.1 Are there any requirements to deduct or withhold tax from (a) interest payable on loans made to domestic or foreign lenders, or (b) the proceeds of a claim under a guarantee or the proceeds of enforcing security?

Withholding tax shall be payable on the interest paid by a Serbian resident borrower, to a non-resident lender, at a 20% tax rate (or 25%, if a lender is a tax haven resident), unless double tax treaty prescribes otherwise. The double taxation treaties of the Republic of Serbia either prescribe a 0% rate or a diminished rate of 10%.

No tax deduction/withholding tax apply to the proceeding of a claim under a guarantee or the enforcement of security, unless the proceeds from the guarantee/enforcement of security are used to settle any part of the interest, in which case the non-resident lender is obliged to submit the tax return and pay appropriate tax on such interest.

6.2 What tax incentives or other incentives are provided preferentially to foreign lenders? What taxes apply to foreign lenders with respect to their loans, mortgages or other security documents, either for the purposes of effectiveness or registration?

There are no incentives provided for the foreign lenders.

No taxes shall be applicable to mortgages or other securities, though other costs could arise from registration of mortgages or securities.

6.3 Will any income of a foreign lender become taxable in your jurisdiction solely because of a loan to or guarantee and/or grant of security from a company in your jurisdiction?

No, the income of the foreign lender will not become taxable solely on the ground of granting a loan, guarantee, or security. The only tax, therefore, would be the tax on interest discussed above under question 6.1.

6.4 Will there be any other significant costs which would be incurred by foreign lenders in the grant of such loan/guarantee/security, such as notarial fees, etc.?

Please see question 3.9 above – there are no costs other than presented above.

6.5 Are there any adverse consequences to a company that is a borrower (such as under thin capitalisation principles) if some or all of the lenders are organised under the laws of a jurisdiction other than your own? Please disregard withholding tax concerns for purposes of this question.

There will be no adverse consequences in this respect solely because of the fact that the lender is a foreign company.

7 Judicial Enforcement

7.1 Will the courts in your jurisdiction recognise a governing law in a contract that is the law of another jurisdiction (a "foreign governing law")? Will courts in your jurisdiction enforce a contract that has a foreign governing law?

Serbian courts recognise foreign governing laws. Contracting parties are free to choose the applicable law for their contract. This freedom can, however, be limited by mandatory provisions and Serbian public policy.

Serbian courts will enforce a contract with a foreign governing law, provided it is legal, binding, valid, and that Serbian courts have jurisdiction over the contract.

7.2 Will the courts in your jurisdiction recognise and enforce a judgment given against a company in New York courts or English courts (a "foreign judgment") without re-examination of the merits of the case?

Judgments rendered by New York courts and English courts will be enforceable by Serbian courts without re-trial or re-examination of the merits of the case if:

1. the jurisdiction of the foreign court is found to be legitimate under Serbian law or the jurisdiction of such foreign court was established by the parties in the relevant documents;
2. the foreign judgment is final (non-appealable) and enforceable according to the law by which it is rendered; and
3. none of the following reasons set out below are applicable to it:
   i. the recognition of the decision would violate Serbian public policy;
   ii. the party against whom the decision was made did not attend the proceedings in person or by way of a representative because the summons, statement of claim or other document on the basis of which the proceedings were initiated was not properly served at his domicile or residence or in a timely fashion in order to allow adequate time to prepare his defence;
   iii. a final judgment has been served or a proceeding has been commenced with respect to the same legal matter and factual background between the same parties prior to the commencement of the foreign proceedings; and
   iv. a Serbian court or other authority has exclusive jurisdiction (for example, proceedings related to real estate located in Serbia).

7.3 Assuming a company is in payment default under a loan agreement or a guarantee agreement and has no legal defence to payment, approximately how long would it take for a foreign lender to (a) assuming the answer to question 7.1 is yes, file a suit against the company in a court in your jurisdiction, obtain a judgment, and enforce the judgment against the assets of the company, and (b) assuming the answer to question 7.2 is yes, enforce a foreign judgment in a court in your jurisdiction against the assets of the company?

Depending on a specific case, it may take a couple of years to reach a final and non-appealable judgment.

The procedure of recognising a foreign judgment may take up to two years.

The enforcement procedure itself generally takes one to three years, based on the complexity of the case, the location of the assets and the cooperation of the debtor, etc.

7.4 With respect to enforcing collateral security, are there any significant restrictions which may impact the timing and value of enforcement, such as (a) a requirement for a public auction, or (b) regulatory consents?

There are two types of enforcement in Serbia: (a) judicial enforcement; and (b) out-of-court enforcement.

In order to commence a judicial enforcement procedure, the creditor must obtain an enforceable document such as a pledge statement. The primary method of realisation in a judicial enforcement procedure is a public sale organised by a bailiff by an auction.

An out-of-court enforcements procedure is less formal and costly than a judicial enforcement. However, the secured creditors make preferences to judicial enforcement given it has a more predictable and certain method.

As to the volume of costs related to enforcement, they vary in accordance with the amount of the claim and pledged collateral, and usually do not exceed EUR 50,000 in large transactions.

7.5 Do restrictions apply to foreign lenders in the event of (a) filing suit against a company in your jurisdiction, or (b) foreclosure on collateral security?

No general restrictions apply, but a foreign lender:

- in the event of (a):
  - i. may be required to pay a bond for payment of the judgment in front of the national courts to ensure that the costs of the legal procedure are to be covered;
  - ii. is required to appoint a delivery agent if it does not have a Serbian registered seat; and
  - iii. can be exempt from payment of court costs only if there is a reciprocity in that matter between Serbia and country of its origin.
- in the event of (b):
  - i. is required to register a bank account in one of the banks operating in Serbia in order to initiate enforcement and finally receive collected funds; and
  - ii. is required to file a request before Serbian Tax office for tax confirmation that collected funds are not subject to any local tax, prior to transferring the received funds from a Serbian bank account to a domicile account.

7.6 Do the bankruptcy, reorganisation or similar laws in your jurisdiction provide for any kind of moratorium on enforcement of lender claims? If so, does the moratorium apply to the enforcement of collateral security?

Upon the passing court ruling on pre-bankruptcy proceedings, a temporary moratorium starts. In case the bankruptcy procedure is ordered and published by the court, the temporary moratorium ends and a general moratorium is granted automatically, meaning all pending enforcement is suspended and no new enforcement can be commenced, until the end of bankruptcy proceedings.

In the case of bankruptcy, all creditors can collect their claims against the debtor in bankruptcy proceedings only.

On the other hand, the debtor or the insolvency administrator is obliged to provide adequate protection of the pledged assets to ensure the value and condition of such assets remain unchanged.

The bankruptcy judge can lift up the moratorium against pledged assets, if one of the following conditions are met:

1. the debtor or the insolvency administrator did not adequately protect pledged assets, meaning pledged assets would be at some risk; or
2. the value of the pledged assets decreases, and there is no other remedy to provide adequate and effective protection against the reduction of value.

Instead of deciding to lift up the moratorium, the bankruptcy judge may pass ruling to impose adequate protection of pledged assets by implementing one or more of the following measures:

1. payment of regular monetary compensation to a secured creditor, in an amount which is equal to the amount for which the value of the assets is reduced or the compensation for actual or estimated losses;
2. the replacement of assets or determination of additional assets that will serve as collateral in order to compensate for a decrease in value;
3. repair, maintenance, insurance or measures of special security and custody of the assets; and/or
4. other protective measures or other types of compensation for which the bankruptcy judge considers them to protect the value of the assets of the secured creditor.

7.7 Will the courts in your jurisdiction recognise and enforce an arbitral award given against the company without re-examination of the merits?

Serbia is a contracting party to the New York Convention on recognition and enforcement of arbitral awards, thus all arbitral awards rendered in the territory of another Contracting Party State shall be recognised and enforced without a re-examination of the merits of the case.

An arbitral award has to, however, fulfil the following conditions:

1. it has to be rendered by a competent court of arbitration;
2. it has to be rendered with respect to the parties' right to participate in the arbitral proceedings (with special consideration on appropriate delivery of relevant documents);
3. it has to be final; and
4. none of the following reasons set out below are applicable to it:
   - a) arbitral tribunal has exceeded given authority;
   - b) there has been a breach of an arbitration agreement;
   - c) the arbitral award was based on a false statement of a witness or expert or on a forged document or the award;
   - d) the subject of dispute is not arbitrable; or
   - e) the recognition of the arbitral award would be against Serbian public policy.

8 Bankruptcy Proceedings

8.1 How does a bankruptcy proceeding in respect of a company affect the ability of a lender to enforce its rights as a secured party over the collateral security?

The bankruptcy proceedings decisively affects the lender's ability to enforce its rights as a secured party over collateral security. From the moment bankruptcy is commenced, no enforcement against the debtor is allowed and all creditors can satisfy their claims in bankruptcy proceedings only.

Regarding other relevant enforcement issues during bankruptcy proceedings, please refer to question 7.6.

8.2 Are there any preference periods, clawback rights or other preferential creditors' rights (e.g., tax debts, employees' claims) with respect to the security?

A company's creditor or bankruptcy manager may contest a company's transactions entered into during specified periods prior to filing for the insolvency.

There are five different types of vulnerable transactions that are exposed to such claw-back claims, as follows:

i. customary settlement – entered into six months prior to a bankruptcy petition filling;

ii. incongruent settlement – entered into 12 months prior to a bankruptcy petition filling;

iii. directly detrimental transaction – entered into six months prior to a bankruptcy petition filling or afterwards;

iv. intentionally detrimental transactions – entered into five years prior to a bankruptcy petition filling; or

v. transactions without or insignificant consideration – entered into five years prior to a bankruptcy petition filling.

There are no preference periods or other preferential creditors' rights with respect to the security.

8.3 Are there any entities that are excluded from bankruptcy proceedings and, if so, what is the applicable legislation?

The following entities cannot be the subject of a bankruptcy proceeding: the Republic of Serbia; autonomous provinces and local self-government units; funds or pension funds; legal entities founded by the Republic of Serbia such as autonomous province or local self-government units, which are financed exclusively or predominantly through the allocated public revenues or from the budget, i.e. the budget of the autonomous province and the local self-government unit; the National Bank of Serbia; the Central Register, depot and clearing of securities; and public agencies.

For the obligations of the abovementioned entities, there is a joint and several liability of their founders and owners, as well as their members and shareholders.

Also, special legislation is applicable on bankruptcy proceedings of banks and insurance organisations.

8.4 Are there any processes other than court proceedings that are available to a creditor to seize the assets of a company in an enforcement?

Once the bankruptcy proceeding starts, there are no other means to seize the assets of a company.

9 Jurisdiction and Waiver of Immunity

9.1 Is a party's submission to a foreign jurisdiction legally binding and enforceable under the laws of your jurisdiction?

Yes (provided that no national asset is involved).

9.2 Is a party's waiver of sovereign immunity legally binding and enforceable under the laws of your jurisdiction?

Yes (provided that no national asset is involved).

10 Licensing

10.1 What are the licensing and other eligibility requirements in your jurisdiction for lenders to a company in your jurisdiction, if any? Are these licensing and eligibility requirements different for a "foreign" lender (i.e. a lender that is not located in your jurisdiction)? In connection with any such requirements, is a distinction made under the laws of your jurisdiction between a lender that is a bank *versus* a lender that is a non-bank? If there are such requirements in your jurisdiction, what are the consequences for a lender that has not satisfied such requirements but has nonetheless made a loan to a company in your jurisdiction? What are the licensing and other eligibility requirements in your jurisdiction for an agent under a syndicated facility for lenders to a company in your jurisdiction?

The activity of granting credits in the Republic of Serbia is exclusively performed by the banks as financial institutions licensed by the NBS, whereas loans can be freely granted by banks, companies and other entities, as well as by natural persons.

Serbian law authorises foreign banks and foreign legal entities to grant credits and loans to residents without any restrictions. However, please note that certain limitations may occur when repaying the credit/loan:

- a credit may be repaid only after the expiration of one year from the date of its disbursement, and if drawn in tranches, after the expiration of one year from the date of the drawdown of each individual tranche;
- if a credit is repaid in several instalments, repayment can only begin after expiration of six months from the date of each use of the credit and the repayment is carried out in proportionate instalments until the total amount repayment;
- banks may use credits with a repayment term shorter than one year, in which case they may start repayment before the expiration of six months from the date of disbursement;
- residents – legal entities and entrepreneurs – may use credits with a repayment term shorter than one year only for the purposes of financing the purchase, processing and production of agricultural products or financing exports of goods and services, but may not start repayment before the expiration of three months from the date of each drawdown on the credit; and
- residents – natural persons – may take foreign credits and loans with a repayment term over one year, provided the funds are credited to the account of that resident with a bank, while a resident branch of a foreign legal entity may take such credits and loans from a non-resident founder.

Foreign credit operations and loans, and any amendments thereof, have to be reported to the NBS by a borrower in order to be utilised. Failure to notify the NBS represents a misdemeanour imposing a fine on a resident legal entity.

Serbian law does not prescribe any additional conditions that a foreign bank or a foreign lender should fulfil. The same applies to the agent under a syndicated facility.

11 Other Matters

11.1 Are there any other material considerations which should be taken into account by lenders when participating in financings in your jurisdiction?

The response to this question depends on specific details of each particular case.

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Since its establishment in 1991, JPM has been positioned as one of the leading law firms in Serbia, providing full service to international and domestic clients from various industries and assisting them in establishing, building and maintaining their business presence in Serbia.

JPM's track record in banking and finance law comprises of numerous, successfully completed landmark transactions in which its lawyers have designed and implemented original, well conceptualised legal solutions.

This firm is focused on developing solutions and implementing practices that meet clients' business goals and ensure compliance and an optimal risk management approach. Its commitment, expertise and experience in resolving complex business and legal issues, as well as in-depth understanding of the clients' industries, enables the firm to deliver the highest quality legal services and cost effective solutions.

The main languages fluently spoken by JPM lawyers are English and German. Additional languages spoken are Russian, French and Italian.

Chapter 68

Singapore

Blossom Hing

Drew & Napier LLC

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1 Overview

1.1 What are the main trends/significant developments in the lending markets in your jurisdiction?

Overall loan growth has picked up over 2017 and Singapore's banking system has seen increased lending both domestically and to the region. Domestic loan growth has increased amidst a recovery in lending to general commerce sectors consistent with general increased activity for consumer-facing industries. Growth in housing loans is also supported by increased activity in the private residential property market, buoyed by increases in both prices and transactions due to improved buyer sentiments and low interest rates. Net lending to emerging Asia has also increased late 2017 in line with strengthening regional economic activity, led by local and Japanese banks.

According to the Monetary Authority of Singapore, overall credit quality and non-performing loans have started to improve due to better economic prospects both domestically and in the region. Overall asset quality has improved as well, although there are still elevated credit risks from the marine and offshore engineering sectors due to continued weakening demand and declining profitability.

The various proposed amendments to the Companies Act (Cap. 50) (***CA***) mentioned in the edition published last year, namely to reduce the regulatory burden of companies and to introduce the inward re-domiciliation regime, came into effect in 2017. These changes include exemption of private companies from holding annual general meetings subject to certain conditions, and allowing foreign entities to transfer their registration from their original jurisdictions to Singapore.

Significant amendments were also made to the CA in a move to enhance the local debt restructuring and corporate rescue framework, in a push to position Singapore as an international centre for debt restructuring. One of the more significant changes in the context of lending is the introduction of super-priority securities for rescue financing. The Court will be empowered to grant rescue financing various levels of priority over other secured and unsecured debts subject to certain conditions and safeguards. Depending on the type of priority sought, a debtor company may apply for priority for rescue financing either before or after obtaining the rescue financing concerned.

1.2 What are some significant lending transactions that have taken place in your jurisdiction in recent years?

One of the more significant loan transactions in 2017 is the grant of loan facilities of S$980 million by BNP Paribas, DBS Bank, OCBC Bank and Standard Chartered Bank to OUE Hospitality Trust to refinance several of the borrower's existing facilities. For debt capital markets, DBS Group Holdings Ltd (***DBSH***) successfully priced the issue of US$500 million floating rate green bonds due 2022 under its US$30 billion Global Medium Term Note Programme. This was the first green bond issuance in Singapore by a financial institution, under the MAS Green Bond Grant Scheme.

Some significant transactions in 2016 include the issuance of Rs 13.3 billion worth of *Masala bonds* that were listed on the Singapore exchange by Indiabulls Housing Finance, and DBSH's US dollar-denominated Basel III-compliant Additional Tier 1 perpetual capital securities offering which reached the target issue size of US$750 million. DBSH's securities were issued under DBSH's US$30 billion Global Medium Term Note Programme.

Significant lending transactions in the previous two years include the syndicated refinancing credit facilities of up to S$2.27 billion granted to Resorts World at Sentosa Pte Ltd. The facilities were underwritten by the original mandated lead arrangers and bookrunners, namely, The Bank of Tokyo-Mitsubishi UFJ, DBS Bank Ltd, The Hongkong and Shanghai Banking Corporation, Oversea-Chinese Banking Corporation and Sumitomo Mitsui Banking Corporation. In the year before, the industry saw the S$5.1 billion amendment-and-extension facility for casino operator Marina Bay Sands to, amongst others, extend the maturities of facilities, in which DBS Bank was coordinator and mandated lead arranger and bookrunner, and the US$4.95 billion bridging loan for the Oversea-Chinese Banking Corporation's acquisition of Wing Hang Bank Ltd., underwritten by the Bank of America Merrill Lynch, the Hongkong and Shanghai Banking Corporation Limited and J.P. Morgan.

2 Guarantees

2.1 Can a company guarantee borrowings of one or more other members of its corporate group (see below for questions relating to fraudulent transfer/financial assistance)?

Yes, subject to there being sufficient corporate benefit and no contravention of specific rules under the CA; for example, relating to guarantee of loans to companies related to directors and provision of financial assistance.

S157 of the CA provides that a director of a company "shall at all times act honestly and use reasonable diligence in the discharge of the duties of his office". This statutory statement is in addition to the directors' duty under general law to exercise their discretion *bona fide* in what they consider is in the best interest of the company. The directors of a company have to ensure there is sufficient corporate benefit in giving any guarantee, including a guarantee for the borrowings of one or more members of its group.

A commonly asked question is whether directors can, in giving a guarantee, consider the interests of the corporate group. The theoretical rule is that companies within a group are separate legal entities. However, in practice, companies are often part of larger groups and it is generally accepted that there is corporate benefit on the face of a transaction involving a holding company guaranteeing the obligations of its subsidiary. It would be harder, however, to show corporate benefit in a subsidiary guaranteeing the debts of its holding or sister companies and in such situations, it would be prudent to have the shareholders of the company sanction the giving of the guarantee.

In addition, companies have to be mindful of the prohibition under s163 of the CA relating to the guarantee of loans, quasi-loans or credit transactions to companies related to directors. There are exceptions to this prohibition, including where the companies involved are in a subsidiary/holding company relationship or are subsidiaries of the same holding company in the legal sense. Members of a corporate group in the legal sense are therefore generally exempted. They are, however, not exempted if they are non-subsidiary affiliates and directors have to be careful then to conduct the necessary enquiry to ensure there is no contravention of the section. With effect from 3 January 2016, a new exception was introduced to allow for prior approval by the company in general meeting to permit such transactions. Where practicable (for example, when dealing with private companies), lenders are likely to require such prior approval by shareholders to be obtained to do away with the risk of triggering this prohibition.

Regard also has to be given to the prohibition against the giving of financial assistance and other considerations where a company is insolvent, as set out in sections 4 and 8 below.

2.2 Are there enforceability or other concerns (such as director liability) if only a disproportionately small (or no) benefit to the guaranteeing/securing company can be shown?

See question 2.1 above. In giving a guarantee, the directors of the company have to ensure there is sufficient corporate benefit. If the corporate benefit to the guaranteeing company is disproportionately small or there is no corporate benefit, then there may be an issue as to whether the directors in giving the guarantee are in breach of their fiduciary duties.

Where directors have given a guarantee in breach of their fiduciary duties, the guarantee may be set aside if the lender had knowledge of the impropriety and the offending directors may be both civilly and criminally liable for their breach.

Other considerations where a company is insolvent are set out in section 8 below.

2.3 Is lack of corporate power an issue?

Unless otherwise limited or restricted by the provisions of its own constitutive documents, a company has full capacity to perform any act, including entering into guarantees. Caution should be taken as there are, however, companies with old forms of constitutive documents that still contain restrictions and limits on the grant of guarantees and if so, such restrictions will continue to apply.

The effect of the lack of corporate power in the grant of a guarantee, whilst it does not invalidate the guarantee *per se*, may be asserted or relied upon in, amongst others, proceedings against the company by any member of the company or, where the company has issued debentures secured by a floating charge over all or any of the company's property, by the holder of any of those debentures to restrain the doing of any act or transfer of any property by the company. The court may, in such a situation, exercise discretion to set aside and restrain the performance of the guarantee but allow for compensation for loss or damage sustained.

The CA deems the power of the directors to bind the company, or authorise others to do so, to be free of any limitation under the company's constitution, in favour of persons dealing with the company in good faith. It remains to be seen if the Singapore courts will find that knowledge of an act being beyond the powers of the directors under the constitutive documents of the company will, by itself, be sufficient to establish a lack of good faith for purposes of this new provision.

2.4 Are any governmental or other consents or filings, or other formalities (such as shareholder approval), required?

No governmental consents or filings are generally required.

A guarantee will be required to be lodged with the companies' registry in Singapore, ACRA, only if by its terms it also seeks to create a charge or agreement to charge within the meaning of s131 of the CA.

In terms of formalities, a contract of guarantee has to be in writing and signed by the person sought to be rendered liable under the guarantee. Board resolutions approving the terms, execution and performance of the guarantee should be passed. Shareholders' approval should also be obtained if there is any potential issue of lack of corporate benefit and breach of directors' duties, or triggering of s163 of the CA or where it is otherwise required by statute (for example, to whitewash the transaction) or the constitutive documents of the company.

2.5 Are net worth, solvency or similar limitations imposed on the amount of a guarantee?

No, unless otherwise restricted by the constitutive documents of the company.

If, however, the amount guaranteed is clearly disproportionate to the corporate benefit received, the issues discussed in question 2.2 above would arise.

Other considerations where a company is insolvent are set out in section 8 below.

2.6 Are there any exchange control or similar obstacles to enforcement of a guarantee?

There are no exchange controls in Singapore which would act as an obstacle to the enforcement of a guarantee.

3 Collateral Security

3.1 What types of collateral are available to secure lending obligations?

Under Singapore law, all types of collateral may potentially be available to secure lending obligations, provided the grant thereof is not against public policy.

Common types of collateral that can be used include real property (land and buildings), personal chattels, debts and other receivables, stocks and shares and other choses in action.

3.2 Is it possible to give asset security by means of a general security agreement or is an agreement required in relation to each type of asset? Briefly, what is the procedure?

It is possible to give asset security by means of a general security agreement; for example, by way of a debenture seeking to take security over different classes of assets, save to the extent that a statutorily prescribed form is required (e.g. to effect a legal mortgage over land under the Land Titles Act (Cap. 157) (***LTA***) or take a legal assignment over book-entry securities).

The main types of security interests that can be created under Singapore law are mortgages, charges, liens and possessory pledges, and the appropriate method of taking security would depend on the nature of the asset over which the security is to be taken and the extent of security required.

Different classes of assets will also be subject to different procedures and perfection requirements.

3.3 Can collateral security be taken over real property (land), plant, machinery and equipment? Briefly, what is the procedure?

Land

Yes, a legal or equitable mortgage/charge or assignment of sale and purchase/lease/building agreement with mortgage-in-escrow is commonly granted over real property (land and to the extent immovable, plant and buildings thereon). The type of security will depend on, amongst other factors, whether title over the land has been issued, the land type and the type of holding.

There are two types of land in Singapore – common law titled land and land under the LTA. Virtually all land in Singapore has been brought under the LTA. A legal mortgage for land under the LTA has to be in a statutorily prescribed form and registered with the Singapore Land Authority (***SLA***). Where title has not been issued for land under the LTA, a lender would take an equitable mortgage over the sale and purchase agreement, lease or building agreement in relation to the land, with an accompanying mortgage-in-escrow for perfection upon issue of title.

Commonly, an appropriate caveat may also be lodged with the SLA against the land to protect the lender's interest during the time between the acceptance of the facility and the registration and perfection of the security.

Related security like an assignment over insurances, rental and sale proceeds and agreements and in the case of land under construction, assignment over construction contracts and performance bonds are usually also taken.

Procedure and perfection steps briefly include taking of relevant title documents, registration with the SLA (or Registry of Deeds, if applicable), registration of the charge with ACRA under s131 of the CA, stamping, consents from lessor of the land or other third parties (if applicable), corporate authorisations, whitewash/shareholders' approval (if applicable), etc. In practice, some banks require shareholders' approval where the assets to be mortgaged/charged constitute the whole or substantially the whole of the company's undertaking or property.

Machinery and equipment

A fixed charge granted by way of a debenture or charge is commonly taken over machinery and equipment.

Registration with ACRA will be required under s131 of the CA. Other perfection steps are (to the extent applicable) discussed above.

3.4 Can collateral security be taken over receivables? Briefly, what is the procedure? Are debtors required to be notified of the security?

Yes, security over receivables (being choses in action) can be taken by way of an assignment or charge (fixed or floating) through a deed of assignment/charge or a debenture, depending on the entire security package to be taken. Generally, lenders may also, for control purposes, obtain a charge (fixed or floating) over the accounts into which the receivables are paid (see question 3.5 below).

In order to take a legal assignment over receivables, it has to be in writing with express notice in writing given to the debtor of the receivables. The giving of notice also enables the lender to secure priority.

A charge to be taken over receivables can be fixed or floating. Where the lender is able to control the receivables and they are not subject to withdrawals without consent, a legal assignment or fixed charge may be created over the subject receivables. Often, however, the receivables are part of the ongoing business of the security provider and the lender does not seek to take control over the same. In such a situation, only a floating charge may be created in substance, regardless of how the charge is termed or labelled in the documentation.

Registration with ACRA will be required if the charge is floating or the receivables fall under one of the prescribed categories of s131 of the CA. Other perfection steps are, to the extent applicable, discussed in question 3.3 above.

3.5 Can collateral security be taken over cash deposited in bank accounts? Briefly, what is the procedure?

Yes, security over cash deposited in bank accounts (being choses in action) can be taken in the same way as receivables and the principles and requirements in question 3.4 apply.

In practice, it may be difficult to obtain a legal assignment or fixed charge over cash deposited in a bank account unless the bank account is opened with and controlled by the lender. Where that is not practicable and/or it is necessary to enable the chargor to make withdrawals from the bank account freely, the lender may be left with taking only a floating charge over the account.

Registration with ACRA will be required if the charge is floating or if it falls under one of the prescribed categories of s131 of the CA. Other perfection steps are as discussed in question 3.3 above.

3.6 Can collateral security be taken over shares in companies incorporated in your jurisdiction? Are the shares in certificated form? Can such security validly be granted under a New York or English law governed document? Briefly, what is the procedure?

Shares in Singapore may be in certificated/scrip or scripless form.

Where shares are certificated, a legal or equitable mortgage may be taken over the shares. A legal mortgage may be granted by way of a share mortgage, accompanied by a transfer and registration of the shares and delivery of share certificates in the mortgagee's name. The procedures and restrictions for the transfer will be set out in the company's constitutive documents and the CA. An equitable mortgage/charge may be granted by way of a share mortgage/charge and deposit of share certificates together with a blank transfer executed by the mortgagor/chargor on the agreement that the mortgagee/chargee may complete the transfer forms upon occurrence of a default event under the facility or by notice.

Where shares are in scripless form (i.e. book-entry securities, being essentially listed shares of companies on the Singapore stock exchange – Singapore Exchange Limited), by statute, a different regime will apply. Security may be taken over such shares by way of a statutory assignment or statutory charge in prescribed form registered with the Central Depository (Pte) Limited in Singapore or by common law subject to certain prescribed requirements.

There is no specific restriction to prohibit the general terms of security over shares to be governed by New York or English law, but the creation and grant of security over shares should be governed by Singapore law as the shares of Singapore companies (and exercise of certain enforcement rights) are regulated by the CA and local property rules.

Registration with ACRA will be required if the charge is floating or the shares fall under one of the prescribed categories of s131 of the CA. Other perfection steps are as discussed in question 3.3 above.

3.7 Can security be taken over inventory? Briefly, what is the procedure?

Yes, a floating charge is most commonly created over inventory. The chargor in this instance will generally be permitted to deal with the inventory in the ordinary course of its business until the occurrence of a default event under the facility or notice from the lender.

Registration with ACRA is required under s131 of the CA. Other perfection steps are as discussed in question 3.3 above.

3.8 Can a company grant a security interest in order to secure its obligations (i) as a borrower under a credit facility, and (ii) as a guarantor of the obligations of other borrowers and/or guarantors of obligations under a credit facility (see below for questions relating to the giving of guarantees and financial assistance)?

Yes for both cases, subject to considerations such as the existence of corporate power and corporate benefit, s162/163 of the CA (prohibition on loans, quasi-loans and credit transactions to directors and related companies) and financial assistance etc., as set out in this chapter.

3.9 What are the notarisation, registration, stamp duty and other fees (whether related to property value or otherwise) in relation to security over different types of assets?

The fee for the registration of a charge/security instrument with ACRA in accordance with s131 of the CA is currently S$60 per charge.

In addition, security interest over certain assets (e.g. aircraft, ships, intellectual property rights and land) will need to be registered at specialist registries and additional fees will be payable. For example, the fee payable for the registration of a mortgage over land with the SLA is currently S$68.30 per mortgage.

Stamp duty is payable on a mortgage, equitable mortgage or debenture of any immovable property and stock or shares. A legal mortgage is subject to *ad valorem* duty at the rate of 0.4% of the amount of facilities granted on the mortgage of immovable property or stocks and shares, subject to a maximum of S$500. An equitable mortgage is subject to *ad valorem* duty at the rate of 0.2% of the amount of facilities granted on the mortgage of immovable property, subject to a maximum of S$500.

Notarisation is not required for security documents which are executed and to be used in Singapore.

3.10 Do the filing, notification or registration requirements in relation to security over different types of assets involve a significant amount of time or expense?

The charge/security instrument to be lodged with ACRA under s131 of the CA must be lodged within 30 calendar days after the creation of the charge where the document creating the charge is executed in Singapore (or within 37 calendar days if executed outside Singapore). The filing (once filing forms are completed) is instantaneous and confirmation of registration from ACRA will normally take two to three business days.

The timeframe for registration at specialist registries differs according to each registry. For example, the registration of a mortgage with the SLA may take several weeks if complex and involving multiple units. In the interim, a lender may protect its interest by the lodgement of a caveat with the SLA.

Fees payable for such registrations are as discussed in question 3.9 above.

3.11 Are any regulatory or similar consents required with respect to the creation of security?

Regulatory consents may be required in certain circumstances; for example, where the subject land is state land leased from the Government or Government statutory boards like the SLA and Urban Redevelopment Authority.

3.12 If the borrowings to be secured are under a revolving credit facility, are there any special priority or other concerns?

Under Clayton's rule, security taken over a revolving loan may be 'reducing' as the loan 'revolves' as a result of the 'first in first out' rule. In the absence of contrary indication, a secured revolving facility may technically lose the security once an amount equal to the original loan and any associated charges and interest has been paid into the account, even though sums have been paid out in the meantime. This is rarely an issue in practice, however, as finance documents will be drafted to provide for inverse order of payment and/or for security to be continuing notwithstanding any intermediate payments made as long as there is anything outstanding under the loan.

3.13 Are there particular documentary or execution requirements (notarisation, execution under power of attorney, counterparts, deeds)?

Execution requirements are predominantly set out in the company's constitutive documents and the CA. In addition, certain instruments are also statutorily required to be in writing or executed by deed. For example, a legal mortgage over land must be by deed. Certain statutory remedies (e.g. power to sell the mortgaged property, to insure the property, to appoint a receiver, etc.) given to mortgagees will also not be available unless the mortgage is by deed. Commonly, it is prudent in any event for securities to be executed by deed so that there is no issue of past consideration.

Where it is envisaged that the execution of the security instrument be completed by virtual means, it is also good practice for it to be done in line with the principles set out in the English case *R (on the application of Mercury Tax Group and another) v HMRC*.

4 Financial Assistance

4.1 Are there prohibitions or restrictions on the ability of a company to guarantee and/or give security to support borrowings incurred to finance or refinance the direct or indirect acquisition of: (a) shares of the company; (b) shares of any company which directly or indirectly owns shares in the company; or (c) shares in a sister subsidiary?

S76 of the CA provides, *inter alia*, that a public company or a company whose holding company or ultimate holding company is a public company, shall not, whether directly or indirectly, give any financial assistance for the purpose of, or in connection with the acquisition by any person (whether before or at the same time as the giving of financial assistance) or proposed acquisition by any person, of shares in the company or in a holding company or ultimate holding company (as the case may be) of the company. The prohibition does not extend to sister subsidiary companies. The CA further provides that financial assistance for the acquisition of shares may be provided by means of a loan, the giving of a guarantee, the provision of security, the release of an obligation or the release of a debt or otherwise.

These provisions may therefore be triggered in the event of the giving of guarantees/securities or other accommodation which may directly or indirectly provide 'financial assistance' within the meaning of the CA. There are, however, whitewash provisions available under our laws, including short form whitewash procedures that would enable the company to effect a whitewash through, *inter alia*, board approval if doing so does not materially prejudice the interests of the company or its shareholders or the company's ability to pay its creditors, or the passing of shareholders' and directors' resolutions and lodgement of solvency statements and papers with ACRA without the need for public notification and objection period or court order. Where the company is unable to effect a short form whitewash, parties have to bear in mind that the need for public notification and objection period for a long form whitewash will mean that a timeframe of six to eight weeks (assuming no objections) may be required.

5 Syndicated Lending/Agency/Trustee/Transfers

5.1 Will your jurisdiction recognise the role of an agent or trustee and allow the agent or trustee (rather than each lender acting separately) to enforce the loan documentation and collateral security and to apply the proceeds from the collateral to the claims of all the lenders?

Yes, Singapore recognises the role of an agent and trustee and these roles are normally taken up by the lead bank to whom the borrower has granted the mandate to arrange the syndicated loan. An express trust will be created to ensure the desired consequences.

The creation of the trust must comply with the relevant formalities. For example, s7 of the Singapore Civil Law Act (Cap. 43) requires a trust in respect of immovable property to be manifested and proved in writing signed by the person who is able to declare such trust. In addition, a validly constituted express trust has to be certain as to intention of the settlor to create the trust, identity of the subject matter and identity of the beneficiaries. Provided the relevant mechanics are set out in the finance documents and the trust is properly constituted, the security trustee will be able to hold the security on trust for the syndicated lenders and will have the right to enforce the finance documents and collateral security, including applying the proceeds from the collateral to the claims of the syndicated lenders in accordance with the finance documents.

5.2 If an agent or trustee is not recognised in your jurisdiction, is an alternative mechanism available to achieve the effect referred to above which would allow one party to enforce claims on behalf of all the lenders so that individual lenders do not need to enforce their security separately?

This is not applicable. Please refer to question 5.1 above.

5.3 Assume a loan is made to a company organised under the laws of your jurisdiction and guaranteed by a guarantor organised under the laws of your jurisdiction. If such loan is transferred by Lender A to Lender B, are there any special requirements necessary to make the loan and guarantee enforceable by Lender B?

The right of Lender B to enforce the loan and guarantee exists provided the procedure for assignment or novation of Lender A's rights and obligations, as set out in the finance documents, are complied with (e.g. consent of borrower and guarantor if required) and the continuity of the guarantee is provided for expressly and preserved under the documents.

Where there are no proper procedures or transfer/preservation provisions within the finance documents or the security agency/trust is not properly constituted, an assignment or novation of the underlying loan may result in an assigned or new debt which is not covered by the guarantee. A transfer in such a situation may fail and the guarantee rendered unenforceable over the assigned or new debt. In such an instance, a fresh guarantee will be required for Lender B to be guaranteed. In practice, confirmation by the guarantor is often sought even if the documents provide expressly for preservation without consent.

6 Withholding, Stamp and Other Taxes; Notarial and Other Costs

6.1 Are there any requirements to deduct or withhold tax from (a) interest payable on loans made to domestic or foreign lenders, or (b) the proceeds of a claim under a guarantee or the proceeds of enforcing security?

Withholding tax is applicable by virtue of s12(6) read with s45 or 45A of the Singapore Income Tax Act (Cap. 134) (***ITA***) where a person is liable to pay another person not known to him to be resident in Singapore any interest, commission, fee or any other payment in connection with any loan or indebtedness or with any arrangement, management, guarantee, or service relating to any loan or indebtedness if such payments are borne, directly or indirectly, by a person resident in Singapore or a Singapore permanent establishment or is deductible against any income accruing in or derived from Singapore. Interest and agency fee payments are generally subject to this withholding tax unless otherwise exempted.

Assuming that such income is not derived by the non-resident person from any trade, business, profession or vocation carried on or exercised by him in Singapore and is not effectively connected with any permanent establishment in Singapore of the non-resident person, the current withholding tax rate is 15% of the gross payment.

There are, however, various exceptions to this. For example, s12(6) payments made to Singapore branches of non-resident banks are not subject to withholding tax. In addition, if the non-resident bank is a resident of a tax treaty country, the Avoidance of Double Taxation Agreement may provide for a different/reduced tax rate.

6.2 What tax incentives or other incentives are provided preferentially to foreign lenders? What taxes apply to foreign lenders with respect to their loans, mortgages or other security documents, either for the purposes of effectiveness or registration?

Singapore has various governmental agencies to assist foreign investors and creditors. The Economic Development Board is the lead governmental agency responsible for planning and executing strategies to attract foreign businesses and investments. International Enterprise Singapore works to position Singapore as a base for foreign businesses to expand into the region, in partnership with Singapore-based companies.

Although incentives are generally industry-specific, and not affected by the residency of the investors or creditors, there are selected schemes directed to attract foreign investors and creditors. For example, Singapore allows for reduced withholding tax rate on interest payments on loans taken to purchase productive equipment for the purposes of trade or business.

Save for withholding taxes as discussed in question 6.1, no taxes specific to loans, mortgages or other security documents, either for the purposes of effectiveness or registration are applicable. Stamp duty as discussed in question 3.9 will be applicable.

6.3 Will any income of a foreign lender become taxable in your jurisdiction solely because of a loan to or guarantee and/or grant of security from a company in your jurisdiction?

Where the bank is not a tax resident in Singapore, withholding tax as discussed in question 6.1 may apply.

Where the bank is a tax resident in Singapore or has a branch in Singapore, any interest, commission, fee or any other payment in connection with any loan or indebtedness or with any arrangement, management, guarantee, or service relating to any loan or indebtedness that is borne, directly or indirectly, by a person resident in Singapore or a Singapore permanent establishment or is deductible against any income accruing in or derived from Singapore, that accrues to or is derived by the bank or its Singapore branch will be deemed to be sourced in Singapore and subject to income tax in Singapore by virtue of s12(6) read with s10(1) of the ITA.

6.4 Will there be any other significant costs which would be incurred by foreign lenders in the grant of such loan/guarantee/security, such as notarial fees, etc.?

Apart from fees and tax payable as discussed above (i.e. questions 3.9 and 6.1), the provision of certain services, for example the provision of guarantee services, may be subject to goods and services tax (***GST***) in Singapore if the provider of the service is registered for GST purposes pursuant to the Singapore Goods and Services Tax Act (Cap. 117A) unless the service qualifies as an international service or is an exempt supply on which no GST is chargeable. The rate at which GST is chargeable on standard-rated supplies of goods and services is presently 7%. During The Budget 2018, it has been announced that the GST rate may be raised to 9% sometime in the period from 2021 to 2025.

6.5 Are there any adverse consequences to a company that is a borrower (such as under thin capitalisation principles) if some or all of the lenders are organised under the laws of a jurisdiction other than your own? Please disregard withholding tax concerns for purposes of this question.

Thin capitalisation principles are not applicable in Singapore. However, it should be noted that should the banks be organised under the laws of a foreign jurisdiction, and no express choice of law is made in the finance documents, the applicable law for the finance documents may be that of the foreign jurisdiction. In such a situation, the borrower may not be able to enjoy the rights and remedies available to a borrower in Singapore, but not in that foreign jurisdiction.

7 Judicial Enforcement

7.1 Will the courts in your jurisdiction recognise a governing law in a contract that is the law of another jurisdiction (a "foreign governing law")? Will courts in your jurisdiction enforce a contract that has a foreign governing law?

Provided that it is *bona fide* and legal and there is no reason for avoiding the choice on the grounds of public policy, the express choice of the laws made by the parties to a contract will be upheld as valid and binding in any action in the courts of Singapore and the courts will enforce a contract that has a foreign governing law.

In January 2015, the Singapore International Commercial Court (***SICC***) was established to hear international commercial disputes, including those governed by foreign laws.

The key features of the SICC are: (i) it is a division of the Singapore High Court. This means that SICC judgments can be enforced as judgments of the Supreme Court of Singapore; (ii) it has a diverse panel of judges that will include eminent international jurists and existing Supreme Court Judges; (iii) its proceedings are open court proceedings although parties may apply for the proceedings to be confidential; and (iv) there is flexibility for parties to seek leave of court to apply alternative rules of evidence (i.e. rules which differ from the existing Singapore rules of evidence) which they may be more familiar with; and to appoint foreign-qualified lawyers to represent them in court where the cases have no substantial connection to Singapore or to address the Court on matters of foreign law.

In its first three years since 2015, the SICC has heard 17 cases involving parties from various jurisdictions. Additionally, the new Supreme Court of Judicature Amendment Bill introduced in 2017 (if passed) clarifies that the SICC has jurisdiction to hear any cases relating to international commercial arbitration and domestic arbitration.

7.2 Will the courts in your jurisdiction recognise and enforce a judgment given against a company in New York courts or English courts (a "foreign judgment") without re-examination of the merits of the case?

A final judgment for a sum of money obtained against a company in Singapore (which is not a judgment for the payment of a fine, penalty or tax, or anything of that nature) in a superior court in England will be enforceable against the company in Singapore subject to the provisions of the Singapore Reciprocal Enforcement of Commonwealth Judgments Act (Cap. 264) (***RECJA***), without re-examination of the merits.

In 2016, Singapore also introduced the Choice of Court Agreements Act 2016 (***CCAA***), which implements the regime created by the 2005 Hague Convention on Choice of Court Agreements (***Hague Convention***). The CCAA applies to judgments given by courts of states that are parties to the Hague Convention. These states currently comprise all of the EU Member States (except Denmark, but including England) and Mexico. The United States of America, People's Republic of China and Ukraine have also signed the Hague Convention and it is pending their ratification. Under the CCAA, where parties have entered into an agreement designating the English courts as having exclusive jurisdiction in respect of a particular matter, and an English court renders a judgment in that matter, the English judgment may be recognised and enforced in Singapore without re-examination of the merits. This is subject to certain exceptions. For example, certain types of matters are excluded from the scope of the CCAA, such as insolvency matters and matters involving consumers. Recognition and enforcement may, depending on the court's discretion, be refused if, for example, where the English judgment is inconsistent with a Singapore judgment given in a dispute between the same parties. On the other hand, there are several grounds on which recognition and enforcement must be refused if, for instance, the foreign judgment was obtained by fraud in connection with a matter of procedure, or where it would be manifestly incompatible with the public policy of Singapore.

A final judgment for a sum of money obtained against a company in Singapore (which is not a judgment for the payment of a fine, penalty or tax, or anything of that nature) issued by New York courts will be enforced in Singapore in accordance with the common law. This is because there is no reciprocal agreement or convention between Singapore and the United States of America in respect of the enforcement of court judgments. Under the common law, a money judgment may be enforced, provided it is final and conclusive, and the foreign court had jurisdiction over the defendant in accordance with conflict principles recognised by the Singapore courts. It will then be for the defendant to prove that the New York courts had no jurisdiction over the matter, or that the judgment was obtained by fraud, or that there were any major procedural irregularities in arriving at the judgment or that enforcement would be contrary to the public policy of Singapore. The Singapore court will not re-examine the merits of the case.

7.3 Assuming a company is in payment default under a loan agreement or a guarantee agreement and has no legal defence to payment, approximately how long would it take for a foreign lender to (a) assuming the answer to question 7.1 is yes, file a suit against the company in a court in your jurisdiction, obtain a judgment, and enforce the judgment against the assets of the company, and (b) assuming the answer to question 7.2 is yes, enforce a foreign judgment in a court in your jurisdiction against the assets of the company?

The timeline for each case would depend on its own facts. Generally, if the claim is against a defendant in Singapore and based on a straightforward loan agreement or guarantee, it is possible to obtain default or summary judgment within three to six months of filing the claim (assuming there is no appeal).

There are generally four main methods of enforcement, namely, a writ of seizure and sale, garnishee proceedings, examination of judgment debtor and bankruptcy proceedings. Depending on which method of enforcement is selected and whether any challenge is mounted by the debtor, the process could take two to six months or longer.

In May 2017, the Companies (Amendment) Act 2017 (***Amendments***) came into effect. Modelled on chapter 15 of the U.S. Bankruptcy Code, and the UK Cross-Border Insolvency Regulations, the Amendments adopted the UNCITRAL Model Law on Cross-Border Insolvency to allow foreign insolvencies to be more easily recognised in Singapore.

7.4 With respect to enforcing collateral security, are there any significant restrictions which may impact the timing and value of enforcement, such as (a) a requirement for a public auction, or (b) regulatory consents?

There is no specific requirement for a public auction, although sale by public auction is commonly carried out as a matter of practice. Secured creditors typically have wide powers under the terms of the security document to take possession, dispose or otherwise deal with the secured assets, or appoint a receiver in respect of the secured assets, to satisfy the secured debts. There may be requirements for regulatory consent in respect of certain types of borrower (for example, where it is a regulated entity).

7.5 Do restrictions apply to foreign lenders in the event of (a) filing suit against a company in your jurisdiction, or (b) foreclosure on collateral security?

There are no specific restrictions on foreign lenders filing a suit or foreclosing on collateral security so long as the Singapore courts have jurisdiction over the matter.

7.6 Do the bankruptcy, reorganisation or similar laws in your jurisdiction provide for any kind of moratorium on enforcement of lender claims? If so, does the moratorium apply to the enforcement of collateral security?

The CA provides for an automatic moratorium where a provisional liquidation or liquidation order is made. Notwithstanding the moratorium, secured creditors may enforce their security in a provisional liquidation or liquidation.

The CA also provides for an automatic moratorium upon the making of an application for a judicial management order, and upon the making of a judicial management order. However, in these situations, a creditor may not enforce any security over the company's assets without permission from the court or the judicial manager.

The court may also grant a moratorium order if requested by an applicant proposing or intending to propose a scheme of arrangement. Generally, a temporary stay of proceedings does not restrict the enforcement of collateral security granted by the applicant. However, the Amendments give the court express power to also restrain the enforcement of security over the property of the applicant or any of its related companies.

The Amendments introduced an automatic 30-day stay that comes into effect on the filing of an application for a moratorium order. The Amendments also allow the moratorium to have worldwide or extraterritorial effect, if creditors are subject to the jurisdiction of the Singapore court.

7.7 Will the courts in your jurisdiction recognise and enforce an arbitral award given against the company without re-examination of the merits?

Arbitral awards may be recognised and enforced in Singapore in accordance with the New York Convention or under the Singapore

Arbitration Act (Cap. 10) without having its merits re-examined. However, the courts may refuse to enforce such awards on the following grounds: incapacity of a party; failure to give proper notice to a party or the inability of a party to present his/her case; issues with the selection of the arbitrators; the award falling outside of the scope of the arbitration agreement; invalidity of the arbitration agreement; the award having been set aside; and/or the enforcement of the award being contrary to the public policy of Singapore.

8 Bankruptcy Proceedings

8.1 How does a bankruptcy proceeding in respect of a company affect the ability of a lender to enforce its rights as a secured party over the collateral security?

Bankruptcy proceedings in respect of a company include receivership, winding up, schemes of arrangement and judicial management. The right to appoint a receiver over a company can arise statutorily, contractually in accordance with the terms of the security document such as a debenture or by an exercise by the court of its power to appoint a receiver on the application of the secured creditor. In such a case, the receiver would act in furtherance of the interests of the secured creditor that appointed the receiver to realise the collateral security. For restrictions on enforcing security in the context of liquidation, schemes of arrangement and judicial management, see question 7.6 above.

8.2 Are there any preference periods, clawback rights or other preferential creditors' rights (e.g., tax debts, employees' claims) with respect to the security?

Yes. Liquidators and judicial managers, but not receivers, can apply to set aside or clawback certain transactions entered into before commencement of winding up. Such transactions include transactions at an undervalue, preferences, avoidance of floating charges and unregistered charges and transactions defrauding creditors. The clawback period ranges from five years (transactions at an undervalue) to six months (preferences) from the commencement of winding up. Generally, floating charges created within six months of the commencement of winding up are invalid except to the amount of any cash paid to the company in consideration of the charge together with interest, unless there is proof that the company was solvent at the time the floating charge was created.

The CA also contains provisions against fraudulent trading, i.e. where the business of a company has been carried on with the intent to defraud creditors or for any fraudulent purpose. A liquidator can in such an instance apply for a declaration for the person/director to be personally responsible for the debts/liabilities of the company.

The tax authorities and employees who are owed wages (up to a certain limit) are preferential creditors and are paid ahead of unsecured creditors but behind secured creditors.

8.3 Are there any entities that are excluded from bankruptcy proceedings and, if so, what is the applicable legislation?

Entities incorporated in Singapore are generally not excluded from bankruptcy proceedings in Singapore.

8.4 Are there any processes other than court proceedings that are available to a creditor to seize the assets of a company in an enforcement?

See question 8.1 above. In addition, creditors may apply for a writ of seizure or to garnish the assets of the debtor.

9 Jurisdiction and Waiver of Immunity

9.1 Is a party's submission to a foreign jurisdiction legally binding and enforceable under the laws of your jurisdiction?

Yes, a party's submission to a foreign jurisdiction will generally be upheld as valid and binding in any action in the courts of Singapore provided that it is *bona fide* and there is no reason for avoiding such submission on the grounds of illegality or public policy.

In particular, where a party has submitted exclusively to the jurisdiction of a state that is party to the Hague Convention, the CCAA would apply and a Singapore court must stay or dismiss proceedings in the Singapore courts in favour of proceedings in the foreign court. This is subject to certain exceptions. For example, the CCAA does not apply to certain types of matters, such as insolvency matters and matters involving consumers. The Singapore court can also refuse to stay or dismiss proceedings in its courts if, for example, the agreement to submit to the foreign jurisdiction is null and void under the law of the foreign jurisdiction, or if giving effect to the agreement would lead to manifest injustice or would be manifestly contrary to the public policy of Singapore.

9.2 Is a party's waiver of sovereign immunity legally binding and enforceable under the laws of your jurisdiction?

A party's waiver of sovereign immunity may be legally binding and enforceable provided it satisfies the conditions as set out in the Singapore State Immunity Act (Cap. 313).

10 Licensing

10.1 What are the licensing and other eligibility requirements in your jurisdiction for lenders to a company in your jurisdiction, if any? Are these licensing and eligibility requirements different for a "foreign" lender (i.e. a lender that is not located in your jurisdiction)? In connection with any such requirements, is a distinction made under the laws of your jurisdiction between a lender that is a bank *versus* a lender that is a non-bank? If there are such requirements in your jurisdiction, what are the consequences for a lender that has not satisfied such requirements but has nonetheless made a loan to a company in your jurisdiction? What are the licensing and other eligibility requirements in your jurisdiction for an agent under a syndicated facility for lenders to a company in your jurisdiction?

Under Singapore law, unless exempted or excluded, a person may not carry on the business of a moneylender without holding the requisite moneylenders' licence. The relevant legislation, the

Moneylenders Act (Cap. 188) (***MA***), provides that any person who lends a sum of money in consideration of a larger sum being repaid (i.e. charge interest), shall be presumed until the contrary is proved to be a moneylender. The same prohibition would apply to a "foreign" lender who carries on the business of moneylending in Singapore from a place outside Singapore.

"Any person licensed, approved, registered or otherwise regulated by the MAS under any other written law", amongst others, would fall outside the ambit of the prohibition as an "excluded moneylender". These would include banks or finance companies which are licensed and regulated under the Banking Act (Cap. 19) and Finance Companies Act (Cap. 108) respectively. The question therefore is whether "foreign" lenders or other non-bank entities that are not so licensed, approved, registered or otherwise regulated by the MAS are necessarily excluded. With effect from 1 March 2009, an amended Moneylenders Act came into force in Singapore pursuant to which, amongst others, "any person who lends money solely to corporations" or "any person who lends money solely to accredited investors within the meaning of section 4A of the Securities and Futures Act (Cap. 289)" would be an "excluded moneylender". Accordingly, a lender can be an "excluded moneylender" provided on the facts it lends (and has lent) money solely to corporations or only to accredited investors.

There has been academic debate on whether a "foreign" unlicensed lender or other non-bank entity would not be deemed to be an excluded moneylender if it had in the past lent money otherwise to individuals who were not accredited investors. The prevailing view, however, is that the Singapore courts are unlikely to allow such a defence without more to succeed in the context of legitimate financial activity of commercial entities.

Corporations convicted of unlicensed moneylending will be imposed a fine of not less than S$50,000 and not more than S$500,000. In addition, subject to certain exceptions, the contracts for such loans, and guarantees or securities given for such loans shall be unenforceable, and any money paid by or on behalf of the unlicensed moneylender under the contracts for the loans will not be recoverable in any court of law.

The granting of loans to corporations *per se* is not otherwise regulated in Singapore. There are no eligibility requirements in Singapore for a lender lending to a company and, subject to the above, it need not be licensed or authorised provided that no other regulated activities (e.g. banking, securities or financial advisory activities) are being conducted.

11 Other Matters

11.1 Are there any other material considerations which should be taken into account by lenders when participating in financings in your jurisdiction?

The principal Singapore law considerations for lenders when participating in financings in Singapore have generally been covered by the above questions and answers.

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The authors would like to acknowledge the assistance of their colleague, Ong Ken Loon, in the preparation of this chapter. Ken Loon is the head of Tax & Private Client Services. She advises on tax aspects of corporate transactions, such as income tax, GST, stamp duty, and property tax. Ken Loon is recommended as one of Singapore's leading tax lawyers by *The Legal 500 Asia Pacific* and *Practical Law Company Which Lawyer?*

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Slovakia


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1 Overview

1.1 What are the main trends/significant developments in the lending markets in your jurisdiction?

The lending market in Slovakia maintains its growing trend, while lending conditions continue to improve. This results from favourable national, as well as global, economic developments and prospects of the Slovak economy. So far, credit conditions have continued to ease, however, in the housing sector, the National Bank of Slovakia has intervened in order to protect the market from overheating. We can see growth in corporate and consumer lending, and financing is generally available under reasonable terms. Despite this, we can also see increased use of alternative methods of financing such as issuance of corporate bonds. Furthermore, new methods of financing such as crowd funding and peer-to-peer funding are being explored.

1.2 What are some significant lending transactions that have taken place in your jurisdiction in recent years?

Several major real estate projects were realised in recent years (either residential or office/shopping park projects). Furthermore, re-financing transactions were also quite frequent due to favourable lending conditions.

2 Guarantees

2.1 Can a company guarantee borrowings of one or more other members of its corporate group (see below for questions relating to fraudulent transfer/financial assistance)?

Intra-group company guarantees are generally not prohibited under Slovak law. However, in certain situations, limitations or potential consequences arising under capital maintenance rules/financial assistance regulation may be triggered (see the answer to question 2.2 and Section 4 for more details).

2.2 Are there enforceability or other concerns (such as director liability) if only a disproportionately small (or no) benefit to the guaranteeing/securing company can be shown?

As of 1 January 2016, "company in crisis" regulation was introduced into the Slovak Commercial Code. It applies to limited liability companies, joint-stock companies and limited partnerships in which the general partner is not an individual.

A company is deemed to be in crisis when it is insolvent (within the meaning of the Insolvency Act) or at risk of becoming insolvent, which is the case if a company's equity (registered capital, reserve fund, other capital funds, etc.) to debt ratio is lower than 8/100.

The statutory body of a company in crisis is under a general duty of care and must take all steps that would normally be taken by a reasonably diligent person to overcome the crisis.

In addition to existing limitations on dividend payments, a company is prohibited to pay dividends if, given all circumstances, such payment would lead the company to crisis.

Additionally, loans and similar payments extended to a company in crisis by its statutory body (director), a proxy, a member of the supervisory board, a shareholder holding at least 5% of capital, or an associated person, are treated as equity under the special regime and any refund of such contributions by the company during the crisis is prohibited.

Further, when a security (guarantee, pledge, etc.) is provided by the above-mentioned persons to secure an obligation of a company in crisis, the company's creditor is entitled to be satisfied directly from such security, without the need to exercise its right against the company first (which would be the normal procedure). The above-mentioned persons may not be reimbursed for the provided security as long as the company remains in crisis or would become in crisis as a result.

2.3 Is lack of corporate power an issue?

The Slovak law does not recognise the *ultra vires* doctrine. Any internal limitations of power of the management are not effective *vis-à-vis* third parties, and do not affect the validity of agreements.

2.4 Are any governmental or other consents or filings, or other formalities (such as shareholder approval), required?

No governmental approvals or formalities are required. However, consent of the general meeting or the supervisory board, as the case may be, may be required if included in the constitutional documents of the respective company.

2.5 Are net worth, solvency or similar limitations imposed on the amount of a guarantee?

There are no such limitations imposed. However, for potential implications and triggering of company-in-crisis regulation, please see our response to question 2.2 above.

2.6 Are there any exchange control or similar obstacles to enforcement of a guarantee?

There are no exchange control or similar obstacles to enforcement of guarantee under Slovak law.

3 Collateral Security

3.1 What types of collateral are available to secure lending obligations?

It is possible to take security over all the assets of the Slovak company. The most common types of available security in Slovakia are as follows:

- share pledge;
- pledge over receivables;
- account pledge;
- mortgage (pledge over real property);
- pledge over IP;
- pledge over undertaking; and
- notarial deed on direct enforceability.

Assignment of the title or transfer of title is also possible but as a means of security is less frequently used in Slovakia. Therefore we do not elaborate on these instruments in detail.

3.2 Is it possible to give asset security by means of a general security agreement or is an agreement required in relation to each type of asset? Briefly, what is the procedure?

Slovak law does not recognise the concept of floating charge or blanket lien. Each type of asset has to be charged individually and specified accordingly in the agreement. It would be possible to combine various types of assets into one agreement, however, that is not the market practice and generally individual security agreements are concluded per each class of assets. The only exception is a share pledge agreement, which standardly also covers pledge over dividend payments connected with shares (which is basically a receivable). This is covered by one security agreement.

3.3 Can collateral security be taken over real property (land), plant, machinery and equipment? Briefly, what is the procedure?

Yes. All of the abovementioned assets can serve as security and are taken as standard collateral security. Slovak law differentiates between establishment of the security (in lending transactions, this would be conclusion of the security agreement) and creation of the security; creation is the subsequent perfection and registration in respective registers. The exception is pledge over movable assets which are to be handed over to the pledgee. In such case, the pledge is created via physical handover. However, in practice, such pledge is not used.

For security over real property, a security agreement in writing must be concluded. Slovak law does not set out any formal requirements for the agreement. But, sometimes lenders require that the signatures of the pledgors are verified by the notary. Pledge over real property (land, plants, buildings) is created via registration in the land registry. Please see answer to questions 3.9 and 3.10 for more information about fees and timing.

For machinery and equipment, the procedure is similar. First, a security agreement shall be concluded which specifies the assets which shall serve as security (please note that also future assets might be subject to a pledge). Subsequently the charge must be registered with the Notarial Central Register of Pledges. This can be done at any notarial office. Please note that for specific types of assets such as aircraft or naval vessels, etc., specific registers may exist where the charge shall be registered.

3.4 Can collateral security be taken over receivables? Briefly, what is the procedure? Are debtors required to be notified of the security?

Security over receivable is taken by way of pledge over receivable. In the first place, parties must conclude a written pledge agreement. For creation of the pledge, registration in the Notarial Central Register of Pledges is required. Notification of the debtors is not required for perfection. However, it will not become effective *vis-à-vis* the debtors until creation of the pledge is notified to them; i.e. until such notification, debtors could validly pay the pledgor.

Security in a form of security assignment is created by the security assignment agreement. No registration is required, but notification *vis-à-vis* the debtor is required in order for the agreement to be effective against debtor. This type of security is rarely used in Slovakia.

3.5 Can collateral security be taken over cash deposited in bank accounts? Briefly, what is the procedure?

Yes. Most commonly, this is done via account pledge agreement. The procedure basically follows the same regime as pledge over receivables. Written pledge agreement must be concluded and subsequently the pledge must be registered with the Notarial Central Register of Pledges.

3.6 Can collateral security be taken over shares in companies incorporated in your jurisdiction? Are the shares in certificated form? Can such security validly be granted under a New York or English law governed document? Briefly, what is the procedure?

Security over shares may be taken via share pledge agreement. The nature and form of shares depend on the type of the company.

Limited liability company: Shares of Slovak limited liability companies are constituted by participation (ownership) interests, which are not deemed to be securities. Therefore, they are not in a certified form. Pledge over participation interests is created via conclusion of a written pledge agreement and registration of the pledge with the Commercial Register.

Joint stock company: shares may be in the form of share certificates or dematerialised, bearer shares, recorded with the Central Depository. For creation of the pledge for either type, a share pledge agreement must be in place. Pledge is created via registration of the pledge with the Register of Pledges maintained by the Central Depository.

We are of the view that legally speaking, New York or English law governed pledge agreements are not *per se* prohibited and securities could be established under such documents. Nevertheless, certain registration requirements and mandatory provisions arising under conflict-of-law rules would need to be compliant with Slovak law. Therefore, this is hardly seen in Slovakia and, due to potential ambiguities and complications, it is not advisable.

3.7 Can security be taken over inventory? Briefly, what is the procedure?

Slovak law does not recognise the concept of floating charge. Therefore, security over inventory may be ensured via pledge over movable assets of the company (existing as well as future). The process is the same as with machinery.

3.8 Can a company grant a security interest in order to secure its obligations (i) as a borrower under a credit facility, and (ii) as a guarantor of the obligations of other borrowers and/or guarantors of obligations under a credit facility (see below for questions relating to the giving of guarantees and financial assistance)?

Subject to limitations and/or consequences described in questions 2.2 and 4.1, a company may secure both its own obligations as borrower, and as a guarantor of the obligations of other borrowers.

3.9 What are the notarisation, registration, stamp duty and other fees (whether related to property value or otherwise) in relation to security over different types of assets?

Slovak law does not impose any stamp duties in relation to security documents. Notarial fees and other registration fees are rather minor.

Fees for the notary for registration of the pledge in the Notarial Central Register of Pledges vary on the basis of the value of the secured obligation. However, the fee is capped at EUR 182.57.

Fee for registration of pledge (mortgage) with the land register is EUR 66 (for standard proceedings where the land registry has 30 days to register the pledge) or EUR 266 (for fast-track proceedings where the land registry shall make the registration within 15 days).

For registration of the pledge over participation interest in a limited liability company with the Commercial Register, the fee amounts to EUR 66.

3.10 Do the filing, notification or registration requirements in relation to security over different types of assets involve a significant amount of time or expense?

In general, filing, notification or registration requirements do not involve significant amounts of time or expense. The exception is registration of mortgage, which may take up to 30 days. Otherwise, registration of pledges with the Notarial Central Register of Pledges is finalised and pledges are registered on the day of registration. The Commercial Register shall register the pledge within two business days.

3.11 Are any regulatory or similar consents required with respect to the creation of security?

There are no general regulatory consent requirements. Only registration requirements must be fulfilled for creation of the security. For the sake of completeness, the consent of the general meeting of a company may be required, if required under constitutional documents. In case of assets owned/managed by the state or municipality, further requirements may be imposed (e.g. approval by local councils, etc.).

3.12 If the borrowings to be secured are under a revolving credit facility, are there any special priority or other concerns?

No, there are not. Security can be created also with regard to future receivables.

3.13 Are there particular documentary or execution requirements (notarisation, execution under power of attorney, counterparts, deeds)?

There are no particular documentary or execution requirements. Slovak law does not require that the security documents be executed in the form of a notarial deed. Only with respect to share pledge agreements do the signatures of the parties require notarisation (i.e. persons executing the document must be verified and confirmed by notary, and a notarial stamp confirming the identity of persons signing the document is subsequently attached thereto). Documents may be executed under the power of attorney, which usually requires notarisation and apostille or legalisation, as the case may be. The number of counterparts is left for determination by the parties.

4 Financial Assistance

4.1 Are there prohibitions or restrictions on the ability of a company to guarantee and/or give security to support borrowings incurred to finance or refinance the direct or indirect acquisition of: (a) shares of the company; (b) shares of any company which directly or indirectly owns shares in the company; or (c) shares in a sister subsidiary?

(a) Shares of the company

A Slovak joint stock company may not advance funds, make loans or give security to acquire its shares by third parties. Any agreements entered in violation of such rules are invalid. This does not apply to ordinary business of banks or acquisition of shares by or for employees, provided that the equity is not below the registered capital and the reserve fund.

In addition, there is general prohibition of acquisitions of own shares of the company, or giving security over own shares. Some exemptions apply here (e.g. mergers).

A Slovak limited liability company is not subject to explicit financial assistance rules. However, there is a direct liability of a company´s shareholders (and directors) for any damage caused to a company´s creditors by its insolvency. This rule may therefore result in comparable self-limitations in some cases. In addition, a general equal treatment rule also applies for all shareholders.

(b) Shares of any company which directly or indirectly owns shares in the company

In case of a joint stock company, the financial assistance rules also apply to the parent company in respect of acquisition of and/or securing shares of the subsidiary company. The Commercial Code defines a parent company in relation to its subsidiary company if, in general, it holds more than 50% shares or voting rights. The accounting or other laws may give an autonomous meaning to the parent company.

In case of a limited liability company, there are no such explicit rules. However, limitations described in (a) above may be relevant.

(c) Shares in a sister subsidiary

There are no explicit rules or case law regarding the acquisition of shares in sister subsidiaries (nor for a joint stock company, neither a limited liability company). General limitations, such as damage liability and equal treatment, may be relevant.

5 Syndicated Lending/Agency/Trustee/Transfers

5.1 Will your jurisdiction recognise the role of an agent or trustee and allow the agent or trustee (rather than each lender acting separately) to enforce the loan documentation and collateral security and to apply the proceeds from the collateral to the claims of all the lenders?

Even though the legal concept of a trustee or an agent is not recognised under Slovak law, lenders usually agree on a debt structuring and appoint a facility and/or security agent to represent them in all matters relating to finance and/or security documents. The scope of rights and obligations of the agent is a matter of commercial agreement and should be incorporated in the transaction documentation in detail.

5.2 If an agent or trustee is not recognised in your jurisdiction, is an alternative mechanism available to achieve the effect referred to above which would allow one party to enforce claims on behalf of all the lenders so that individual lenders do not need to enforce their security separately?

Please see the response to question 5.1 above.

5.3 Assume a loan is made to a company organised under the laws of your jurisdiction and guaranteed by a guarantor organised under the laws of your jurisdiction. If such loan is transferred by Lender A to Lender B, are there any special requirements necessary to make the loan and guarantee enforceable by Lender B?

Loans are usually transferred by assignment or novation.

To perfect the assignment of loan, the borrower/debtor must be notified thereof. Until the notification, the debtor may pay to the original lender. A consent of the borrower/debtor is not required unless agreed otherwise.

All security rights, including a guarantee (which is generally considered as an accessory claim), are automatically transferred by the time of assignment of the loan. The initial/original lender shall inform the guarantor (or party providing the security) on the assignment without undue delay in order to avoid the risk of fulfilling its guarantee to the initial/original lender. The change on the lender's side should be registered in respective securities registers (kept by notary, cadastral office, etc.).

In a novation, a new loan is created and agreement of all parties thereto is required. The securities shall secure the new loan automatically. However, if the guarantor or pledgors do not agree with the novation, then the existing collaterals continue to secure the novated claim only to the extent of the originally secured obligation.

6 Withholding, Stamp and Other Taxes; Notarial and Other Costs

6.1 Are there any requirements to deduct or withhold tax from (a) interest payable on loans made to domestic or foreign lenders, or (b) the proceeds of a claim under a guarantee or the proceeds of enforcing security?

Withholding tax applies on foreign lenders in Slovakia. Generally, interest paid by a Slovak tax resident to a Slovak tax non-resident is subject to withholding tax of 19%. However, interest payable to a resident of a country not specified in the so-called "white list" (the list published by the Slovak Ministry of Finance or a country with which Slovakia has not entered into a double tax treaty, or agreement on the exchange of information relating to taxes) is subject to a 35% tax rate. Tax exemption is applicable on interest payable to a non-resident, in accordance with the EU Directive on the common system of taxation applicable to interest and royalty payments.

Under certain circumstances, the other proceeds of a claim may also be subject to the withholding tax in Slovakia. The other proceeds do not have a statutory meaning. Therefore, all relevant aspects must be taken into account, especially if the other proceeds may be viewed as income similar to the interest.

6.2 What tax incentives or other incentives are provided preferentially to foreign lenders? What taxes apply to foreign lenders with respect to their loans, mortgages or other security documents, either for the purposes of effectiveness or registration?

No Slovak tax or other incentives are provided preferentially to foreign lenders. No taxes (such as stamp, issue, registration or similar taxes or duties) apply with respect to loan, mortgages or other security documents for the purpose of effectiveness or registration.

6.3 Will any income of a foreign lender become taxable in your jurisdiction solely because of a loan to or guarantee and/or grant of security from a company in your jurisdiction?

Income of a foreign lender will not become taxable in Slovakia solely because of a loan to or guarantee and/or, generally, the grant of security from a company in Slovakia, as long as they do not have a permanent establishment in Slovakia which is effectively connected to the proceeds of the loan, guarantee or security interest.

6.4 Will there be any other significant costs which would be incurred by foreign lenders in the grant of such loan/guarantee/security, such as notarial fees, etc.?

No. Please see answer to question 3.9 above.

6.5 Are there any adverse consequences to a company that is a borrower (such as under thin capitalisation principles) if some or all of the lenders are organised under the laws of a jurisdiction other than your own? Please disregard withholding tax concerns for purposes of this question.

Interest and related costs on borrowings and loans provided by related parties are tax-deductible at no more than 25% of adjusted

EBITDA (the total of the result of operations before tax, including depreciation charges and the interest expense).

Transfer pricing rules (which may require notification to the tax authority and preparation of transfer pricing documentation) apply to borrowings from foreign-affiliated lenders.

7 Judicial Enforcement

7.1 Will the courts in your jurisdiction recognise a governing law in a contract that is the law of another jurisdiction (a "foreign governing law")? Will courts in your jurisdiction enforce a contract that has a foreign governing law?

In general yes, the courts will recognise a foreign governing law. Regulation (EC) 593/2008 on the Law applicable to Contractual Obligations (Rome I) is directly applicable in Slovakia and parties are free to choose a governing law.

Therefore, subject to standard conflict-of-law rules such as overriding mandatory principles, public policy, etc., the courts in Slovakia will enforce a contract governed by the foreign law.

7.2 Will the courts in your jurisdiction recognise and enforce a judgment given against a company in New York courts or English courts (a "foreign judgment") without re-examination of the merits of the case?

In principle, yes. However, one should distinguish whether the foreign judgment was rendered by an EU Member State or non-EU Member State.

With respect to EU Member States, European regulation Brussels I is directly applicable and the Slovak courts should not re-examine the merits of the case.

As for foreign judgments rendered in non-EU Member States, such judgments may be refused only on limited grounds stated under the Act on Conflict of Laws or bilateral/international conventions. The decisions will be recognised and enforceable without re-examination if:

(a) Slovak courts do not have exclusive jurisdiction to decide the case;

(b) the decision is valid and effective (no further appeals available);

(c) the decision deals with the merits of the case (i.e. no preliminary decisions or dealing only with particular questions);

(d) the party's rights to a fair trial were not violated by the foreign body during the proceedings;

(e) the Slovak court did not render a valid and effective decision on the merits of the case or there is no former foreign decision which was already recognised; or

(f) it is not in contradiction with Slovak public order (*ordre publique*).

7.3 Assuming a company is in payment default under a loan agreement or a guarantee agreement and has no legal defence to payment, approximately how long would it take for a foreign lender to (a) assuming the answer to question 7.1 is yes, file a suit against the company in a court in your jurisdiction, obtain a judgment, and enforce the judgment against the assets of the company, and (b) assuming the answer to question 7.2 is yes, enforce a foreign judgment in a court in your jurisdiction against the assets of the company?

It is difficult to assess, as there are various aspects and factors such as workload of the courts, complexity of the case etc., which would influence the duration.

In simple matters with respect to letter a), it may be up to a year and half. With respect to letter b), the enforcement proceeding, if not contested, may take up to six months depending on the type of assets and cooperation of the company.

However, the timing may be substantially longer.

Please note that in lending transactions in Slovakia, lenders require as a collateral notarial deed on direct enforceability. If such document is executed, then lenders are not required to go to court in order to obtain an enforcement title. Rather they may proceed with enforcement on the basis of the notarial deed. Furthermore, for enforcement of security in a form of a pledge, one does not need to go to a court to obtain any judicial decision but may initiate enforcement of the pledge out of court directly.

7.4 With respect to enforcing collateral security, are there any significant restrictions which may impact the timing and value of enforcement, such as (a) a requirement for a public auction, or (b) regulatory consents?

Slovak law allows for out-of-court enforcement of collateral security in a form of pledges. There are no significant restrictions and no judicial document is required in order to proceed with such enforcement. The condition for such enforcement is notification about commencement of the enforcement and its registration with respective registers, as the case may be. After such notification, at least 30 days need to lapse before actual commencement of the enforcement of the pledge.

Parties are free to agree on the method of enforcement, i.e. direct sale is allowed and the asset does not have to be sold via public auction. Nevertheless, public auction is a standard method of enforcement in Slovakia, and frequently used.

7.5 Do restrictions apply to foreign lenders in the event of (a) filing suit against a company in your jurisdiction, or (b) foreclosure on collateral security?

In general, no; no distinction is made between domestic and foreign lenders.

7.6 Do the bankruptcy, reorganisation or similar laws in your jurisdiction provide for any kind of moratorium on enforcement of lender claims? If so, does the moratorium apply to the enforcement of collateral security?

The commencement of bankruptcy proceedings triggers automatic stay of enforcement with respect to lender claims and collateral security. This does not apply to enforcement of account pledge or enforcement of pledge over transferable securities and enforcement via public auction.

7.7 Will the courts in your jurisdiction recognise and enforce an arbitral award given against the company without re-examination of the merits?

Under Slovak law, an arbitral award is deemed to have the same effects as the judgment of the court.

Slovakia is a party to the New York Convention on Arbitration of 1958. Slovak courts shall not re-examine the merits of the case. However, there are certain grounds for which the recognition and enforcement may be refused (e.g. the arbitration agreement is not valid, irregularities with composition of the tribunal, etc.). An award would not be recognised if the subject matter cannot be settled by arbitration in Slovakia or if the award goes against public policy.

8 Bankruptcy Proceedings

8.1 How does a bankruptcy proceeding in respect of a company affect the ability of a lender to enforce its rights as a secured party over the collateral security?

Please see the response to question 7.6. Commencement of bankruptcy proceedings triggers automatic stay of enforcement proceedings.

8.2 Are there any preference periods, clawback rights or other preferential creditors' rights (e.g., tax debts, employees' claims) with respect to the security?

The insolvency administrator or creditor may contest legal actions of the insolvent party subject to certain statutory requirements. Such clawback right shall be applied at latest within one year from commencement of the bankruptcy proceedings, otherwise it ceases to exist. Time spans depend on the nature and ground of challenge.

The insolvency administrator may challenge legal actions on the following grounds: i) the legal action was without adequate consideration; ii) the legal action was beneficial only to one creditor; iii) the challenged legal action is "shortening" other creditors; and iv) legal action was taken after the bankruptcy proceedings.

The insolvency administration may challenge legal actions on the grounds under i) and ii) if the legal action occurred one year (three years in case of related parties transactions) prior to commencement of the bankruptcy proceedings. The insolvency administration may challenge legal actions which occurred up to five years prior to commencement of the bankruptcy on the grounds under iii).

8.3 Are there any entities that are excluded from bankruptcy proceedings and, if so, what is the applicable legislation?

Certain entities governed by public law, such as state, state entities, municipalities, etc. are excluded from the application of Slovak bankruptcy law.

8.4 Are there any processes other than court proceedings that are available to a creditor to seize the assets of a company in an enforcement?

Pledges may be enforced without initiating any court proceedings directly by the creditor(s). In such case, the creditor is acting on behalf of the borrower and enforces the pledge via an agreed method of enforcement contained in the pledge agreement (e.g. direct sale, public auction, etc.). Notarial deed on direct enforceability is an enforcement title as well, and the creditor does not need to go to court in order to enforce its claim.

9 Jurisdiction and Waiver of Immunity

9.1 Is a party's submission to a foreign jurisdiction legally binding and enforceable under the laws of your jurisdiction?

In general, yes. Slovak courts will decline jurisdiction if parties agree that a foreign court is to have an exclusive jurisdiction. Slovak courts may, however, seize jurisdiction if, for example: i) Slovak courts should have exclusive jurisdiction, such as disputes relating to rights *in rem*; ii) employment, consumer or insurance contracts; iii) the defendant has already taken steps and initiated the proceedings with Slovak courts; or iv) if the Slovak courts would deem them to be an appropriate forum to hear the case.

9.2 Is a party's waiver of sovereign immunity legally binding and enforceable under the laws of your jurisdiction?

A waiver of sovereign immunity is generally legally binding, unless: (i) it conflicts with public international law; or (ii) covers areas that are specifically protected by international law.

10 Licensing

10.1 What are the licensing and other eligibility requirements in your jurisdiction for lenders to a company in your jurisdiction, if any? Are these licensing and eligibility requirements different for a "foreign" lender (i.e. a lender that is not located in your jurisdiction)? In connection with any such requirements, is a distinction made under the laws of your jurisdiction between a lender that is a bank *versus* a lender that is a non-bank? If there are such requirements in your jurisdiction, what are the consequences for a lender that has not satisfied such requirements but has nonetheless made a loan to a company in your jurisdiction? What are the licensing and other eligibility requirements in your jurisdiction for an agent under a syndicated facility for lenders to a company in your jurisdiction?

A banking licence will be required only if the lender conducts banking activities as defined under the Slovak Act on Banks or if other conditions set out under the Slovak Act on Banks are met. According to the Slovak Act on Banks, no person may provide, without a banking licence, loans or credits as part of its business or other activity by using repayable funds obtained from other persons on the basis of a public offer. Furthermore, consumer loans may be provided only under the special licence issued by the National Bank of Slovakia.

If the lender provides loans: i) in Slovakia; ii) on a continuous basis; iii) in its own name, at own responsibility; and iv) with the aim to achieve profit, then a free trade licence may be required even if a banking licence would not be required (the activity would qualify as conducting business for which a trade licence is required).

A banking licence is not required for banks which obtained their banking licence in different EU Member States. Such lenders may passport their licence under EU regulation.

There are no different requirements for foreign lenders and local lenders. If the company provides loans without a licence, it may face fines or may commit a crime of unlawful undertaking. There are no eligibility requirements for an agent and generally, such role does not trigger any licensing requirements.

11 Other Matters

11.1 Are there any other material considerations which should be taken into account by lenders when participating in financings in your jurisdiction?

Special and material considerations might be required depending on the structure and nature of the transaction. In any event, consultation with local counsels is recommended.

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ŠKUBLA & PARTNERI

ADVOKÁTSKA KANCELÁRIA | LAW FIRM

The Law firm Škubla & Partneri is one of the largest law firms in Slovakia (consisting of more than 20 legal professionals) providing legal services in various areas of law. In particular, it renders its services in the field of corporate law, competition law, private equity, disputes and arbitration, banking and finance, real estate and construction law, and civil law. We are renowned for our client-friendly and proactive approach, high degree of expertise and level of specialisation. In the fields of banking finance, the Law firm Škubla & Partneri regularly advises and participates in major local lending transactions, mostly representing borrowers.

Slovenia

Andraž Jadek

Jadek & Pensa

Žiga Urankar

1 Overview

1.1 What are the main trends/significant developments in the lending markets in your jurisdiction?

Following the setback during the economic and financial crisis, the economic situation in Slovenia continued to improve in 2017. The value of the composite Economic Sentiment Indicator almost reached pre-2008 levels. The economic forecast for Slovenia is also optimistic. In November 2017, the European Commission forecast that the GDP growth in 2018 in Slovenia will be 4.0%, the third highest in the European Union.

Furthermore, the volume of loans to domestic non-banking sector increased in 2017 for the first time since 2010. Favourable economic conditions contributed to growth in corporate loans and loans to non-monetary financial institutions. In the last few years, enterprises have increased the demand for investment loans and working capital loans, while the demand for loans for refinancing has eased.

On the other hand, continued uncertainty surrounding the details of Brexit and the 2018 parliamentary elections in Slovenia may adversely affect the economic situation and increase volatility in lending markets in Slovenia.

2 Guarantees

2.1 Can a company guarantee borrowings of one or more other members of its corporate group (see below for questions relating to fraudulent transfer/financial assistance)?

Two most common forms of companies in Slovenia are the limited liability company (*družba z omejeno odgovornostjo*) and the stock corporation (*delniška družba*). While both company forms are regulated under the Companies Act, there are several differences regarding the rules that apply individually.

LLCs. Entering into a guarantee agreement by an LLC to guarantee borrowings of its subsidiary (i.e. a downstream guarantee) is legally permissible and generally unproblematic. However, when providing a guarantee for borrowings of its shareholders or their subsidiaries (i.e. an upstream guarantee or cross-stream guarantee), an LLC must abide by the capital maintenance rules applicable under the Companies Act and receive appropriate consideration. According to the prevailing theory (referencing German legal theory), the entry into a guarantee agreement securing obligations of a shareholder can on its own breach the capital maintenance rules of an LLC before any payments are made through enforcement of security. The capital maintenance rules prohibit the LLC from making payments or other distributions of value to its shareholders from the assets required for preservation of its share capital and restricted capital reserves. The recipient of the prohibited capital distribution must be in bad faith. Financial institutions acting as lenders are held to a higher standard of diligence and annual reports of LLCs are publicly available in Slovenia. Therefore, a balance sheet test must be made to determine whether the value of the security (i.e. guarantee) exceeds the amount of free reserves available for distribution. If that amount was exceeded and the recipient was in bad faith, giving of such security is prohibited and the guarantee agreement would be null and void.

Corporations. Slovenian capital maintenance rules are much stricter for corporations than LLCs. Under the Companies Act, any distribution of capital to shareholders outside the distribution of dividends is prohibited. This rule does not restrict corporations giving downstream guarantees, which are legal and generally unproblematic. However, upstream and cross-stream guarantees made by corporations are generally prohibited in absolute terms. Most notably, the exception of a guarantee made under an applicable group controlling agreement may apply.

The above rules apply to both guarantees and other forms of security agreements.

2.2 Are there enforceability or other concerns (such as director liability) if only a disproportionately small (or no) benefit to the guaranteeing/securing company can be shown?

Members of management and supervisory boards are jointly and severally liable to the company for damages arising from violation of their duties, unless they can demonstrate that they fulfilled their duties fairly and conscientiously. Therefore, when a guarantee is not made under arm's length terms and in violation of the capital maintenance rules described under question 2.1 above, this can be ground for directors' liability. If in order to implement the transaction the controlling company, through its legal representatives or otherwise, used its controlling influence and caused the subsidiary to consent to a transaction that is harmful, this may generate a loss, which the controlling company has to compensate unless a controlling contract was in place. If the loss is not compensated during the financial year, this must be determined and appropriately reported and audited. Legal representatives of the controlling company may be held liable for all damages caused to the subsidiary if the loss from a harmful transaction which was induced upon the subsidiary was not timely compensated as provided under the Companies Act. Compensation claims of the subsidiary may also be pursued by its creditors, if the subsidiary is unable to repay them.

Guarantees that breach capital maintenance rules are null and void and thus cannot be enforced by the lender.

2.3 Is lack of corporate power an issue?

Under the Companies Act, legal transactions entered into by a company with third parties which are beyond the scope of the company's activity laid down by its articles or memorandum of association (i.e. *ultra vires*) or permitted transactions shall be valid unless a third party was aware or should have been aware of such fact. The indication of activities in articles or memorandum of association shall not mean that a third party was aware or should have been aware of this fact. Note, however, that in legal theory this limitation is considered mainly as an internal limit of powers of the company's bodies. Therefore, in practice, the "awareness criterion" has limited relevance.

2.4 Are any governmental or other consents or filings, or other formalities (such as shareholder approval), required?

Executive directors do not need shareholder or any other approval to grant guarantees as this falls within their general corporate powers. That said, directors may avoid liability for damages arising from the grant of a guarantee if they acted based on a lawful shareholder resolution. Approval of the transaction by the management or supervisory board does not relieve the executive directors of their liability. This applies to both LLCs and corporations.

Insolvent companies may not grant guarantees and a debtor in a bankruptcy procedure requires consent of the court.

2.5 Are net worth, solvency or similar limitations imposed on the amount of a guarantee?

See the answers to questions 2.1 and 2.2 above.

2.6 Are there any exchange control or similar obstacles to enforcement of a guarantee?

There are presently no exchange or asset controls in Slovenia. As Slovenia is a member of the Economic and Monetary Union, any exchange controls are imposed by the ECB. The Regulation (EC) No 1889/2005 on controls of cash entering or leaving the Community imposes controls on cash and other securities. Other asset controls may be imposed on the basis of the Slovenian Prevention of Money Laundering and Terrorist Financing Act.

3 Collateral Security

3.1 What types of collateral are available to secure lending obligations?

Under Slovenian law, the following types of collateral are most commonly used:

Real estate

- mortgage; and
- maximum mortgage.

Motor- and rail vehicles, equipment, inventory, and certain types of animals

- pledge (possessory or non-possessory by registration); and
- fiduciary transfer of title.

Other movables

- pledge (possessory or non-possessory); and
- fiduciary transfer of title.

Shares

- pledge; and
- fiduciary assignment.

Receivables

- pledge; and
- fiduciary assignment.

Cash account

- pledge; and
- fiduciary assignment.

Intellectual property

- pledge; and
- fiduciary assignment.

3.2 Is it possible to give asset security by means of a general security agreement or is an agreement required in relation to each type of asset? Briefly, what is the procedure?

Under Slovenian law, it is not possible to give security over assets by means of a general security agreement. The concept of a floating charge is not recognised and a separate security agreement normally needs to be entered into with regard to each individual asset class.

However, a so-called general fiduciary assignment is possible with respect to fiduciary assignment of receivables, where security may be created over all existing and future receivables of an assignor and/or its legal relationships. A general fiduciary assignment is ordinarily entered into in the form of a written contract even though no specific form is legally required. For the assignee to obtain the right to a separate settlement in insolvency of the assignor, the security agreement shall be concluded in the form of a notarial deed.

Similarly, a pledge over inventory has certain elements of general security, since the description of individual parts is not required to create security. Such collateral remains valid despite subsequent changes in inventory.

3.3 Can collateral security be taken over real property (land), plant, machinery and equipment? Briefly, what is the procedure?

Collateral security can be taken over real estate (land) and movables (including equipment, plant and machinery) that do not constitute a fixture. Special regulation applies to collateral security over motor- and rail vehicles, certain types of animals, ships, and aircraft.

Real estate. The security on real estate is a mortgage which is an accessory security right. This means that it secures a specific secured obligation and ceases by operation of law when the secured obligation is repaid or otherwise terminates. The mortgage needs to be perfected by entry into the land register. The mortgage agreement shall be concluded in a written form with the signature of the pledger notarised. For the mortgage to be directly enforceable it shall be entered into in the special form of a directly enforceable notarial deed.

Mortgages are often created in the form of a maximum mortgage where all existing and future claims arising from specific business relationships are secured by the same mortgage on real estate up to a specific secured amount. Maximum mortgages are most often used for securing revolving credit facilities. For the maximum mortgage to be directly enforceable it shall be entered into in the special form of a directly enforceable notarial deed. In addition, the outstanding amounts of secured obligations also have to be recognised in the form of the notarial deed.

Equipment, plant and machinery, motor- and rail vehicles, and animals. Both, possessory and non-possessory pledges can be created over these movables. Non-possessory pledges over equipment, motor- and rail vehicles, and certain animals (cattle and equines) can be registered in the public register in Slovenia. Such registration legally perfects the pledge and unique identifiers are assigned in the process. The registration has the effect of publicity against third persons, resulting in the presumption of bad faith with respect to registered collateral. Non-possessory pledge on these assets is not valid without a security agreement in the form of a directly enforceable notarial deed and registration. Collateral is created at the time of an entry into the register. Registrations are normally done by notaries, but pledges may also be registered by enforcement officers, tax collectors, courts or other public authorities in certain instances. For fees, see question 3.9 below.

A separate and specialised register also exists for non-possessory pledges on ships and aircrafts. A similar regime applies for perfection of security over these two types of assets.

A possessory pledge on a movable is created when a pledger delivers the pledged movable into the direct possession of the pledgee or a third person such that only the pledgee can demand its delivery. Written form is required only if out-of-court sale of the collateral was agreed.

3.4 Can collateral security be taken over receivables? Briefly, what is the procedure? Are debtors required to be notified of the security?

Collateral security can be taken over receivables in the form of a pledge or fiduciary assignment.

Pledge. There is no special formal requirement for creation of a pledge on receivables, but normally a written pledge agreement is entered into. Notarisation is not required. The pledge is validly created once the debtor is notified of the pledge. Until such notification, the pledge does not legally exist.

Fiduciary assignment. Even though no special form is required, fiduciary assignment is at the minimum entered into in the form of a written contract. For the assignee to obtain the right to separate settlement in insolvency of the assignor, the security agreement shall be concluded in the form of a notarial deed. Therefore, in practice, all fiduciary assignment agreements are concluded in such from.

Fiduciary assignment is valid upon execution of the contract. Neither confirmation nor notification of the debtor are prerequisites for perfection. A good faith debtor is entitled to discharge its debt to the assignor until he has been notified of the assignment. Therefore, in practice, notification to the debtor is advisable.

Financial collateral agreements. Note that both Directive 2002/47/EC on financial collateral arrangements and subsequently adopted Directive 2009/44/EU were transposed into Slovenian legislation with the Financial Collateral Act. The Financial Collateral Act applies to collateral agreements between certain participants in the financial market, *inter alia*, (i) public authorities, central banks, credit institutions, insurance companies, investment funds, management companies on one hand, and (ii) large, mid-sized and small companies on the other hand. The Financial Collateral Act regulates both pledges on and fiduciary assignments of financial instruments, cash and credit claims.

The following special rules apply:

- a maximum pledge can be created over financial instruments, cash and credit claims recorded in a register under the rules applicable to maximum mortgage;
- an out-of-court sale of the pledged financial instruments and credit claims is permitted without specific requirements or restrictions (such as prior notice, waiting period, public auction or consent);
- fiduciary assigned financial instruments, cash and credit claims may in case of default be retained, sold, and/or set-off by the lender;
- financial collateral agreements and rights arising from them (including enforcement and set-off rights) remain in full force and effect even after insolvency proceeding is initiated against the debtor; and
- conditions for challenging of financial collateral in insolvency are more restrictive.

3.5 Can collateral security be taken over cash deposited in bank accounts? Briefly, what is the procedure?

Collateral security in the form of a pledge or fiduciary assignment can be taken over cash deposited in bank accounts.

A pledge or fiduciary assignment of deposited cash is a pledge or assignment of receivables, therefore the general procedure and specific regulation under the Financial Collateral Act as described in question 3.4 above apply.

3.6 Can collateral security be taken over shares in companies incorporated in your jurisdiction? Are the shares in certificated form? Can such security validly be granted under a New York or English law governed document? Briefly, what is the procedure?

Collateral security can be taken over shares in companies incorporated in Slovenia in the form of a pledge or through fiduciary assignment, whereas the pledge is the predominant type of security over shares used in Slovenia.

Neither business shares in LLCs nor shares in corporations are in certified form. While shares in LLCs do not legally constitute securities, corporations issue shares in dematerialised form which are registered in a securities registry administered by the Slovenian Securities Depository.

New York or English law may govern the respective pledge or fiduciary assignment over shares so long as mandatory provisions of Slovenian law governing the creation, perfection and enforcement of such collateral security are complied with.

LLCs. The pledge agreement must be concluded in the form of a notarial deed and the pledge must be entered into the court register. The same rules apply to fiduciary assignment.

Corporations. Pledges over shares in corporations are validly created and perfected by registration in the securities register. The pledge is registered based on the order of the titleholder. Pledged shares may not be disposed of without express permission of the pledgee, but the pledger retains the voting rights. All dividends and other payments belong and are paid to the pledgee, but the parties may agree that the profit distributions are passed to the pledger. The fiduciary assignment is created and perfected by the order to transfer the shares. For specific rules under the Financial Collateral Act, see question 3.4 above.

3.7 Can security be taken over inventory? Briefly, what is the procedure?

Collateral security can be taken over inventory in the form of a pledge or non-possessory pledge by registration. The same regime as described in question 3.3 above applies.

3.8 Can a company grant a security interest in order to secure its obligations (i) as a borrower under a credit facility, and (ii) as a guarantor of the obligations of other borrowers and/or guarantors of obligations under a credit facility (see below for questions relating to the giving of guarantees and financial assistance)?

Yes, subject to the limitation described in questions 2.1 and 2.2 above.

3.9 What are the notarisation, registration, stamp duty and other fees (whether related to property value or otherwise) in relation to security over different types of assets?

There are no stamp duties or taxes applicable to creation or perfection of security over assets in Slovenia.

Both notary and court register fees apply for creation of collateral security.

A notary fee of up to EUR 1,000 would apply for a security agreement concluded in the form of a notarial deed. The fee depends on the value of the secured obligations. In addition, a fee of EUR 0.50 per page of counterpart issued by the notary to the parties applies. Notaries are also entitled to reimbursement of actual costs or the lump-sum amount of 2% of the first EUR 459 and 1% of the excess, if the actual costs cannot be determined.

The following additional fees apply in relation to the following collateral security:

Security over real estate (mortgages). A filing fee of EUR 37 applies for each entry into the land register by a notary and a court fee of EUR 50 applies to each land register procedure. In addition, a fee of EUR 23 applies for each review of the land register before registration by the notary.

Non-possessory pledges. A registration fee of up to EUR 50 applies.

Security over shares in LLC. A fee of EUR 37 applies for each entry into the court register by a notary. A fee of EUR 23 also applies for each review of the court register before registration by the notary.

Security over intellectual property. A fee of up to EUR 70 applies if security is created by registration in the intellectual property register.

3.10 Do the filing, notification or registration requirements in relation to security over different types of assets involve a significant amount of time or expense?

Regarding expenses, please see qurestion 3.9 above.

The registration of collateral security over real estate (mortgage) normally takes up to one month, provided that there are no unresolved entries and notices of pending actions in the land register on the applicable real estate. Any pending entries and notices can prolong the procedure substantially. Perfection of collateral security on shares normally takes up to one week and registration in the non-possessory register shall generally be concluded within two weeks.

3.11 Are any regulatory or similar consents required with respect to the creation of security?

No such regulatory consents are required in Slovenia.

3.12 If the borrowings to be secured are under a revolving credit facility, are there any special priority or other concerns?

There are no such special priority or other concerns in Slovenia.

With real estate in most cases revolving credit facilities are secured by a maximum mortgage, which secures all existing and future claims arising from a specific business relationship. For details see question 3.3 above.

3.13 Are there particular documentary or execution requirements (notarisation, execution under power of attorney, counterparts, deeds)?

Regarding notarisation, see questions 3.3, 3.4 and 3.6 above.

Powers of attorney must be in the same form as the security agreement (i.e. if the security agreement needs to be notarised, so does the power of attorney).

Foreign entities are entered into the land register as pledgees with a special Slovenian identification number which needs to be obtained in advance.

4 Financial Assistance

4.1 Are there prohibitions or restrictions on the ability of a company to guarantee and/or give security to support borrowings incurred to finance or refinance the direct or indirect acquisition of: (a) shares of the company; (b) shares of any company which directly or indirectly owns shares in the company; or (c) shares in a sister subsidiary?

(a) Shares of the company

LLCs. Apart from the obligation to comply with the capital maintenance rules (described in question 2.2 above), Slovenian law prescribes no further prohibitions or restrictions on the ability of an LLC to guarantee and/or give security to support borrowings incurred to finance or refinance the direct or indirect acquisition of its shares.

Corporations. Under the Companies Act, a legal transaction by which a corporation secures an advance payment or a loan for the acquisition of its shares or any other transaction with a comparable effect shall be null and void. According to the case law, giving of a guarantee or providing collateral over its assets is considered a transaction with a comparable effect that is prohibited. Therefore, a guarantee and/or security to support borrowings incurred to finance or refinance the direct or indirect acquisition of shares in a corporation is null and void.

(b) Shares of any company which directly or indirectly owns shares in the company

Same as the answer to (a) above.

(c) Shares in a sister subsidiary

Same as the answer to (a) above.

5 Syndicated Lending/Agency/Trustee/Transfers

5.1 Will your jurisdiction recognise the role of an agent or trustee and allow the agent or trustee (rather than each lender acting separately) to enforce the loan documentation and collateral security and to apply the proceeds from the collateral to the claims of all the lenders?

The roles of agents and trustees as they are normally undertaken by them in syndicated lending transactions are not statutorily regulated as special legal concepts in Slovenia. Therefore, the parties cannot rely on a developed legal framework tailored for this purpose. That said, there are no rules that would prohibit or limit the contractual appointment of an agent or trustee to such roles and authorising them to enforce the loan documentation and collateral security and to apply the proceeds from the collateral to the claims of all the lenders.

5.2 If an agent or trustee is not recognised in your jurisdiction, is an alternative mechanism available to achieve the effect referred to above which would allow one party to enforce claims on behalf of all the lenders so that individual lenders do not need to enforce their security separately?

While the concept of parallel debt is not explicitly regulated by Slovenian law, the view of the legal theory is that the creation of "quasi" parallel debt structures in Slovenia shall be permissible as an available alternative mechanism either by creation of joint and several claims or parallel collective claims of the agent or trustee. Since there is no authoritative case law on the validity of such parallel debt arrangements, it is not possible to maintain that such structures would indeed be fully valid and enforceable in all respects. Lenders therefore in general avoid relying on parallel debt of the agents and arrange for creation, perfection and enforcement of security for their individual secured claims whereby agents or trustees are appointed and authorised to act on behalf of all lenders in enforcement of their security as authorised representatives.

5.3 Assume a loan is made to a company organised under the laws of your jurisdiction and guaranteed by a guarantor organised under the laws of your jurisdiction. If such loan is transferred by Lender A to Lender B, are there any special requirements necessary to make the loan and guarantee enforceable by Lender B?

While neither confirmation by nor notification to the debtor or guarantor about the transfer of the loan receivables are a prerequisites for perfection of such transfer, a debtor and the guarantor acting in good faith are entitled to discharge its debt to the original lender until he has been notified of the assignment.

Guarantees are accessory to loans and are automatically transferred to the assignee together with the assigned loan receivable. Therefore, no additional requirements other than notification as described above are necessary for the guarantee to be enforceable after the assignment.

Note that the transfer of the whole loan and/or guarantee agreement and relationship requires prior consent of the debtor and guarantor to be valid and enforceable. Such consent shall be given in the same form as the underlying agreement. Therefore, most loan and guarantee transfers are made through assignment.

6 Withholding, Stamp and Other Taxes; Notarial and Other Costs

6.1 Are there any requirements to deduct or withhold tax from (a) interest payable on loans made to domestic or foreign lenders, or (b) the proceeds of a claim under a guarantee or the proceeds of enforcing security?

Generally, the debtor is liable to deduct or withhold the tax from interest on loans when they are paid by a Slovenian tax resident or by a Slovenian permanent establishment of a foreign tax resident. Proceeds of a claim under a guarantee or the proceeds of enforcing security are subject to withholding tax, if they have the nature of interest. Interest shall comprise the income arising from all types of receivables, regardless of whether they are collateralised with a mortgage, and interest arising from all debt securities and other debt financial instruments, including premiums and bonuses belonging to such securities and financial instruments, other than interest for late payment. Under the Slovenian domestic law, tax at a rate of 15% shall be withheld when making the payment to a corporate taxpayer and at a rate of 25% for payments to individual taxpayers.

6.2 What tax incentives or other incentives are provided preferentially to foreign lenders? What taxes apply to foreign lenders with respect to their loans, mortgages or other security documents, either for the purposes of effectiveness or registration?

Tax exemption may apply (i) when the payment is made to a tax resident of Slovenia (corporate taxpayer) or to a Slovenian permanent establishment of a foreign tax resident (corporate taxpayer), (ii) when conditions under the EU Interest & Royalty Directive and/or under Double Tax Treaties are met, and (iii) if there are special regulations on withholding tax on interest arising from debt securities which have been issued by Slovenian business entities.

No taxes (such as stamp duty and similar) apply with respect to loans, mortgages, securities or other similar documents.

6.3 Will any income of a foreign lender become taxable in your jurisdiction solely because of a loan to or guarantee and/or grant of security from a company in your jurisdiction?

Income of a foreign lender shall not become taxable in Slovenia solely because of a loan to or guarantee and/or grant of security from a company in the Slovenian jurisdiction, provided that (i) the incomes are not related to the activities of a Slovenian permanent establishment of a foreign lender or the foreign lender is not a tax resident of Slovenia, and/or (ii) the incomes are not considered as Slovenian-source incomes.

6.4 Will there be any other significant costs which would be incurred by foreign lenders in the grant of such loan/guarantee/security, such as notarial fees, etc.?

Costs of foreign lenders generally will not differ significantly from costs of domestic lenders. See question 3.9 above on fees.

Additional costs to foreign lenders may arise due to the fact that all security documentation necessary for registration must be submitted to the Slovenian authorities in the Slovenian language. Notarial deeds are also entered into primarily in the Slovenian language. Costs of official translations may therefore apply.

6.5 Are there any adverse consequences to a company that is a borrower (such as under thin capitalisation principles) if some or all of the lenders are organised under the laws of a jurisdiction other than your own? Please disregard withholding tax concerns for purposes of this question.

No, generally there are no such adverse consequences under Slovenian law.

7 Judicial Enforcement

7.1 Will the courts in your jurisdiction recognise a governing law in a contract that is the law of another jurisdiction (a "foreign governing law")? Will courts in your jurisdiction enforce a contract that has a foreign governing law?

In Slovenia, the conflict of laws regime is governed by a directly applicable EU Regulation (EC) 593/2008 on the Law applicable to Contractual Obligations (Rome I Regulation), which accordingly also governs the choice of law rules. Subject to limitations set forth in Rome I Regulation, courts in Slovenia will therefore recognise and enforce contracts that have a foreign governing law.

7.2 Will the courts in your jurisdiction recognise and enforce a judgment given against a company in New York courts or English courts (a "foreign judgment") without re-examination of the merits of the case?

Judgments of courts of EU Member States (e.g. England, as of now). For these judgments, Regulation (EU) No 1215/2012 on jurisdiction and the recognition and enforcement of judgments in civil and commercial matters (recast) (Brussels I Regulation) shall apply.

Under Article 36 of Brussels I Regulation, a judgment of a court shall be recognised in the other Member States without any special procedure. As for the enforcement, under Article 39 of Brussels I Regulation, a judgment of a court of an EU Member State, which is enforceable in that Member State, shall be enforceable in other Member States without a declaration of enforceability. That said, all the grounds for refusal or suspension of enforcement under the law of the Member State addressed shall generally apply (subject to certain exceptions from Brussels I Regulation).

According to Brussels I Regulation any interested party can apply for refusal of recognition or enforcement of a judgment of a court of an EU Member State. Such application can, however, be made on very limited grounds (e.g. based on arguments of public policy (*ordre public*), due process or irreconcilable judgments (*res judicata*)).

Judgments of courts of non-EU countries (e.g. New York). For these judgments, the Slovenian Private International Law and Procedure Act shall apply. A special recognition procedure needs to be carried out to recognise such foreign judgments. The recognition procedure is very limited in scope, as the judgment will not be recognised only for explicitly quoted reasons (e.g. if the effect of recognition would run counter to the public order of Slovenia (*ordre public*), if exclusive jurisdiction over the matter involved lies with Slovenian courts or authorities, if a court or another authority of Slovenia rendered a final decision on the same matter or if some other foreign judicial decision rendered on the same matter was recognised in Slovenia (*res judicata*)). Slovenian courts will not re-examine the merits of the case outside the scope described.

7.3 Assuming a company is in payment default under a loan agreement or a guarantee agreement and has no legal defence to payment, approximately how long would it take for a foreign lender to (a) assuming the answer to question 7.1 is yes, file a suit against the company in a court in your jurisdiction, obtain a judgment, and enforce the judgment against the assets of the company, and (b) assuming the answer to question 7.2 is yes, enforce a foreign judgment in a court in your jurisdiction against the assets of the company?

The duration of obtaining and recognising judgments and enforcing them before Slovenian courts will depend on several factors, predominantly the workload of the courts and the complexity of the matter, as well as the country where the judgment was issued (for enforcement procedures).

Generally, it can be expected that a first-instance judgment will be issued in two to three years (and an additional two years for appeal). Enforcement of judgments issued by EU Member State courts shall generally be a matter of weeks, while the recognition and enforcement procedure regarding judgments from non-EU countries is usually a matter of months.

7.4 With respect to enforcing collateral security, are there any significant restrictions which may impact the timing and value of enforcement, such as (a) a requirement for a public auction, or (b) regulatory consents?

Slovenian law provides for detailed rules on enforcement proceedings, both generally and specifically for different types of assets that are subject of enforcement proceedings. The court has generally a leading role in and conducts the proceedings, as well as issues orders to other entities involved (bailiffs, banks, appraisers, etc.). Enforcement proceedings for the sale of security collateral depend on the type of security and collateral.

Enforcement on real estate. Such enforcement can be carried out via a court sale or an out-of-court sale (if conditions for the latter are fulfilled). In a court sale, real estate is first appraised and afterwards sold by the court in an auction or by collecting binding offers (sale without an auction requires consent of all parties involved). In the first auction, the price for the real estate may not be lower than 70% of the appraised value and in the second auction, the price may not be lower than 50% of the appraised value (lower prices than these require consent of all parties involved). According to the Financial Collateral Act, an out of court sale of real estate via a notary is also possible. Such sale can only be conducted based on a directly enforceable notarial deed and if the creditor is a bank or a similar institution and if the debtor is not a natural person, a micro-sized company or a sole entrepreneur. The process is carried out via a collection of mandatory bids. The price may not be lower than 70% of the estimated value of real estate.

Enforcement on movables. Pledged movables can be generally sold out of court if the pledger and pledgee entered into a written agreement permitting out of court sale, if the pledge agreement is a commercial contract or concluded in a form of a directly enforceable notarial deed (i.e. registered pledges on movables). The pledged movables can be sold out of court in public auction or for market price. The parties may agree in detail on the procedure for the determination of the market price of movables and the sales process. Otherwise, movables are seized by the bailiff, stored and appraised. They can either be sold directly to a buyer or in an auction by the bailiff. The movables shall not be sold for less than the appraised value. If such purchase price cannot be achieved through a direct sale within the set deadline or at first auction, the movables may be sold at auction for a lower purchase price, but in no event for less than a third of the appraised value.

Enforcement on shares in LLCs. For sale of shares in LLC the same rules as for movables (see above) apply.

Shares (stocks) in corporations. For sale of shares (stock) in corporations the same rules as for movables (see above) apply. Agreement on out of court sale is presumed under the law.

Note that the timing of enforcement depends significantly on whether the security is established by a directly enforceable notarial deed. In that case, the lender does not need to initiate any legal action before enforcing security and is able to initiate enforcement proceedings immediately. If security is not created by a directly enforceable notarial deed, several years can pass before Slovenian courts issue a final judgment that allows for the enforcement proceedings to begin.

7.5 Do restrictions apply to foreign lenders in the event of (a) filing suit against a company in your jurisdiction, or (b) foreclosure on collateral security?

No additional restrictions apply to foreign lenders.

7.6 Do the bankruptcy, reorganisation or similar laws in your jurisdiction provide for any kind of moratorium on enforcement of lender claims? If so, does the moratorium apply to the enforcement of collateral security?

The Slovenian Financial Operations, Insolvency Proceedings and Compulsory Winding-up Act provides for moratorium on enforcement of lender claims and collateral security. Different rules apply to preventive restructuring proceedings (PRP) and insolvency proceedings (i.e. bankruptcy and compulsory settlement proceedings).

PRP. During PRP (from the time of the publication of the resolution on the initiation of the proceedings), judicial enforcement of all financial claims is bared and ongoing enforcement proceedings are terminated on request of the debtor. The debtor is deemed not to be at default for payment of the principal amounts of financial claims and the limitation period for financial claims is suspended.

Insolvency Proceedings. All enforcement proceedings initiated against the debtor before the beginning of either a compulsory settlement or bankruptcy proceedings are terminated upon the initiation of such proceedings. No new enforcement procedures can be initiated against the debtor after an insolvency proceeding has been initiated.

7.7 Will the courts in your jurisdiction recognise and enforce an arbitral award given against the company without re-examination of the merits?

Recognition and enforcement of arbitral awards in Slovenia is governed by the Convention on the Recognition and Enforcement of Foreign Arbitral Awards (New York, 1958). In accordance with Article III thereof, Slovenia shall recognise arbitral awards as binding and enforce them in accordance with the rules of procedure of the territory where the award is relied upon. Therefore, Slovenian courts will generally not re-examine the merits of the award.

8 Bankruptcy Proceedings

8.1 How does a bankruptcy proceeding in respect of a company affect the ability of a lender to enforce its rights as a secured party over the collateral security?

Secured lenders have a right to separate settlement in bankruptcy proceedings (and other insolvency proceedings), meaning that they have a right to a preferred distribution from the proceeds from the collateral security. Accordingly, unsecured parties are only repaid from the remainder of the proceeds from the collateral security and other assets that are free from collateral.

Note that for the assignee of a receivable to obtain the right to a separate settlement, the assignment agreement must be concluded in the form of a notarial deed. For more see question 3.4 above.

Also note that according to the Financial Collateral Act, financial collateral agreements and rights arising from them (including enforcement and set-off rights) remain in full force and effect even after an insolvency proceeding is initiated against the debtor.

8.2 Are there any preference periods, clawback rights or other preferential creditors' rights (e.g., tax debts, employees' claims) with respect to the security?

Creditors have clawback rights if the following conditions are met:

- the debtor in bankruptcy has concluded or carried out the legal transaction or other legal action in the period as of the beginning of the 12 months prior to the introduction of bankruptcy proceedings up to the initiation of bankruptcy proceedings;
- the consequence of such action is either (i) a decrease in the net value of assets of the debtor in bankruptcy, so as to enable other creditors to receive payment for their claims in a smaller portion than if the action had not been done, or (ii) that a person to the benefit of whom the act has been executed, has acquired more favourable payment conditions for a claim against the debtor in bankruptcy (i.e. objective criterion); and
- a person to the benefit of whom the action was executed, at the time when such act was executed, was aware of, or should have been aware of, the fact that the debtor was insolvent (i.e. subjective criterion).

Note that when another person comes into possession of the debtor's assets without being liable to execute its counter-fulfilment, or for a counter-fulfilment of small value, such action shall be challengeable irrespective of the fulfilment of the subjective criterion. In these cases, the suspected period extends from 12 to 36 months.

Furthermore a number of claims are considered preferential (e.g. claims arising from salaries, severance pays, taxes and contributions). These preferential claims, however, do not affect creditors' rights to separate settlements arising from the collateral.

8.3 Are there any entities that are excluded from bankruptcy proceedings and, if so, what is the applicable legislation?

Bankruptcy proceedings may generally be conducted against any legal entity. Only a few exceptions apply (e.g. only the Bank of Slovenia can initiate bankruptcy over a bank and a social enterprise may only be the subject of bankruptcy proceedings upon prior approval from the government).

On the other hand, a special form of PRP may only be conducted against a legal entity which (i) is a company with share capital, (ii) is classified as a small, medium-sized or large company in accordance with the Companies Act, and (iii) can be subject to compulsory settlement proceedings.

8.4 Are there any processes other than court proceedings that are available to a creditor to seize the assets of a company in an enforcement?

For out of court sale of real estate, see question 7.4 above.

As for movables, according to Slovenian Law of Property Code, a pledger and a pledgee can agree in a security agreement on an out of court sale. In such sale, the movables are sold by either a public auction or at a market price. The lender (pledgee) must return the remaining proceeds of the sale to the pledger. In agreements between business entities, an agreement on an out of court sale of movables is presumed. Note that the lender (pledgee) retains the right to an out of court sale of movables even after the initiation of the bankruptcy proceedings.

9 Jurisdiction and Waiver of Immunity

9.1 Is a party's submission to a foreign jurisdiction legally binding and enforceable under the laws of your jurisdiction?

Generally, choices of court are legally binding and enforceable under Slovenian law.

If the parties agree on jurisdiction of a court in one of the EU Member States. In this case, Brussels I Regulation shall apply. According to Article 25 of Brussels I Regulation, such choice of law is valid, unless the agreement is null and void as to its substantive validity under the law of that Member State. The agreed on jurisdiction shall be exclusive unless the parties have agreed otherwise. Specific rules apply regarding the form of the agreement (i.e. agreement in writing is advisable, but not necessarily required).

If the parties agree on jurisdiction of a court in a non-EU country. In this case, Slovenian law shall apply. A choice of court in a non-EU country is permissible provided that (i) at least one of the parties to the agreement on jurisdiction is a foreign citizen or a legal person with their principal place of business abroad, and (ii) no dispute is involved which would be subject to the exclusive jurisdiction of the courts in Slovenia.

9.2 Is a party's waiver of sovereign immunity legally binding and enforceable under the laws of your jurisdiction?

Waivers of sovereign immunity are neither required under Slovenian law nor common in lending agreements governed by Slovenian law. However, in principle, such waivers shall be legally binding and enforceable, unless they conflict with public international law.

10 Licensing

10.1 What are the licensing and other eligibility requirements in your jurisdiction for lenders to a company in your jurisdiction, if any? Are these licensing and eligibility requirements different for a "foreign" lender (i.e. a lender that is not located in your jurisdiction)? In connection with any such requirements, is a distinction made under the laws of your jurisdiction between a lender that is a bank *versus* a lender that is a non-bank? If there are such requirements in your jurisdiction, what are the consequences for a lender that has not satisfied such requirements but has nonetheless made a loan to a company in your jurisdiction? What are the licensing and other eligibility requirements in your jurisdiction for an agent under a syndicated facility for lenders to a company in your jurisdiction?

There are no general licensing and other eligibility requirements for lenders to a company in Slovenia. Since the role of agents under syndicated facilities is not regulated, no specific licensing or other eligibility requirements apply. Requirements and limitations arise primarily from (i) banking regulation, and (ii) consumer lending regulation.

Banking regulation. According to the Banking Act, banks shall only be allowed to provide financial services (e.g. taking of deposits and lending) after obtaining a licence from the Bank of Slovenia. A licence shall be obtained for each of the financial services the bank intends to provide.

Since passporting applies to EU Member States banks, these banks do not need to obtain a separate licence in Slovenia. On the other hand, banks from non-EU countries need to obtain a licence from the Bank of Slovenia and certain additional requirements may apply (i.e. the Bank of Slovenia may require from such a foreign bank a deposit of cash or assets or other appropriate financial collateral for obligations arising from business activities of the bank in Slovenia).

Consumer lending regulation. Licensing and eligibility requirements also apply in the field of consumer lending. In accordance with the Consumer Credit Act, several requirements need to be met by a lender to qualify for a licence for granting of consumer loans or financial leasing. Those relate to adequate ownership premises, number of employees with certain levels of education and duration of previous work experience, adequate technical and organisational conditions, etc. Stricter requirements apply if real estate is involved as collateral or otherwise connected to the loan. Generally exempted from the requirement to obtain a specific licence are Slovenian and EU Member State licensed credit institutions and those carrying out consumer lending activities via a branch office in Slovenia, as well as public law entities for certain specific retail loans.

Since passporting applies to EU Member States, EU-based consumer lenders, similarly to banks, do not need to obtain a separate licence in Slovenia. Consumer lending by entities from non-EU countries is not permitted under the passporting rules.

Consumer lending without previously obtaining a licence is considered an offence for which a monetary penalty of between EUR 50,000 and EUR 125,000 shall be issued. Such lending shall also be prohibited by the Market Inspectorate.

11 Other Matters

11.1 Are there any other material considerations which should be taken into account by lenders when participating in financings in your jurisdiction?

On 13 February 2018, the Slovenian legislature adopted the amendment to the Claim Enforcement and Security Act, which will enter into force on 25 March 2018.

Several provisions of the amendment are aimed at adapting the Act to the EU Regulations (including Brussels I Regulation and Regulation (EU) No 655/2014 establishing a European Account Preservation Order procedure). Due to direct enforceability of EU regulations these changes predominantly clarify and amend the procedures to comply with the respective regulations.

This amendment also overhauls the rules on the non-possessory pledges register by modernising, simplifying and automating the registration procedure. Data from the non-possessory pledges register will be linked with the tax and business register and automatically updated in real time. A government regulation implementing and specifying these changes shall be adopted by 2020.

Finally, a major change in the amendment is the introduction of an online auction platform for both real estate and movables that will be operated by the Slovenian Supreme Court. The platform will enable users to search for and participate in online auctions. The online auction platform will increase transparency and shorten the enforcement procedures. The online auction system will not be fully operational until the system is technically established and further regulated.

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JADEK & PENSA

Jadek & Pensa is a top-tier Slovenian law firm with a strong platform in corporate, M&A, banking, commercial, restructuring, and financial law. We constantly leverage our vast experience in these fields to provide insight and innovative solutions tailored to the individual project.

Jadek & Pensa has been engaged in the most significant transactions in Slovenia since its inception in the early 1990s. We have advised foreign and domestic lenders and borrowers in bilateral, club and syndicated lending and restructuring transactions, including security documentation, as well as sellers, buyers, financiers, targets and other clients in M&A and commercial matters. As a result, we have developed internal processes and effective document tools for a wide variety of corporate, lending and commercial transactions, which we can effectively deploy for a particular matter and incorporate into a solution in a time effective manner. We have also taken steps to serve our clients via automated processes responding to market demands with ground-breaking approaches.

South Africa

Lionel Shawe

Lisa Botha

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1 Overview

1.1 What are the main trends/significant developments in the lending markets in your jurisdiction?

While South Africa accounted for the largest loan issuance in Africa in 2017, with 26 reported deals totalling $10.98 billion (Thomson Reuters LPC Report, December 2017), the lending market in South Africa was mostly subdued during 2017. Business confidence has been low due to political uncertainty and lack of clear direction for the economy which remains sluggish. South Africa's sovereign debt was downgraded to sub-investment or junk status by both Fitch and S&P Global following a cabinet reshuffle at national government level in March 2017. Moody's downgraded South Africa to one notch above junk with an under-review outlook.

In December 2017, South Africa's ruling political party, the African National Congress (the ANC), elected new party leadership. This change in party leadership received promising investment interest at the World Economic Forum held end-January 2018.

There has also been a rapid development of financial technology (**fintech offerings**) with the emergence of three new banks – Discovery Bank, Bank Zero and TymeDigital – all of which expect to go live mid-to-late 2018. The emergence of these new banks is expected to robustly alter the financial services sector this year with their fintech offerings.

1.2 What are some significant lending transactions that have taken place in your jurisdiction in recent years?

Notwithstanding 2017 being a challenging year in the lending market of South Africa, there were some significant lending transactions which included:

- Royal Bafokeng Platinum raised ZAR3.2 billion in a particularly difficult market in which to raise funds for platinum projects. The funding was raised by way of a ZAR2 billion bank debt package and ZAR1.2 billion convertible bond offering.
- Sibanye Gold Limited raised approx. USD3,725,000,000 to fund (a) the acquisition of Stillwater Mining Company, (b) ongoing capital expenditure and general corporate and working capital requirements, and (c) the refinancing of certain existing facility agreements. This deal reduced the company's dependence on aging South African mining assets and will make it the world's third largest palladium producer and fourth largest PGM miner. It is the second largest SA outbound M&A transaction since 2015.
- Peermont, a casino and hotel operator in South Africa, underwent a significant debt-refinance and equity restructure.
- The financing of large-scale replacement broad-based black economic empowerment schemes transactions for large corporates such as Exxaro, Sasol and Telkom.

2 Guarantees

2.1 Can a company guarantee borrowings of one or more other members of its corporate group (see below for questions relating to fraudulent transfer/financial assistance)?

Generally yes, provided the company satisfies the requirements for the granting of financial assistance and (to the extent applicable) the making of a distribution under the relevant provisions of the South African Companies Act, 2008 (the **SA Companies Act**) prior to its obligations under the guarantee coming into force.

See question 4 below for the requirements for financial assistance under the SA Companies Act.

2.2 Are there enforceability or other concerns (such as director liability) if only a disproportionately small (or no) benefit to the guaranteeing/securing company can be shown?

There is no requirement under South African law for there to be corporate benefit to the guaranteeing/securing company. Directors have a fiduciary duty both in terms of the SA Companies Act and South African common law to act in good faith and for a proper purpose and in the best interests of a company. A breach of fiduciary duty may attract personal liability for that director.

2.3 Is lack of corporate power an issue?

Under South African law, a company has all the legal powers and capacity of a natural person except to the extent (1) it is incapable of exercising such power or of having such capacity, or (2) its memorandum of incorporation provides otherwise. However, where capacity of a company is limited in terms of its memorandum of incorporation, all third party effects of the limitation are voided. A transaction outside the 'limited' capacity of a company only gives rise to internal remedies. Shareholders, directors or prescribed officers of a company may apply to court to restrain a company from acting contrary to a limitation on its capacity, but any such action is without prejudice to the rights of a third party who obtained such rights in good faith and who did not have actual knowledge of the limitation of capacity. In addition, any action outside the 'limited' capacity of a company is capable of ratification by special resolution of the shareholders. To the extent, however, any limitation applies to a company's ability to grant financial assistance, any provision of financial assistance in contravention of that limitation (or the SA Companies Act) is not capable of ratification.

2.4 Are any governmental or other consents or filings, or other formalities (such as shareholder approval), required?

Under the SA Companies Act, the provision of financial assistance (which includes the granting of a guarantee) requires shareholder approval by way of special resolution (unless such financial assistance is pursuant to an employee share scheme that satisfies the requirements of section 97 of the SA Companies Act) and board approval. The shareholder approval can be generic (i.e. approval for a category of recipients and the recipient falls within that category) or transaction-specific and it must have been adopted within the past two years of the board resolution. Prior to authorising the provision of financial assistance at board level, the board must be satisfied that: (1) the company would satisfy the solvency and liquidity test immediately after providing the financial assistance in question; (2) the terms under which the financial assistance is given are fair and reasonable to the company; and (3) any conditions for financial assistance contained in the company's memorandum of incorporation have been satisfied.

To the extent the financial assistance (i.e. the guarantee) is granted for the benefit of a director or officer of the company or a related or inter-related company and the total value of the financial assistance granted exceeds 1/10th of 1% of the guaranteeing company's net worth at the time of the board resolution authorising the financial assistance is taken, the board of the guaranteeing company must give notice of the financial assistance to all shareholders of the company and any trade unions representing employees of the company. This is an administrative step and not a requirement for financial assistance under the SA Companies Act.

In addition to financial assistance, a guarantee for the benefit of one or more holders of any shares of the guaranteeing company (i.e. an upstream guarantee) or one or more holders of any shares of another company within the same corporate group constitutes a "distribution" as defined in section 1 of the SA Companies Act and requires board approval under section 46 of the SA Companies Act. This approval must include an acknowledgement that the board has applied the solvency and liquidity test and has reasonably concluded that the company will satisfy the solvency and liquidity test immediately after completing the proposed distribution.

See question 2.5 below for an explanation on the solvency and liquidity test under the SA Companies Act.

2.5 Are net worth, solvency or similar limitations imposed on the amount of a guarantee?

Not strictly, although the board of the guaranteeing company is required to confirm that the company will satisfy the solvency and liquidity test as provided for in the SA Companies Act immediately after providing the financial assistance, and to the extent applicable, immediately after completing the distribution.

The solvency and liquidity test is satisfied if, considering all reasonably and foreseeable financial circumstances of the company at that time the test is applied: (1) the assets of the company (fairly valued) equal or exceed the liabilities of the company (fairly valued); and (2) the company will be able to pay its debts as they become due in the ordinary course of business for the 12-month period following the provision of financial assistance or completion of the distribution, as applicable.

See question 2.6 below regarding limitations that may be imposed by the South African Reserve Bank.

2.6 Are there any exchange control or similar obstacles to enforcement of a guarantee?

Funds flowing in and out of South Africa are subject to exchange control in terms of the Exchange Control Regulations, issued under the Currency and Exchanges Act, 1933 (the **Exchange Control Regulations**). Exchange control is controlled by the Financial Surveillance Department (**FinSurv**) of the South African Reserve Bank. Certain powers set out in the Currency and Exchanges Manual for Authorised Dealers (previously known as the exchange control rulings) have been delegated to authorised dealers, which are banks authorised by FinSurv to deal in foreign exchange.

The enforcement of a guarantee given by a South African resident in favour of a foreign lender is subject to the requisite exchange control approval for that guarantee being in place. The approval must be obtained from FinSurv on application by the South African resident company through its authorised dealer. While there is no regulatory limitation on the amount of a guarantee under the Exchange Control Regulations or rulings, FinSurv has a general discretion to impose any conditions on the approval granted by it. FinSurv has recently tended to include in its approval a limitation that any amount recovered under the guarantee is limited to the net asset value of the guaranteeing company at the time of recovery.

The approval process generally takes between four and six weeks.

3 Collateral Security

3.1 What types of collateral are available to secure lending obligations?

It is possible to take security over most common assets of a South African company.

3.2 Is it possible to give asset security by means of a general security agreement or is an agreement required in relation to each type of asset? Briefly, what is the procedure?

South Africa does not have a universal corporate security interest covering all assets generically. The appropriate form of security is determined by reference to the classification of the assets concerned as immovable (land) or movable and in respect of movable assets, further sub-classification as corporeal (tangible) or incorporeal (intangible).

3.3 Can collateral security be taken over real property (land), plant, machinery and equipment? Briefly, what is the procedure?

Security over immovable property (land) is created by way of registration of a mortgage bond specially mortgaging the land in accordance with the requirements under the Deeds Registries Act, 1937. Registration at the deeds registry where the land is registered perfects the security. There is no prescribed form for mortgage bonds, although there are recommended forms for certain types of mortgage bonds. The content of a mortgage bond is determined by banking and conveyancing practice, the common law and statute law.

Security over plant, machinery and equipment may be caught by any mortgage bond over the land to the extent those assets are sufficiently attached to the mortgaged land and were intended to be annexed permanently to the land. In these circumstances, the plant, machinery or equipment would be classified as immovable property.

Security over plant, machinery or equipment not constituting immovable property under South African property law is usually taken by way of mortgage in the form of either a special notarial bond or a general notarial bond. A special notarial bond is a mortgage by the debtor of specifically identified tangible movable property in favour of a creditor as security for a debt or other obligation. It must comply with the requirements outlined in the Security by Means of Movable Property Act, 1993; including the requirement that the property secured must be clearly identified and described in such a manner which makes it readily recognisable. A special notarial bond must be registered at the deeds registry within three months after the date of its execution. Once registered, the creditor is a secured creditor in the estate of the debtor.

A general notarial bond is a mortgage by the debtor of all its present and future tangible movable property in favour of a creditor as security for a debt or other obligation. A general notarial bond must be registered at the deeds registry within three months after the date of its execution. A general notarial bond does not confer a real right of security in the property concerned unless the creditor obtains possession of the property prior to insolvency of the debtor by way of a perfection order obtained from a court.

Both a special and general notarial bond must be prepared by a notary public and executed by either the owner of the movable assets (the mortgagor) encumbered under the bond or the notary public under a formal power of attorney granted to him by the mortgagor.

It is also possible to grant security over plant, machinery and equipment by way of a pledge, although this form of security requires delivery of the assets concerned, in addition to the agreement to grant the security over the asset, to perfect the security over those assets.

3.4 Can collateral security be taken over receivables? Briefly, what is the procedure? Are debtors required to be notified of the security?

Security over receivables is taken by way of cession. There are no formalities: the security interest is created by the debtor agreeing to grant security by way of cession over the receivables in favour of the creditor.

It is not necessary to notify the underlying debtors of the cession to perfect the security created over the receivables and given the fluctuating nature of receivables, it is fairly uncommon to give notice of the cession to the underlying debtors prior to the occurrence of an event of default. In the absence of notice, however, any payment by an underlying debtor to security provider following the occurrence of the event of default constitutes a valid discharge by the underlying debtor of its obligations in respect of such receivables and the creditor will have to recover these amounts from the security provider.

3.5 Can collateral security be taken over cash deposited in bank accounts? Briefly, what is the procedure?

Yes, security over cash deposited in a bank account is taken by way of cession.

As discussed above in relation to security over receivables, there are no formalities for a cession: the security interest is created by the debtor agreeing to grant security by way of cession over the cash in the bank accounts in favour of the creditor.

It is more common in the case of a cession over cash in bank accounts to notify the banks of the security interest created at the time of creation of the security interest.

3.6 Can collateral security be taken over shares in companies incorporated in your jurisdiction? Are the shares in certificated form? Can such security validly be granted under a New York or English law governed document? Briefly, what is the procedure?

Yes, security can be taken over shares in companies incorporated in South Africa. Shares in a private company are generally in certificated form; while shares in a public company are generally in uncertificated form.

Security over shares in a South African company is taken by way of pledge and cession. Similar to security over receivables and cash in bank accounts, the security interest is created by the debtor agreeing to grant security over the shares in question. There are no other perfection requirements; although it is fairly common to have any share certificates together with undated and blank share transfer forms delivered to the secured creditor at the time of creation of the security interest to facilitate enforcement if needed following the occurrence of default. There is a statutory obligation (not a perfection requirement) to "effect" any security interest over shares lodged and immobilised in South Africa's central securities depository by "flagging" the relevant securities account in accordance with the Financial Markets Act, 2012.

Under South African law, the proper law for a security document granting security over assets situated in South Africa is South African law.

3.7 Can security be taken over inventory? Briefly, what is the procedure?

Yes, security over inventory is possible and usually takes the form of a special or general notarial bond.

See question 3.3 above for the procedure for taking security by way of a special or general notarial bond.

3.8 Can a company grant a security interest in order to secure its obligations (i) as a borrower under a credit facility, and (ii) as a guarantor of the obligations of other borrowers and/or guarantors of obligations under a credit facility (see below for questions relating to the giving of guarantees and financial assistance)?

Yes, provided the requirements for the granting of financial assistance and the making of a distribution under the SA Companies Act are satisfied where applicable.

See section 4 below for the requirements for financial assistance under the SA Companies Act.

3.9 What are the notarisation, registration, stamp duty and other fees (whether related to property value or otherwise) in relation to security over different types of assets?

There is no stamp duty or other documentary tax payable under South African law for the granting, or taking, of security. Nominal registration fees are payable for the registration of mortgage bonds, general and special notarial bonds, aircraft mortgages, ship mortgages, hypothecations relating to trade marks, designs and patents. A mortgage bond must be prepared by a conveyancer and a notarial bond by notary public, both of whom are entitled to charge fees on a tariff-fee basis in South Africa calculated by reference to the principal amount of the secured debt for preparing the bonds.

3.10 Do the filing, notification or registration requirements in relation to security over different types of assets involve a significant amount of time or expense?

The costs for the preparation and lodgement of mortgage bonds and notarial bonds can be significant. It is fairly common, however, for conveyancers and notaries public preparing and lodging these documents to offer a fairly significant discount to the tariff rates.

3.11 Are any regulatory or similar consents required with respect to the creation of security?

Exchange control approval is required for the enforcement by a foreign lender of any security granted by a South African resident but it is common practice to obtain this approval prior to the of creation of the security. As discussed in question 2.6 above for exchange control for a guarantee, the approval must be obtained from FinSurv on application by the South African resident company through its authorised dealer. The approval process generally takes between four and six weeks.

There may be particular requirements for regulated entities or assets. For example, a cession over shares in a company that holds a mining licence requires the consent of the Department of Minerals and Energy in South Africa.

3.12 If the borrowings to be secured are under a revolving credit facility, are there any special priority or other concerns?

Generally, no.

3.13 Are there particular documentary or execution requirements (notarisation, execution under power of attorney, counterparts, deeds)?

Creditors generally expect to receive board and/or shareholder resolutions approving the transaction for evidentiary purposes and to ensure any financial assistance requirements have been satisfied.

The Uniform Rules of Court (of South Africa) provide for the authentication of any document signed outside of South Africa which is to be received in the courts of South Africa. A document executed outside of South Africa that has not been authenticated in accordance with the Uniform Rules of Court (of South Africa) remains valid and is admissible in evidence in a South African court but there is an evidentiary risk in respect of due execution. This risk can be mitigated in various ways, including but not limited to resolutions passed authorising a person to execute documents, specimen signatures of signatories and copies of passports or identity documents of signatories.

4 Financial Assistance

4.1 Are there prohibitions or restrictions on the ability of a company to guarantee and/or give security to support borrowings incurred to finance or refinance the direct or indirect acquisition of: (a) shares of the company; (b) shares of any company which directly or indirectly owns shares in the company; or (c) shares in a sister subsidiary?

Both a private and public company are restricted from providing financial assistance (including by way of guarantee or security) in connection with the acquisition of:

(a) its own shares;

(b) the shares of its holding company; and

(c) the shares in a sister company,

unless the financial assistance has been approved in accordance with the relevant provisions of the SA Companies Act.

The board of a company may not authorise the provision of any financial assistance unless that financial assistance is pursuant to an employee share scheme under section 97 of the SA Companies Act or has been approved by way of a special resolution of the shareholders of that company that provides for generic approval for a category of recipients and the recipient falls within that category or for transaction specific approval. The shareholder resolution must have been adopted within the past two years of the board resolution. Further, the board must be satisfied that: (1) the company would satisfy the solvency and liquidity test immediately after providing the financial assistance in question; (2) the terms under which the financial assistance is given are fair and reasonable to the company; and (3) any conditions for financial assistance contained in the company's memorandum of incorporation have been satisfied.

The SA Companies Act also restricts the provision of financial assistance to a director or officer of the company or a related or inter-related company of the company granting the financial assistance. The requirements discussed above apply equally in these circumstances.

See question 2.5 for an explanation on the solvency and liquidity test under the SA Companies Act.

5 Syndicated Lending/Agency/Trustee/ Transfers

5.1 Will your jurisdiction recognise the role of an agent or trustee and allow the agent or trustee (rather than each lender acting separately) to enforce the loan documentation and collateral security and to apply the proceeds from the collateral to the claims of all the lenders?

South African law does recognise the concept of a trust. However, the security trustee structure recognised under English and New York law is not recognised under South African law. South African law requires that the security provider owe a valid principal obligation (not an accessory obligation) to the creditor. The security trustee structure does not meet this requirement.

5.2 If an agent or trustee is not recognised in your jurisdiction, is an alternative mechanism available to achieve the effect referred to above which would allow one party to enforce claims on behalf of all the lenders so that individual lenders do not need to enforce their security separately?

Where a security agent is used for the purpose of holding South African security, a parallel debt arrangement is normally used in order to ensure that the security can be validly given to the security agent. The security interest, however, vests in the estate of the security agent and as a result, lenders take insolvency risk on the security agent.

Another alternative structure commonly used in South African law-governed transactions entails the establishment of a separate special purpose vehicle (known as the security SPV) to act as beneficiary of the security granted by the security provider. The security SPV will provide a guarantee to the creditors for all of the secured obligations of the security provider, and the security provider will provide an indemnity to the security SPV. The shares in the security SPV are held by an owner trust.

5.3 Assume a loan is made to a company organised under the laws of your jurisdiction and guaranteed by a guarantor organised under the laws of your jurisdiction. If such loan is transferred by Lender A to Lender B, are there any special requirements necessary to make the loan and guarantee enforceable by Lender B?

Exchange control approval is required for a loan (whether in Rand or foreign currency denominated) made to a South African resident by a foreign lender as well the granting of security or a guarantee by the South African resident in favour of the foreign lender.

Any change in the foreign lender does not require fresh approval but must be notified to the exchange control authorities through the relevant authorised dealer.

6 Withholding, Stamp and Other Taxes; Notarial and Other Costs

6.1 Are there any requirements to deduct or withhold tax from (a) interest payable on loans made to domestic or foreign lenders, or (b) the proceeds of a claim under a guarantee or the proceeds of enforcing security?

Yes, interest payable to or for the benefit of a foreign lender is subject to withholding tax at the rate of 15% to the extent that the amount is regarded as having been received or accrued from a source within South Africa under the South African Income Tax Act, 1962 (the **SA Income Tax Act**), unless the levying of withholding tax is exempted under the applicable provisions of the SA Income Tax Act or the amount of withholding tax is reduced as a result of a double taxation treaty.

Under the SA Income Tax Act, the exemptions relevant to withholding tax on interest fall into three broad groups:

- the payor (i.e. the person paying the interest);
- the instrument (i.e. the instrument giving rise to the interest, for example the debt or the investment); and
- the recipient of the interest.

A foreign person is exempt from the withholding tax on interest if the debt claim for which interest is paid is effectively connected with a permanent establishment of that foreign person if that foreign person is registered as a taxpayer in South Africa.

It is not clear from the current wording of the withholding tax provisions of the SA Income Tax Act whether the proceeds of a claim under a guarantee representing any amount of interest under the loan would be subject to withholding tax. The current market view is that this is not the case.

6.2 What tax incentives or other incentives are provided preferentially to foreign lenders? What taxes apply to foreign lenders with respect to their loans, mortgages or other security documents, either for the purposes of effectiveness or registration?

There are no preferential tax incentives for foreign lenders lending into South Africa.

6.3 Will any income of a foreign lender become taxable in your jurisdiction solely because of a loan to or guarantee and/or grant of security from a company in your jurisdiction?

A foreign lender is not liable to pay tax in South Africa by reason only of its entering into a loan or exercising its rights (including taking steps to enforce its rights) under a loan, guarantee or security agreement.

Unless an exemption under the SA Income Tax Act applies, a foreign lender may be subject to tax on income that has, or is deemed to have, its source in South Africa. Income is or will be deemed to have its source in South Africa if, for example, it relates to rental on property situated in South Africa. South-African-sourced interest which is received or accrued by or to a foreign lender is exempt unless the debt from which the interest arises is effectively connected to a permanent establishment of that foreign lender in South Africa.

See question 6.1 above for the application of withholding tax on payments of interest under a loan to a foreign lender.

6.4 Will there be any other significant costs which would be incurred by foreign lenders in the grant of such loan/guarantee/security, such as notarial fees, etc.?

There is no stamp duty or other documentary tax payable under South African law on the execution of enforcement of a loan or guarantee.

See question 3.9 for fees associated with taking security in certain circumstances.

6.5 Are there any adverse consequences to a company that is a borrower (such as under thin capitalisation principles) if some or all of the lenders are organised under the laws of a jurisdiction other than your own? Please disregard withholding tax concerns for purposes of this question.

If one of the lenders is connected to the South African borrower and a tax benefit has arisen, the South African borrower cannot claim, in terms of section 31 of the SA Income Tax Act, a deduction of interest on any portion of the financing that is not at arm's length (i.e. any excessive portion of the financing). There are essentially two requirements that must be met before section 31 can be applied: (1)

the terms and conditions of the transaction must differ from what they would have been had the parties been independent persons acting at arm's length (i.e. unconnected persons); and (2) the transaction must result (currently or in the future) in a tax benefit being derived by a person that is a party to the transaction. 'Tax benefit' is defined in the SA Income Tax Act as any avoidance, postponement or reduction of any liability for tax under the SA Income Tax Act.

Further, the amount of interest that may be deducted by the South African borrower is limited under section 23M of the SA Income Tax Act if: (1) the lender is in a controlling relationship with the borrower or it has obtained the funding from a person that is in a controlling relationship with the borrower; and (2) the amount of interest is not subject to tax in South Africa in the hands of the foreign lender. If the interest paid to the foreign lender is subject to withholding tax, the provisions of section 23M do not apply. A 'controlling relationship' is one where a person holds (directly or indirectly) 50% of the equity shares in a company or at least 50% of the voting rights in a company.

The location of any unconnected lender has no other adverse consequences for a South African borrower (disregarding withholding tax concerns).

7 Judicial Enforcement

7.1 Will the courts in your jurisdiction recognise a governing law in a contract that is the law of another jurisdiction (a "foreign governing law")? Will courts in your jurisdiction enforce a contract that has a foreign governing law?

South African law gives effect to the choice of law exercised by contracting parties, subject to certain exceptions. Where foreign governing law applies, the applicable legal position is often the subject of expert evidence in litigation or arbitration proceedings. There are certain aspects which cannot be governed by the law chosen by the parties, however. For example, the proper law for a security document granting security over assets situated in South Africa is South African law.

7.2 Will the courts in your jurisdiction recognise and enforce a judgment given against a company in New York courts or English courts (a "foreign judgment") without re-examination of the merits of the case?

A foreign judgment is not automatically enforceable in South Africa but does constitute a cause of action and would be recognised and enforced by the South African courts (on application brought under the Enforcement of Foreign Civils Judgments Act, 32 of 1988) without re-examination of the merits of the case, provided:

- the court which pronounced the judgment had jurisdiction to entertain the case according to the principles recognised by South African law with reference to the jurisdiction of foreign courts;
- the judgment is final and conclusive in its effect and has not become superannuated;
- the recognition and enforcement of the judgment would not be contrary to public policy in South Africa;
- the judgment was not obtained by fraudulent means;
- the judgment does not involve the enforcement of a penal or revenue law of the foreign state; and
- the enforcement of the judgment is not precluded by the provisions of the Protection of Businesses Act, 1978. This Act requires that the consent of the Minister of Trade and Industry be obtained before certain foreign judgments can be enforced. The South African courts have interpreted the ambit of the Act restrictively and the current market view is that the ambit of the Act would appear not to include loans from, or guarantees to, foreign lenders.

7.3 Assuming a company is in payment default under a loan agreement or a guarantee agreement and has no legal defence to payment, approximately how long would it take for a foreign lender to (a) assuming the answer to question 7.1 is yes, file a suit against the company in a court in your jurisdiction, obtain a judgment, and enforce the judgment against the assets of the company, and (b) assuming the answer to question 7.2 is yes, enforce a foreign judgment in a court in your jurisdiction against the assets of the company?

(a) A South African court will exercise jurisdiction in a contractual dispute notwithstanding the chosen law of the agreement being foreign, if the normal grounds for jurisdiction exist. A foreign lender, like any local lender, can initiate legal proceedings in one of two ways: by way of action for matters involving a factual dispute, or (less likely in the circumstances) by way of application for matters where no factual dispute exists but involves application of the relevant law in question.

An action is initiated by way of service of summons. After formal service of that summons by the Sheriff of the Court, the defendant must file a notice of intention to defend if he wishes to oppose the action (within 10 court days after service). Two scenarios arise:

- If no notice of intention to defend is filed, the foreign lender can apply to the registrar of the court for default judgment without further notice to the defendant. This procedure, if successful, takes approximately four weeks from initiation of proceedings.
- If the defendant delivers a notice of intention to defend, and the claim is liquid (which is likely to be the case in the context of this query) the foreign lender can apply for summary judgment. The courts are reluctant to grant summary judgment unless the foreign lender has satisfied the court that the defendant has no *bona fide* defence and has entered a notice of intention to defend solely for the purposes of delaying the action. The summary judgment procedure, if successful, takes approximately six to eight weeks from initiation of proceedings. If the defendant is able to demonstrate under oath that it has a *bona fide* defence, alternatively, the defendant puts up security for the sum claimed in the summons, the matter will proceed to trial and it is likely that the court will grant an adverse costs order against the foreign lender. A full trial procedure usually takes between one to two years from initiation of the proceedings given an unfortunate backlog in the South African courts as regards the allocation of trial dates.

(b) A foreign lender seeking to enforce a foreign judgment in South Africa must first apply to a local court for an order recognising the judgment. If the foreign judgment satisfies the requirements for its recognition as discussed in question 7.2 above and the local court grants an order recognising it, the foreign lender can enforce the judgment in the ordinary course as if it were a judgment of a South African court – i.e. the foreign lender can obtain a writ of execution and attach the defendant's assets for sale in execution in satisfaction of the judgment.

7.4 With respect to enforcing collateral security, are there any significant restrictions which may impact the timing and value of enforcement, such as (a) a requirement for a public auction, or (b) regulatory consents?

In the case of foreclosing on a mortgage bond or a general notarial bond where the secured creditor is not in possession of the assets, the secured creditor would need to first obtain a court order before enforcement. This will have an impact on the cost and timing of recovery.

Regulatory consents may be required if the company is a regulated entity or the assets are regulated.

7.5 Do restrictions apply to foreign lenders in the event of (a) filing suit against a company in your jurisdiction, or (b) foreclosure on collateral security?

No, foreign lenders are essentially treated the same as domestic lenders. A defendant will, however, be entitled to request (on application to the registrar, or court, depending on the circumstances) that the foreign lender provide security for the defendant's legal costs.

7.6 Do the bankruptcy, reorganisation or similar laws in your jurisdiction provide for any kind of moratorium on enforcement of lender claims? If so, does the moratorium apply to the enforcement of collateral security?

On liquidation, a *concursus creditorum* occurs and the estate of the insolvent is essentially frozen. The aim in liquidation is to realise the unsecured assets of the company for the benefit of creditors as a whole (save for secured creditors). All legal proceedings against the company are suspended until the appointment of a liquidator and any civil attachment of assets of the company after insolvency proceedings have been commenced is void. A secured creditor is not entitled to enforce its rights under its security agreement but must rather deliver any secured property held by it to the liquidator of the insolvent estate for realisation. There are limited circumstances in which a secured creditor may realise certain secured assets itself without the consent of the liquidator of the insolvent estate. These limited circumstances relate to where the secured property comprises marketable securities (i.e. property ordinarily sold through a stockbroker); financial instruments or bills of exchange. Any cash proceeds realised through any disposal of the secured assets would then have to be turned over to the liquidator unless an agreement is reached with the liquidator for the lender to retain the proceeds subject to paying the fees of the liquidator and Master of the High Court.

A company in "financial distress" may be placed into business rescue with the aim of rehabilitating the company by providing for the temporary supervision and management of the company's affairs and business by a business rescue practitioner. During business rescue, no creditor may institute any legal proceedings or take any enforcement action (including enforcement of any collateral security) against the company. In certain circumstances proceedings may be brought against the company with the written consent of the business rescue practitioner or with the leave of the court.

The terms and effect of any reorganisation of a company (including whether any moratorium applies) by way of compromise with its creditors will depend on terms agreed between the company and all its creditors.

7.7 Will the courts in your jurisdiction recognise and enforce an arbitral award given against the company without re-examination of the merits?

In terms of the recently promulgated International Arbitration Act, 2017 (the **International Arbitration Act**) (which came into effect on 20 December 2017), the Model Law on International Commercial Arbitration, as adopted by the United National Commission on International Trade Law, has been wholly adopted into South African law for the purposes of international arbitral awards. In effect, as regards to enforcement of arbitral awards:

- a foreign arbitral award is binding between the parties to that foreign arbitral award, and may be relied upon by those parties by way of defence, set-off or otherwise in any legal proceedings;
- a foreign arbitral award must be made an order of court on application to court;
- a foreign arbitral award may be enforced in the same manner as any judgment or order of court, and the party seeking such order must produce: an original award and arbitration agreement (as authenticated in a manner acceptable to a South African court (i.e. by a notary public, or certified as true originals)); and, if issued in a foreign language, an authenticated sworn translation or the award and arbitration agreement;
- a court may only refuse to recognise or enforce a foreign arbitral award if:
    - the court finds that a referral to arbitration of the subject matter of the dispute is impermissible in South African law, or is contrary to public policy;
    - the parties against whom the award is invoked proves to the satisfaction of the court that:
        - a party to the arbitration agreement had no capacity to contract under the law applicable to that party;
        - the arbitration agreement is invalid under the law to which the parties have subjected it, and, where no law is subjected, the law of the country in which the arbitral award was made;
        - the required notice was not given as regards to the appointment of an arbitrator, and/or the constitution of an arbitration, and that party was not able to present its case;
        - the arbitral award is beyond the arbitrator's jurisdiction – i.e. it deals with a dispute not contemplated by / falling within the terms of reference / scope of the arbitrator's appointment;
        - the constitution of the arbitration proceedings was not in accordance with or provided for in the arbitration agreement or the law of the country in which it is constituted; and
        - the award is not yet binding on the parties, has been set aside or suspended by a competent authority in the country in which, or under the law of which, the arbitral award was made;
- an arbitral award can be recognised and enforced in part, provided that the aspects which a party seeks to enforce can be separated from the rest of the award; and
- where an application for the setting aside or suspension of an award had been made to a competent authority, the court where recognition or enforcement is sought may, where appropriate, adjourn its decision *and*, on application by the party seeking recognition and enforcement, order the other party against whom the arbitral award is being invoked to provide suitable security.

Importantly, as regards to the applicability of the new International Arbitration Act, the new provisions will apply to all international commercial arbitration agreements regardless of whether they were entered into before or after the commencement of the new International Arbitration Act. It will not, however, apply where:

- proceedings for the enforcement of an arbitral award under the old Act; or

- proceedings for the enforcement, setting aside or remittal of an arbitral award under the Arbitration Act (42 of 1965),

were already in progress prior to 20 December 2017 – i.e. the old position will still apply to such proceedings.

8 Bankruptcy Proceedings

8.1 How does a bankruptcy proceeding in respect of a company affect the ability of a lender to enforce its rights as a secured party over the collateral security?

A secured creditor is not entitled to enforce its rights under its security agreement during insolvency proceedings but must rather deliver any secured property held by it to the liquidator of the insolvent estate for realisation. There are limited circumstances in which a secured creditor may realise certain secured assets itself without the consent of the liquidator. These limited circumstances relate to where the secured property comprises marketable securities (i.e. property ordinarily sold through a stockbroker); financial instruments or bills of exchange. Any cash proceeds realised through any disposal of the secured assets would then have to be turned over to the liquidator unless an agreement is reached with the liquidator for the lender to retain the proceeds subject to paying the fees of the liquidator and Master of the High Court.

8.2 Are there any preference periods, clawback rights or other preferential creditors' rights (e.g., tax debts, employees' claims) with respect to the security?

Certain pre-liquidation contracts can be set aside by a liquidator exercising anti-avoidance (or clawback) powers afforded to it under the SA Insolvency Act. Clawback could be available in relation to: dispositions (commonly known as impeachable dispositions) made not for value; dispositions having the effect of preferring creditors and not made in the ordinary course of business; dispositions made with intent to prefer creditors; collusive dealings; and dispositions in fraud of creditors.

The definition of a "*disposition*" in terms of the SA Insolvency Act is very wide, and is designed to cover every loss of rights to property, which includes the granting of security.

A disposition will only qualify as an impeachable disposition if it was made at a time when the debtor's liabilities exceed its assets or, in the case of a disposition at no value, the debtor's estate was rendered insolvent by the disposition. For this purpose, "insolvent" means that the insolvent's liabilities must exceed the value of his assets (fairly valued) at the date of the disposition.

Where a special notarial bond or mortgage bond is passed over assets to secure a debt and such bond is not registered within two months of the debt being incurred, and the debtor is liquidated within six months of the registration of the notarial bond or mortgage bond, no preference is recognised under the notarial bond or mortgage bond and the lender effectively loses its security.

Creditors in the insolvent estate are paid according to the following order of rank:

- costs of liquidation – this includes the costs of court application; the liquidator and masters fees; and sheriff's costs;
- secured creditors – payment is made to secured creditors from the proceeds of a sale of the secured assets (after the proportionate liquidation costs have been deducted from the proceeds of the realised secured asset). Where a secured creditor's claim is not secured in full, the unpaid balance is treated as a concurrent claim. Secured claims include mortgage bonds over immovable property which are satisfied in the order in which they are registered or recorded; pledges over movable property; special notarial bonds registered over movable property are satisfied in the order in which they are registered; and cessions over intangible movable property;
- preferent creditors – these are creditors who do not hold security for their claims but rank above the claims of concurrent creditors. They are paid from the proceeds of the unencumbered assets (the free residue) in a pre-determined order as follows:
  - the salary and wages of employees (and certain other amounts payable to, or on behalf of, employees);
  - certain statutory obligations (such as amounts owing to the workmen's compensation fund; any customs or sales tax due under the Customs Excise Act, 1964; any value-added tax or penalty due under the Value-Added Tax Act, 1991; and any amounts owing to the unemployment insurance fund);
  - income tax; and
  - preferential claims arising from bonds giving preferences (i.e. general notarial bonds or special notarial bonds registered before 7 May 1993);
- concurrent creditors – these are creditors who are paid from the proceeds of the free residue that remains after preferent creditors have been paid in full in proportion to the amounts owed to them;
- subordinated creditors – if they have subordinated their claims to the claims of concurrent creditors; and
- shareholders (holders of preference shares generally take priority to holders of ordinary shares).

8.3 Are there any entities that are excluded from bankruptcy proceedings and, if so, what is the applicable legislation?

Special legislation and special insolvency regimes may apply to certain businesses (e.g. banks/credit institutions and investment firms).

8.4 Are there any processes other than court proceedings that are available to a creditor to seize the assets of a company in an enforcement?

The lender and security provider may agree that the lender has a right (called *parate executie*) to sell the secured assets without an order of court by public auction to the highest bidder or in such manner as may be otherwise agreed between the parties.

The debtor may seek the protection of the court if, on any just ground, he can show that, in carrying out the agreement and effecting a sale, the creditor acted in a manner which prejudiced the debtor in his rights, is valid in respect of a security interest created over movable property.

An agreement in a mortgage bond entitling the mortgagee to resort to *parate executie* by taking possession of the property and selling it privately is, however, invalid.

9 Jurisdiction and Waiver of Immunity

9.1 Is a party's submission to a foreign jurisdiction legally binding and enforceable under the laws of your jurisdiction?

Generally yes, submission to a foreign jurisdiction is legally binding and enforceable under South African law. However, as per the Foreign States Immunities Act, 87 of 1981, the inherent jurisdiction of the South African courts cannot be ousted and, as such, a South African court may exercise its discretion not to take cognisance of the submission to foreign jurisdiction clause in commercial transactions with a foreign state, or, where the obligations of a foreign state (in terms of a contract, whether a commercial transaction or not) falls to be performed wholly or partly in South Africa. Commercial transactions falling within the ambit of the Foreign States Immunities Act relate to: (i) any contract for the supply of services or goods; (ii) a loan or other transaction for the provision of finance, and any guarantee or indemnity in respect of any such loan or other transaction, or, of any other financial obligation; and (iii) other transactions/activities, or a commercial, industrial, financial, professional or other similar character contract into which a foreign state enters, or in which it engages other than in the exercise of sovereign authority. It does not, however, include a contract of employment between foreign state and an individual.

9.2 Is a party's waiver of sovereign immunity legally binding and enforceable under the laws of your jurisdiction?

Yes, sovereign immunity may be waived as per the Foreign States Immunities Act, 87 of 1981. More particularly, a waiver of immunity may be effected after the dispute which gave rise to the proceedings has arisen, or by prior written agreement.

A provision in an agreement that it is to be governed by the law of South Africa shall not be regarded as a waiver, but a foreign state shall be deemed to have waived its immunity: (i) if it has instituted the proceedings; or (ii) if it has intervened or taken any step in the proceedings (save for where this "step" is taken for the purpose of claiming immunity, or asserting an interest in property in circumstances such that the foreign state would have been entitled to immunity if the proceedings had been brought against it). A waiver in respect of any proceedings shall also apply to any appeal and to any counter-claim arising out of the same legal relationship or facts as the claim.

10 Licensing

10.1 What are the licensing and other eligibility requirements in your jurisdiction for lenders to a company in your jurisdiction, if any? Are these licensing and eligibility requirements different for a "foreign" lender (i.e. a lender that is not located in your jurisdiction)? In connection with any such requirements, is a distinction made under the laws of your jurisdiction between a lender that is a bank *versus* a lender that is a non-bank? If there are such requirements in your jurisdiction, what are the consequences for a lender that has not satisfied such requirements but has nonetheless made a loan to a company in your jurisdiction? What are the licensing and other eligibility requirements in your jurisdiction for an agent under a syndicated facility for lenders to a company in your jurisdiction?

Lending activity as such is not a regulated activity in South Africa unless credit is provided to consumers (i.e. retail lending activity).

However, under the Banks Act, 1990 (the **SA Banks Act**) no person may conduct "the business of a bank" unless such person is a public company and registered as a bank under the SA Banks Act. The business of a bank is widely defined and includes accepting deposits from the general public as a regular feature of the business in question. The SA Banks Act does not define nor offer guidance as to what constitutes the "general public" but it is generally understood to refer, with reference to the SA Banks Act, to any section of the public, irrespective of any pre-selective or pre-determinative criteria applicable to a particular group of persons. It would not include any private or domestic arrangements.

The South African Reserve Bank is responsible for bank regulation and supervision in South Africa. It is not, however, necessary under the laws of South Africa that a foreign lender is licensed, qualified or otherwise entitled to carry on business in South Africa to enable it to exercise its rights (including taking steps to enforce its rights) under any lending arrangements entered into with a South African borrower, or to enter into or perform its obligations under the lending arrangements.

11 Other Matters

11.1 Are there any other material considerations which should be taken into account by lenders when participating in financings in your jurisdiction?

Under the Financial Advisory and Intermediary Services Act, 2002 (**FAIS**), no person may provide intermediary services or advice to clients in respect of financial products (including insurance products, bank deposits and securities) unless that person has been issued a licence under FAIS. Authorised financial service providers holding the requisite licence under FAIS are bound by principles and rules set out in the applicable codes of conduct created by the Financial Services Board, the regulatory body responsible for administering FAIS.

Foreign investors should also consider a recently enacted piece of legislation, the Protection of Investment Act, 2015. This Act was assented to by the President of South Africa in December 2015 but is yet to come into force (its effective date still needs to be proclaimed). This Act is intended to replace South Africa's bilateral investment treaties and provide for the protection of investors and their investments in South Africa in accordance with and subject to the Constitution of South Africa in a manner which balances the public interest and the rights and obligations of investors.

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Chapter 72

Spain

Manuel Follía

Cuatrecasas

María Lérida

1 Overview

1.1 What are the main trends/significant developments in the lending markets in your jurisdiction?

The enormous liquidity and the variety of financing products available to borrowers in Spain has provided a very attractive opportunity for banks, credit funds and equity players.

Bank financing is still the main source of financing, although the structures have changed as a result of the extension of the financing products available to borrowers. In this sense, jointly with the traditional senior and mezzanine facilities, a variety of financing sources have proliferated, such as bridge-to-equity, second-lien or hybrid-equity-like facilities. Unitranche, in turn, is also making its way into the Spanish market.

Furthermore, and besides the continued increase in acquisition financings and refinancing transactions, it is worth singling out the notable increase in project finance transactions, and in particular, in the real estate and energy sectors, for which the market seems to have a particular appetite as a consequence of the high economic expectations in Spain derived from the Government's projected 2.6% GDP growth for the year 2017.

Finally, the Spanish banking sector has continued to progress and make substantial developments, taking significant steps to consolidate the regulations approved during the previous year. As such, the Spanish Parliament passed Royal Decree-Law 11/2017 on June 23rd, by means of which it approved urgent measures to allow certain banking entities to adopt strategies to improve their resilience to certain risks which may arise from the exercise of their activity, as well as to facilitate their compliance with new international standards.

1.2 What are some significant lending transactions that have taken place in your jurisdiction in recent years?

2017 has seen a continued rise in lending transactions as investors began to regain interest in the Spanish lending market, which has allowed us to expand both nationally, and internationally, through our core lending business and the continued development of our distressed debt practice. Some of our year's highlights would be the following:

- Corporate refinancing and debt restructuring processes: For some years now, we have been actively participating in debt refinancing and restructuring processes, involving large national and international companies from different sectors, which have required forming multidisciplinary teams with a high international element. Some examples include our advice in the debt restructuring of Intrum Justitia AB and Lock AS (€1,100 billion), Grupo Sando group refinancing (through a judicial homologation) (€600 million), Europastry refinancing (€600 million), Elecnor refinancing (€500 million), Atresmedia refinancing (€350 million), as well as our advice on the insolvency proceedings of certain Spanish toll roads (Madrid Radial Highway Network) (€4,528 billion – current total liabilities).
- Project and real estate finance: After several years of putting this advice "on hold" due to Spanish economic recession, we have become active again, advising on transactions involving fresh money. Aside from advising in relevant projects in Spain, we would like to remark that our clients have been increasing their activity abroad, participating in large cross-border transactions worldwide, including projects located in Peru, Chile, Algeria, Saudi Arabia and South Africa. We would highlight our assistance to Natixis for the acquisition of a hotel real estate portfolio (€519 million), Dragados and Iridium in the framework of Pacífico 1 highway concession in Colombia, Pemex in the framework of Litoral Project in Mexico, as well as our involvement with FIEM in the Sadara project, a 19 billion transaction for the construction and operation of a petrochemical plant in Jubail.
- Distressed debt: We are one of the most specialised law firms advising on distressed debt transactions, acquisition of corporate debt, loan portfolios and restructuring debt processes. We have been chosen by major international and prestigious funds and have advised either the distressed/special situations funds (as a purchaser), or the financial institution (as a seller) in many significant deals. Among others, some recent transactions include advising on the sale of non-performing loans portfolio such as Project Tramuntana, Far, Egeo, Nilo, Jets and Gregal, clearly showing the Spanish bank's interest in cleaning up its balance sheets, and international investors' interest in Spanish assets.

2 Guarantees

2.1 Can a company guarantee borrowings of one or more other members of its corporate group (see below for questions relating to fraudulent transfer/financial assistance)?

Such guarantees are not restricted under Spanish law, but certain financial assistance restrictions need to be considered (see question 4.1 below). However, and although Spanish law does not entail any specific obligation for a Spanish company to justify the granting of such guarantee or security, when based on corporate benefit it is advisable (and in some cases, expressly required by law) for both the

Management Body and the General Meeting of Shareholders of the company to approve a resolution indicating that they are aware of the transaction at hand, that they have had the chance to review the documentation of the transaction, and that they validate the terms and conditions of the same, making express reference to the corporate interest or benefit that the guaranteeing or securing company (or the group as a whole, as applicable) will obtain through such transaction.

Finally, subject to certain case law and according to Section 71.2 of the Spanish Insolvency Act, the relevant guarantee constituted by a Spanish subsidiary in favour of its parent company might be challenged by a Spanish court if no consideration (*contraprestación*) is provided to such subsidiary, the mere allegation of the generic interest to the group not being sufficient.

2.2 Are there enforceability or other concerns (such as director liability) if only a disproportionately small (or no) benefit to the guaranteeing/securing company can be shown?

Directors of a Spanish company have a duty of care towards the same, and must act faithfully and loyally towards it. When there is a clear disproportion between the benefit obtained by the borrowing company and that of the securing/guaranteeing company, borrowers tend to request the inclusion of certain limitation language in the collateral documentation and in the corporate resolutions, to minimise a potential liability risk for the Management Body of such securing/guaranteeing company.

Additionally, in case of an eventual insolvency situation on the part of the company, there is a potential risk that the insolvency administrators might presume that the granting of collateral by the company could have resulted in the insolvency and allege that it is detrimental to the insolvency estate; in such case the Management Body could be held liable for its actions.

2.3 Is lack of corporate power an issue?

Yes, in Spain the agreements need to be executed by duly empowered representatives of the company with sufficient corporate power to act on its behalf.

2.4 Are any governmental or other consents or filings, or other formalities (such as shareholder approval), required?

Usually, no governmental consents or filings are required to grant guarantees or security interests in Spain (see question 3.11 below).

Regarding internal corporate approvals, in general terms, any actions or activities which fall within the scope of the corporate purpose of the company are subject to fewer formalities. However, in case of private limited liability companies (*sociedades de responsabilidad limitada*), shareholders' approval may need to be obtained before carrying out certain transactions. In public limited liability companies (*sociedades anónimas*), despite not being mandatory, the shareholders' approval is also usually obtained (see question 2.1 above for more information on corporate benefit).

Additionally, and taking into account the amendments introduced in this field by Law 31/2014 of December 3rd, it may be understood that as a result of the granting of security over an essential asset, a disposal or sale of the same may eventually take place in an enforcement scenario. Therefore, in such cases, and in accordance with article 160.f of the Spanish Companies Law, it is advisable to obtain the relevant shareholders' approval.

For the purposes of the above, an asset shall qualify as essential when the value of the transaction related to such asset exceeds 25% of the value of the assets included in the last balance sheet approved by the company.

2.5 Are net worth, solvency or similar limitations imposed on the amount of a guarantee?

No, although certain limitation language is included in case of a disproportionate benefit between the borrowing company and the guaranteeing/securing company (see question 2.2 above for more information).

2.6 Are there any exchange control or similar obstacles to enforcement of a guarantee?

There are no exchange control regulations on the enforcement of a guarantee. However, Spanish Insolvency Law imposes an important restriction on lenders facing imminent or real insolvency of its debtors, as any termination clauses solely based on insolvency of the debtor which may have been included by the parties in an agreement are deemed as non-applicable or non-enforceable.

3 Collateral Security

3.1 What types of collateral are available to secure lending obligations?

The most commonly used types of collateral in the framework of a financing transaction are generally classified into two main groups: (1) *in rem* security interests, the most frequent being: (i) mortgage over real estate (*hipoteca inmobiliaria*); (ii) ordinary pledge over movable assets with transfer of possession (*prenda ordinaria*) (e.g., pledge over shares, over credit rights or over bank accounts); (iii) chattel mortgage (*hipoteca mobiliaria*); and (iv) non-possessory pledge over assets (*prenda sin desplazamiento de la posesión*); and (2) personal guarantees, mainly being first demand guarantees (*garantías a primer requerimiento*).

The main difference between *in rem* security interests and personal guarantees is that, in the former, a specific asset secures the fulfilment of the obligation, while in the latter, an individual or corporate entity guarantees the fulfilment of the obligation. There are also material differences in their respective enforcement proceedings, as well as how they are considered in an insolvency scenario (*concurso*) under the Spanish Insolvency Act.

3.2 Is it possible to give asset security by means of a general security agreement or is an agreement required in relation to each type of asset? Briefly, what is the procedure?

Spanish law does not provide for or contemplate a so-called "universal security" over the entire debtor's assets. Furthermore, neither does it generally admit the creation of a "floating" or "adjustable" lien or encumbrance, except for certain mortgages granted over real estate. Therefore, a security agreement is usually required in relation to each type of asset.

The creation of guarantees and security interests requires the notarisation of the agreements by means of which they are granted. Such notarisation allows the agreements to qualify as executive title (*título ejecutivo*) in an enforcement scenario, pursuant to article 517 of the Spanish Law on Civil Procedure. Notarial deeds (being either *pólizas notariales* or *escrituras públicas*) provide certainty of the date and content of the applicable document *vis-à-vis* third parties. Furthermore, some of these types of security interests are subject to compulsory entry on public registries, such as the Land Registry (*Registro de la Propiedad*) (e.g., real estate mortgage) or the Chattel Registry (*Registro de Bienes Muebles*) (e.g., mortgage on inventory or non-possessory pledge over assets), while such registration is not required for other collateral (e.g., ordinary pledge with transfer of possession).

3.3 Can collateral security be taken over real property (land), plant, machinery and equipment? Briefly, what is the procedure?

Real property is taken as security by means of a real estate mortgage (*hipoteca inmobiliaria*). Under Spanish law, real estate mortgages cover: (i) the plot of land and the buildings built on it (or which may be built in the future); (ii) the proceeds from the insurance policies insuring such property; (iii) the improvement works carried out on the property; and (iv) natural accretions. Should the parties agree so, such mortgage may also include (i) movable items located permanently in the property, (ii) civil fruits, and (iii) due rents that have not already been satisfied.

Security over machinery and equipment can be created by means of a chattel mortgage (*hipoteca mobiliaria de maquinaria industrial*) or a non-possessory pledge (*prenda sin desplazamiento de maquinaria industrial*). The choice will depend on whether the specific asset meets certain legal requirements.

For both types of security, notarisation is necessary, as well as registration with the relevant public registry (see question 3.2 above).

3.4 Can collateral security be taken over receivables? Briefly, what is the procedure? Are debtors required to be notified of the security?

Security over receivables can be taken in two different manners: (i) by creating a possessory pledge *(prenda ordinaria)*; or (ii) by creating a non-possessory pledge (*prenda sin desplazamiento de la posesión*) which needs to be registered in the Chattel Registry.

With regards to the possessory pledge over receivables, in order for the pledge to be perfected, it is required that the debtor be notified of the granting of the pledge. However, and taking into consideration the commercial impact which such notification could have in the business of the pledgor, sometimes the notice to the relevant debtors is either left in escrow (to be released or delivered only upon potential or effective default) or postponed to a later stage (usually, a stage in which the lender becomes aware of an effective or imminent default).

On the contrary, the non-possessory pledge (*prenda sin desplazamiento de la posesión*) does not require notification to the relevant debtor, since the publicity *vis-à-vis* third parties is obtained through the filing of such pledge with the relevant Chattel Registry.

Further to the above, those claims which are secured by a pledge over future receivables shall be considered as "privileged" in an insolvency proceeding, so long as the following requirements are met: (i) the security interest granted is documented by means of a public deed (*escritura pública*) when it comes to ordinary pledges; or (ii) the security interest is formalised by means of a deed (*póliza notarial*) and is registered in the relevant Chattel Registry in case of a non-possessory pledge.

3.5 Can collateral security be taken over cash deposited in bank accounts? Briefly, what is the procedure?

The pledge over bank accounts is simply a pledge over the credit rights of the holder of the account *vis-à-vis* the bank, which should typically correspond to the account balance.

The formal requirements are identical to those which apply in the case of any other possessory pledge over receivables (notarisation is needed). As indicated in question 3.4 above for the pledge over credit rights, possession is transferred by notification to the depository bank. The creation of the pledge does not imply the freezing of the bank accounts (unless otherwise agreed by the parties), even though such restriction is customarily included in agreements, the triggering event being the occurrence of an enforcement event.

3.6 Can collateral security be taken over shares in companies incorporated in your jurisdiction? Are the shares in certificated form? Can such security validly be granted under a New York or English law governed document? Briefly, what is the procedure?

Yes, collateral security can be taken over shares in companies incorporated in Spain. However, and by virtue of the *lex rei sitae* principle, such pledges should always be governed by Spanish law, not New York or English law. Exceptionally, creating a pledge over shares in companies incorporated in Spain under a law other than Spanish law might be considered, although enforcement proceedings will be longer and burdensome.

Perfection requirements for pledges over shares in Spain usually include: (i) endorsement of share certificates (if these have been issued); (ii) registration of the pledge in the relevant Registry Book of Shareholders or Shares, as applicable; (iii) registration of the pledge in the deeds of acquisition of the relevant shares; and (iv) in the event of shares represented by book entries (*anotaciones en cuenta*) and therefore, belonging to listed companies, registration of the pledge in the book entry register.

Further to the above, and according to Law 14/2013 of 27 September, on Support to Entrepreneurs and its internationalisation (*Ley de Apoyo a los Emprendedores y su internacionalización*), the relevant Registry Book of Shareholders or Shares, as applicable, shall be kept updated and legalised by electronic means (enabling smooth and faster control of the relevant entries).

3.7 Can security be taken over inventory? Briefly, what is the procedure?

Yes, Spanish law foresees a specific mechanism for creating security over inventory, which is the non-possessory pledge over inventory (*prenda sin desplazamiento de inventario*). As provided in questions 3.2 and 3.3 above, this type of collateral requires notarisation as well as registration in the relevant Chattel Registry.

However, it is also possible to create a security over inventory by granting a chattel mortgage over a business (*hipoteca de establecimiento mercantil*), which will include not only the inventory, but the whole business.

3.8 Can a company grant a security interest in order to secure its obligations (i) as a borrower under a credit facility, and (ii) as a guarantor of the obligations of other borrowers and/or guarantors of obligations under a credit facility (see below for questions relating to the giving of guarantees and financial assistance)?

Yes, such possibility is available, although always subject to the Spanish prohibition of financial assistance (see question 4.1 below) and certain corporate benefit issues (see question 2.1 above).

Aside from this, and considering the restriction in Spain regarding floating charges (see question 3.2 above), if the obligations to be secured arise from different types of credit agreements, the Spanish principle of integrity (*principio de especialidad*) (by virtue of which a security interest can secure only one main obligation and its ancillary obligations, such as interest, costs, etc.) must be complied with, which in practice means that when there are two different main obligations which need to be secured, two different security interests (over different assets or portions of the same asset) must be created.

3.9 What are the notarisation, registration, stamp duty and other fees (whether related to property value or otherwise) in relation to security over different types of assets?

Notarial fees are fixed amounts which vary according to the secured liability (approximately 0.03% of the secured liability amount). However, in those transactions with an aggregate value superior to €6 million, such fees can be reduced if negotiated with the notary.

As regards security subject to compulsory entry into public registries (particularly mortgages and non-possessory pledges), in addition to the registry fees (approximately 0.02% of the secured liability amount), some mortgages and certain non-possessory pledges (in particular, those which have been documented by means of a public deed (*escritura pública*) rather than a deed (*póliza notarial*)), also imply payment of stamp duty tax (varying from 0.5% to 1.5% of the secured liability amount – the aggregate of principal, interest and any related costs – depending on the Spanish autonomous region where the collateral is located). Stamp duty tax is not levied on ordinary pledges.

3.10 Do the filing, notification or registration requirements in relation to security over different types of assets involve a significant amount of time or expense?

As regards security documents that need to be filed within a public registry, the expected amount of time from the date the documents are notarised to the actual registration by the public registry is usually from two to six weeks, assuming the relevant security document was correctly drafted and no errors have been identified by the registry which need to be amended by the parties to comply with Spanish legislation. As to related expenses, see question 3.9 above.

3.11 Are any regulatory or similar consents required with respect to the creation of security?

Regulatory or other consents with respect to the creation of security over real property or machinery would apply only in very limited cases, depending on the exact location of the asset, its nature and the parties involved (e.g. mortgage over administrative concessions, which would require the approval by the relevant administrative body).

3.12 If the borrowings to be secured are under a revolving credit facility, are there any special priority or other concerns?

In rem security interests securing a financing have, as a general rule and according to the Spanish Insolvency Act, the status of credits with special privilege. This privilege will be granted to claims arising under the credit facility as a whole, independent of the fact that it is of a revolving nature. Please see section 8 for a better understanding of the priority of such privilege.

3.13 Are there particular documentary or execution requirements (notarisation, execution under power of attorney, counterparts, deeds)?

As explained in question 3.2 above, in Spain security interests are almost always notarised. To appear before a Spanish Notary, all parties must be duly empowered (they can act under powers of attorney, which in case of foreign entities must bear an apostille in accordance with The Hague Convention or a legalisation from the relevant consulate or other competent body).

Signature in counterparts is not used in Spanish law-governed agreements. It is worth mentioning that all parties that are signatories to a Spanish notarial deed must have a Spanish Tax Identification Number (*Número de Identificación Fiscal* or "NIF"), even for non-resident parties and their non-resident attorneys (either individuals or entities), which must request such number before the Spanish Tax Authorities (*Agencia Tributaria*).

Additionally, the Spanish Anti-Money Laundering Law (*Ley 10/2010, de 28 de abril, de prevención del blanqueo de capitales y de la financiación del terrorismo*), requires certain disclosure obligations when executing transactions before a Spanish Notary Public (with certain exceptions, such as those for listed companies or certain financial institutions). In particular, individuals executing a public deed before a Notary Public on behalf of a company need to disclose the identity of the ultimate beneficial owner (*titular real*) of the company, which is:

- the ultimate shareholder or shareholders (individuals) of the company, in the event that a certain person holds (individually), directly or indirectly, a stake exceeding 25% in the share capital of this company; or
- the individual which directly or indirectly controls the management of such company (being understood as control the capacity to name more than half of the members of such management body).

In the event that no individuals hold such a direct or indirect stake or control, the directors/members of the management body of the company are to be regarded as the ultimate beneficial owners and need to be identified too.

4 Financial Assistance

4.1 Are there prohibitions or restrictions on the ability of a company to guarantee and/or give security to support borrowings incurred to finance or refinance the direct or indirect acquisition of: (a) shares of the company; (b) shares of any company which directly or indirectly owns shares in the company; or (c) shares in a sister subsidiary?

Generally, Spanish law prohibits funds being provided (whether by way of loans, guarantees or any other kind of financial support made available before or after the acquisition) by a target company to a third party so that the third party is able to acquire the target company's shares or quotas, or by any other company in the group to which the target company belongs.

Financial assistance is currently prohibited in Spain for:

(a) *sociedades anónimas* (*S.A.*) (public limited companies): for their own shares or the shares of any direct or indirect parent company; and

(b) *sociedades de responsabilidad limitada* (*S.L.*) (private limited companies): for their own units and the units of any member of their corporate group.

The consequence is that, if financial assistance is deemed to have been provided, any such financial assistance will be null and void.

5 Syndicated Lending/Agency/Trustee/Transfers

5.1 Will your jurisdiction recognise the role of an agent or trustee and allow the agent or trustee (rather than each lender acting separately) to enforce the loan documentation and collateral security and to apply the proceeds from the collateral to the claims of all the lenders?

Spanish law does not recognise trusts as a legal figure. Therefore, security trustees, although used in transactions where foreign lenders are involved, are seldom used for the Spanish security package. Instead, lenders tend to appoint an agent for the Spanish security which would hold the Spanish security in its own name and on behalf of the other lenders.

It is possible for the security agent to enforce claims on behalf of the lenders and the other secured parties, as long as each party grants a notarised power of attorney to the security agent expressly authorising it to carry out any enforcement proceedings which may be required. However, authors and case law are inconsistent regarding the role of an agent acting on behalf of the syndicate of lenders upon enforcement.

5.2 If an agent or trustee is not recognised in your jurisdiction, is an alternative mechanism available to achieve the effect referred to above which would allow one party to enforce claims on behalf of all the lenders so that individual lenders do not need to enforce their security separately?

As stated in question 5.1 above, the appointment of an agent for Spanish security is usual market practice for cross-border financings.

5.3 Assume a loan is made to a company organised under the laws of your jurisdiction and guaranteed by a guarantor organised under the laws of your jurisdiction. If such loan is transferred by Lender A to Lender B, are there any special requirements necessary to make the loan and guarantee enforceable by Lender B?

In Spain, debt is traded through assignment (*cesión*), and due to the accessory nature of security interests under Spanish law, any assignment of a participation in a secured financing agreement would automatically entail the proportional assignment of the security interests granted to secure such assigned debt by virtue of article 1,528 of the Spanish Civil Code.

However, for certain types of collateral (mainly those acceding to registers such as mortgages and non-possessory pledges), in order to be effective against third parties the assignment of the relevant collateral must be notarised and registered with the relevant public registry.

6 Withholding, Stamp and Other Taxes; Notarial and Other Costs

6.1 Are there any requirements to deduct or withhold tax from (a) interest payable on loans made to domestic or foreign lenders, or (b) the proceeds of a claim under a guarantee or the proceeds of enforcing security?

In general, interest that Spanish borrowers pay for loans made to domestic lenders (other than financial institutions) is subject to 19% withholding tax in 2018. Likewise, interest income payable on loans made to non-EU tax residents is subject to 19% withholding tax, unless a lower rate applies under a tax treaty (treaty rates range between 5% and 15%). Interest payments to EU residents and EU permanent establishments (except those residing in tax-haven jurisdictions) are not subject to withholding tax (irrespective of whether payments are made to a financial institution or a company).

Second, proceeds of a claim under a guarantee or the proceeds of enforcing security are generally subject to withholding tax as if these payments were made by the borrower.

Since 2012, under the Spanish Corporate Income Tax Act, there have been some limitations to the deductibility of financial expenses:

(a) Financial expenses derived from intergroup indebtedness are not tax-deductible if the funds are used to make capital contributions to other group entities, or to acquire from other group entities shares in other entities, unless the taxpayer proves there are valid economic reasons for doing so.

Overall, financial expenses deriving from indebtedness used for any other reason are fully deductible, unless anti-abuse clauses apply.

However, since 1 January, 2015, interest paid for leveraged buy-out share acquisitions is not tax-deductible unless the following requirements are met:

- Indebtedness must be lower than 70% of the purchase price.
- Indebtedness will be reduced proportionally in the eight years following the transaction by up to 30% of the mentioned price.

(b) Net financial expenses (financial expenses minus financial income) exceeding 30% of the operating profit for the financial year are not tax-deductible, with a minimum of €1 million deductible amount guaranteed. Net financial expenses that, by applying the 30% limit, are not tax-deductible, may be deductible in the following financial years without a time limitation. If the 30% limit is not reached, the difference may increase the applicable limit for the following five financial years.

(c) Interests paid on shareholder loans or participative loans granted by another company, which is part of the same group of companies under Section 42 of the Spanish Commercial Code, are not tax-deductible.

Additionally to the limitations set above, financial expenses, arising from transactions carried out between related parties, are not tax-deductible when the interests paid are not taxed because of the application of different legal qualification under local regulations (i.e. when those interests paid are considered as dividends under the lender's local regulations).

6.2 What tax incentives or other incentives are provided preferentially to foreign lenders? What taxes apply to foreign lenders with respect to their loans, mortgages or other security documents, either for the purposes of effectiveness or registration?

As a member of the European Union, Spain benefits from free movement of capital within the EU, including exchange rate fluctuations and transaction costs. Therefore, Spain's EU membership represents a significant part of its foreign policy.

Additionally, Spain currently has more than 90 income tax treaties in force and a solid treaty network with Latin American countries that reduce or eliminate Spanish taxes payable to residents of treaty countries. In this sense, on July 7th, 2017, Spain signed the OECD multilateral instrument, which modifies a large number of existing bilateral tax treaties by including anti-tax avoidance measures developed in the BEPS project.

These provisions could affect the tax treatment of interests paid by Spanish borrowers to foreign lenders, but a case-by-case analysis should be carried out. These provisions could also affect the withholding taxes applicable to dividends.

The main tax incentive is the Spanish international holding companies ("**ETVEs**") regime, a well-established legal framework that has helped Spain become one of the most favourable jurisdictions in the EU to channel and manage international investments. ETVEs can benefit from an exemption on inbound and outbound dividends and capital gains provided several requirements are met. Since ETVEs are Spanish regular entities, they are treated like regular limited liability companies, thus benefiting from tax treaties signed by Spain and from EU Directives.

Under Spanish law, no relevant additional taxes apply to foreign investments besides those applicable to Spanish investors.

6.3 Will any income of a foreign lender become taxable in your jurisdiction solely because of a loan to or guarantee and/or grant of security from a company in your jurisdiction?

No, under current Spanish Corporate Income Tax regulations, interest or fees paid to the lenders will not be subject to any withholding or deduction, provided that the lenders are lending entities or financial credit establishments entered on the special registries of the Bank of Spain and have their registered office in Spain, or entities resident in the European Union that have submitted certification of their tax residence.

6.4 Will there be any other significant costs which would be incurred by foreign lenders in the grant of such loan/guarantee/security, such as notarial fees, etc.?

To be able to enforce any rights regarding third parties and benefit from summary proceedings (see question 7.3 below) a loan, a guarantee or a security document must be notarised and eventually registered (depending on the asset).

For more detailed information on notarial and registry fees and stamp duty tax, please see question 3.9 above.

6.5 Are there any adverse consequences to a company that is a borrower (such as under thin capitalisation principles) if some or all of the lenders are organised under the laws of a jurisdiction other than your own? Please disregard withholding tax concerns for purposes of this question.

Most tax consequences do not differ as a result of the tax residency or applicable law of the borrower. Exceptionally, adverse tax consequences (documentation obligations and other anti-abuse measures) might arise when the borrower/lender is a tax resident in a tax-haven jurisdiction.

7 Judicial Enforcement

7.1 Will the courts in your jurisdiction recognise a governing law in a contract that is the law of another jurisdiction (a "foreign governing law")? Will courts in your jurisdiction enforce a contract that has a foreign governing law?

Yes, courts in Spain recognise a foreign governing law in contracts in line with Regulation (EC) No. 593/2008 of the European Parliament and of the Council of 17 June, 2008 on the law applicable to contractual obligations ("*Regulation Rome I*").

Regulation Rome I has *erga omnes* effects. Hence, whatever it is, the foreign law chosen to govern a contract is enforceable, irrespective of whether or not it is an EU Member State.

Spanish Courts will certainly enforce a contract governed by foreign law; however, the choice of the parties will not avoid the application of *ius cogens* provisions of Spanish law that cannot be derogated by agreement (public policy). Also, the content and validity of foreign law must be proved in the proceedings; if the foreign law is not proved, the court will resort to Spanish law.

7.2 Will the courts in your jurisdiction recognise and enforce a judgment given against a company in New York courts or English courts (a "foreign judgment") without re-examination of the merits of the case?

A distinction must be made between judgments rendered in English courts or courts of EU Member States and judgments rendered in New York ("**NY**") courts.

Regarding a judgment rendered in English courts, Council Regulation (EC) No. 1215/2012 of December 12th, 2012 on jurisdiction and the recognition and enforcement of judgments in civil and commercial matters ("*Regulation Brussels I recast*"), establishes that a judgment rendered in an EU Member State is to be recognised without special proceedings in any other EU Member State, unless the recognition is contested. Under no circumstances can the merits of a foreign judgment be reviewed. A declaration that a foreign judgment is enforceable is to be issued following purely formal checks of the documents supplied.

However, a judgment will not be recognised if: (i) the recognition is manifestly contrary to public policy in the EU Member State in which recognition is sought; (ii) the defendant was not served with the document that instituted the proceedings in sufficient time and in such a way as to enable the defendant to arrange for his defence; (iii) it is irreconcilable with a judgment given in a dispute between the same parties in the EU Member State in which recognition is sought; (iv) it is irreconcilable with an earlier judgment given in another EU or non-EU country involving the same cause of action and the same parties; or (v) the judgment was adjudicated by a court lacking jurisdiction in case of exclusive jurisdiction.

Regulation Brussels I recast does not apply to a judgment rendered in NY courts. In the absence of a multilateral or bilateral treaty between Spain and the United States addressing the matter, under the recent Act 29/2015, on International Cooperation, final judgment rendered by US courts will have the same force as it is given in the US provided that it complies with the requirements for its recognition set forth in article 46 of the Act on International Cooperation (*inter alia*, the judgment does not infringe Spanish public policy, the defendant has been properly served with the originating process, the matter is not subject to Spanish exclusive jurisdiction for certain matters, or is not in contradiction with a previous Spanish judgment). Once the exequatur is granted, the judgment can be enforced according to the rules set forth in the Spanish Civil Procedure Act.

7.3 Assuming a company is in payment default under a loan agreement or a guarantee agreement and has no legal defence to payment, approximately how long would it take for a foreign lender to (a) assuming the answer to question 7.1 is yes, file a suit against the company in a court in your jurisdiction, obtain a judgment, and enforce the judgment against the assets of the company, and (b) assuming the answer to question 7.2 is yes, enforce a foreign judgment in a court in your jurisdiction against the assets of the company?

This depends primarily on whether the enforcement action is grounded on an executive title, such as public instruments (i.e. a public deed), or on an ordinary title, such as private contracts.

(a) Executive titles can be enforced directly, through summary proceedings, which consist of a swift procedure that should take between nine and 18 months. Otherwise, the so-called ordinary proceedings, which inevitably lead to a decision which should be enforced through an enforcement proceeding, may take on average between 12 and 18 months plus the nine to 18 months of the enforcement proceeding.

(b) Enforcement of an English court decision will follow the same proceeding as explained in point (a), given that the judgment will be recognised without special proceedings. Enforcement of a US judgment would require prior exequatur proceedings (it takes on average between six and nine months). Once the judgment has been recognised, enforcement will follow the same proceeding as explained in point (a) above.

7.4 With respect to enforcing collateral security, are there any significant restrictions which may impact the timing and value of enforcement, such as (a) a requirement for a public auction, or (b) regulatory consents?

Enforcement of collateral security is typically carried out through a public auction (by means of an online auction), in the context of judicial or notarial proceedings. For notarial enforcements, see question 8.4 below. Additionally, the enforcement of pledges over credit rights may also be achieved through set-off or assignment of claims.

The rights derived from the relevant security can be judicially enforced either through declaratory civil proceedings or summary proceedings. The latter action is faster and more effective, while the former is costly and time-consuming. However, to start summary proceedings certain requirements must be met, particularly the determination of the due and payable amount in accordance with the Civil Procedure Act.

Once the court has published a date for auction, the debtor will only be able to object under limited circumstances, such as the prior extinction of the pledge, full payment of the secured obligation, the existence of a material mistake or the existence of abusive clauses.

Concerning the enforcement of pledges over shares, the Financial Collateral Directive was transposed in Spain by means of Royal Decree Law 5/2005, which sets forth a speedy proceeding that applies to obligations of a "financial" nature and which permits direct appropriation of the collateral by the creditor where the financial agreement expressly states so.

7.5 Do restrictions apply to foreign lenders in the event of (a) filing suit against a company in your jurisdiction, or (b) foreclosure on collateral security?

Generally, there is no distinction between domestic and foreign entities when it comes to foreclosing Spanish security.

7.6 Do the bankruptcy, reorganisation or similar laws in your jurisdiction provide for any kind of moratorium on enforcement of lender claims? If so, does the moratorium apply to the enforcement of collateral security?

Bankruptcy declaration triggers an automatic stay of one year (unless the debtor gets the approval of a composition agreement or files for liquidation earlier). This automatic stay concerns secured creditors with collateral over assets that are necessary to continue the ordinary course (except security interests subject to the special regime on financial collateral).

During the stay, the bankruptcy officer may decide to treat the secured claim as an administrative expense (pre-deductible claims from the estate) in order to avert enforcement of the security interest.

This automatic stay can also apply if the debtor serves a "5 *bis*" notice, which enables the debtor to negotiate an out-of-court solution to financial distress in a four-month period. The stay of enforcement action, which does not apply to public claims, lasts for a three- or four-month period (there are different criteria) and concerns assets that are necessary to continue the ordinary course. Yet any enforcement action conducted by holders of financial claims may be stayed if the debtor obtains a standstill supported by 51% of the financial claims. Security interests subject to the special regime on financial collateral escape this automatic stay in any event.

Lastly, if the secured creditor fails to enforce the security interest prior to liquidation (or reinitiate the formerly stayed enforcement proceeding as a result of bankruptcy declaration), it may lose control over the collateral if the liquidation plan sets forth the sale of the business unit as a going concern. In exchange for losing control to enforce the security interest on a stand-alone basis, secured creditors obtain a portion of the price equivalent to the weight of the collateral in the estate. If that percentage of the price is less than the value recognised in the proceeding for the security interest, secured lenders that initiated the enforcement proceeding prior to bankruptcy declaration, but did not reinitiate it after the one-year automatic stay, have a veto right as to the approval of the liquidation plan, unless 75% in value of the secured claims from the same class (financial, labour, public, commercial) were to consent to it.

Lastly, the Civil Procedure Act provides that the moratorium on enforcement on the grounds of criminal procedure may halt the enforcement and performance of such agreements until the criminal court issues a final resolution in such proceedings.

On another front, the Civil Procedure Act provides a moratorium on enforcement on the grounds of criminal procedure which may halt the enforcement and performance of such agreements until the criminal court issues a final resolution in such proceedings.

7.7 Will the courts in your jurisdiction recognise and enforce an arbitral award given against the company without re-examination of the merits?

Yes, Spain has been a party to the 1958 New York Convention on Recognition and Enforcement of Foreign Arbitral Awards ("New York Convention") since 1977, and it is therefore subject to recognition and enforcement of foreign arbitral awards in the terms established therein.

Given that Spain has not presented any reservations to the New York Convention, its proceedings are applied to the enforcement of all arbitral awards, including those rendered in countries that did not sign the convention. The Spanish Arbitration Act specifically establishes that the exequatur of foreign awards will be governed by: (i) the New York Convention, without prejudice to the provisions of other, more favourable international treaties on the granting of foreign awards; and (ii) the proceedings established in the civil procedural system for judgments handed down by foreign courts.

Spanish courts will not re-examine the merits of the case. However, an arbitral award might not be recognised if certain requirements are not met (e.g. the arbitration agreement is not valid, irregularity in the composition of the arbitration authority or in the arbitral procedure, etc.). Furthermore, an award will not be recognised if the subject matter cannot be settled by arbitration in Spain or the recognition is contrary to the public policy of Spain.

8 Bankruptcy Proceedings

8.1 How does a bankruptcy proceeding in respect of a company affect the ability of a lender to enforce its rights as a secured party over the collateral security?

Bankruptcy declaration triggers an automatic stay of one year (unless the debtor gets the approval of a composition agreement or files for liquidation earlier). This automatic stay concerns secured creditors with collateral over assets that are necessary to continue the ordinary course (except security interests subject to the special regime on financial collateral or relating to collateral located outside of Spain).

During the stay, the bankruptcy officer may decide to treat the secured claim as an administrative expense (pre-deductible claims from the estate) in order to avert enforcement of the security interest.

This automatic stay can also apply if the debtor serves a "5 *bis*" notice, which enables the debtor to negotiate an out-of-court solution to financial distress in a four-month period. The stay of enforcement actions lasts for a three- or four-month period (there are different criteria) and concerns assets that are necessary to continue the ordinary course. Yet, any enforcement action conducted by holders of financial claims may be stayed if the debtor obtains a standstill supported by 51% of the financial claims. Security interests, subject to the special regime on financial collateral, escape this automatic stay in any event. Besides, public claims cannot be affected in any way by a "5 *bis*" notice.

Lastly, if the secured creditor fails to enforce prior to liquidation, it may lose control over the collateral concerning business units sales, in which case it would get a portion of the price equivalent to the weight of the collateral in the estate. Even secured creditors having enforced prior to liquidation may lose control over the collateral within the framework of business units sales, provided they receive a percentage of the price equivalent to the security interest value as recognised in the bankruptcy proceeding (otherwise, individual consent would be needed unless 75% of the secured claims from the same class sign off). The claim comprising the difference between the resulting price and the value of the secured claim (the deficiency claim) will be classified as unsecured.

8.2 Are there any preference periods, clawback rights or other preferential creditors' rights (e.g., tax debts, employees' claims) with respect to the security?

Pursuant to compulsory priority rules, claims are divided into privileged, ordinary, and subordinated. Privileged claims, which are in turn divided into special privileged (secured) claims and general privileged claims (such as certain torts, tax, social security and employees' claims), are given preferential treatment over ordinary claims, which in turn have preference over subordinated claims. A controlling principle is the equal treatment of creditors from the same class.

Administrative expenses (*créditos contra la masa*) have a cash flow privilege over claims (*créditos concursales*). In contrast to administrative expenses, claims can only be settled pursuant to a plan of reorganisation or with the proceeds arising out of liquidation (either piecemeal or, preferably, as a going concern business). Having said that, secured creditors may auction or repossess the collateral to apply the proceeds thereof to settle their claims (over which administrative expenses have no priority).

Acts or transactions beyond the ordinary course of business entered into within two years prior to bankruptcy declaration may be subject to clawback, so long as: (i) the debtor does not receive reasonably equivalent value in exchange; or (ii) certain creditors are preferred to others when the company is currently insolvent (i.e. unable to regularly pay its debts as they come due). The hardening period in both cases is two years.

The law sets forth certain rebuttable and non-rebuttable presumptions of transactions that are detrimental to the estate. There are also certain safe harbours (namely acts and transactions done within the ordinary course of business, and certain ring-fenced out-of-court solutions).

Actual intent or fraud is not required to bring a clawback action successfully. Yet, in case of actual fraud the reach-back period is four years (and the action can be brought both within and aside from an insolvency proceeding). Moreover, fraud is a requirement to claw back security interests subject to the special regimen on financial collateral.

Concerning acts or transactions subject to foreign law, the defendant may thwart the clawback action by proving that such act or transaction is ring-fenced under applicable law.

8.3 Are there any entities that are excluded from bankruptcy proceedings and, if so, what is the applicable legislation?

Governmental entities of any type (whether territorially based – such as national, regional, municipal authorities – or of a functional nature) are excluded from bankruptcy proceedings. However, companies directly or indirectly controlled by governmental entities are subject to general bankruptcy law.

Additionally, certain types of companies (such as insurance companies) are subject to specific insolvency regulations, although the composition, appointment and operation of the insolvency administration will still be regulated by general bankruptcy law.

8.4 Are there any processes other than court proceedings that are available to a creditor to seize the assets of a company in an enforcement?

Yes, out-of-court enforcement proceedings, available for certain types of security, are typically carried out by a Notary Public and take the form of a public auction. The terms and conditions of such auction are not entirely regulated in the law and hence they usually follow the provisions agreed by the parties in the relevant security documents. Absent a specific agreement, the Notary Public also tends to follow equivalent provisions applicable to judicial enforcements.

In the case of security over bank accounts or listed securities, particularly when the secured obligation consists of cash settlement agreements or derivative contracts, secured lenders may appropriate directly and immediately the secured assets (or offset), without conducting a public auction. Equally, certain regional laws (such as Catalonian law) expressly permit either private sales or, in the case of highly liquid security, appropriation by set-off.

9 Jurisdiction and Waiver of Immunity

9.1 Is a party's submission to a foreign jurisdiction legally binding and enforceable under the laws of your jurisdiction?

The submission by the parties of an agreement to a foreign jurisdiction is valid, binding and enforceable in Spain:

(i) in the case of submission to the courts of an EU Member State: in accordance with the provisions on *prorogation of jurisdiction* contained in Regulation Brussels I recast (*supra* question 7.2), except in cases where the rules on exclusive jurisdiction of the Regulation are to be applied (in general, concerned with proceedings referred to: (a) *in rem* rights or tenancies in immovable property; (b) the validity of the constitution, nullity or dissolution of companies or other legal persons, or the validity of the decisions of their organs; (c) the validity of entries in public registers; (d) the registration of patents, trademarks, designs or other similar rights subject to deposit or registration; and (e) the enforcement of judgments);

(ii) in the case of submission to non-EU foreign courts abiding by conventions: in accordance with the applicable international bilateral conventions (*ad ex*. Hague Convention of June 30th, 2005 on Choice of Court Agreements); and

(iii) in the case of submission to foreign courts not covered by conventions: in accordance with the Spanish Organic Law of the Judiciary, such submission would be valid, unless the exclusive jurisdiction of the Spanish courts is violated (in general, the same cases described *supra* in (i) (a) to (e), with regard to Regulation Brussels I recast).

9.2 Is a party's waiver of sovereign immunity legally binding and enforceable under the laws of your jurisdiction?

Under Spanish law, the waiver of sovereign immunity (either of jurisdiction or of execution) by a foreign state is legally valid and enforceable. The waiver may be explicit (by means of an international agreement, a written contract or a declaration, or a written communication made within the proceedings to the relevant tribunal) or tacit (as a result of certain acts on the side of the foreign state), in accordance with Spanish Organic Law 16/2015 of October 27th, 2015.

Absent the waiver of sovereign immunity, no asset owned or controlled by a foreign state and allocated to public and official (i.e., non-commercial) purposes can be seized or subject to enforcement proceedings in Spain. This includes assets: (a) used by the diplomatic missions or consular offices of the foreign state for the performance of their duties and functions (including bank accounts, with the exception of accounts exclusively used for commercial purposes); (b) used for military purposes; (c) of the central bank or similar monetary authority of the foreign state and used for the performance of their duties and functions; (d) forming part of the foreign state's cultural heritage or with scientific, cultural or historical interest (with the exception of assets offered for sale); and (e) official vessels and airships, exclusively attached to public services of a non-commercial nature.

10 Licensing

10.1 What are the licensing and other eligibility requirements in your jurisdiction for lenders to a company in your jurisdiction, if any? Are these licensing and eligibility requirements different for a "foreign" lender (i.e. a lender that is not located in your jurisdiction)? In connection with any such requirements, is a distinction made under the laws of your jurisdiction between a lender that is a bank *versus* a lender that is a non-bank? If there are such requirements in your jurisdiction, what are the consequences for a lender that has not satisfied such requirements but has nonetheless made a loan to a company in your jurisdiction? What are the licensing and other eligibility requirements in your jurisdiction for an agent under a syndicated facility for lenders to a company in your jurisdiction?

There is no need for foreign or local lenders or agents under a syndicated facility to be resident, licensed, qualified or entitled to do business in Spain to execute or enforce any rights in Spain under any financing agreements or collateral agreements, provided that, in the case of foreign lenders (and where and if applicable), they are licensed, qualified or entitled to do business in their own jurisdiction of incorporation. Consequently, there is no material distinction between domestic and foreign creditors for the purposes of granting loans or security. Nevertheless, foreign lenders are still subject to some of the abovementioned formalities, such as the obligation to obtain a Spanish tax identification number (*NIF*) (as explained in question 3.13 above).

11 Other Matters

11.1 Are there any other material considerations which should be taken into account by lenders when participating in financings in your jurisdiction?

Most of the relevant issues have already been covered in the previous questions. However, we take the opportunity to point out that the Spanish Companies Act sets out the conditions under which a Spanish company (whether in the form of a public limited liability company (*sociedad anónima*) or in the form of a private limited liability company (*sociedad de responsabilidad limitada*)) may issue and guarantee debt securities.

Because of recent amendments to such law, limited liability companies are now allowed (as opposed to the previous regulations in this regard) to issue and guarantee bonds and other securities that create or recognise debt, except for convertible instruments (i.e., securities which can be converted into equity).

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CUATRECASAS

With over 900 lawyers and more than a century of professional practice, Cuatrecasas is a leading law firm present in over 11 countries. We cover all areas of business law with a sectorial approach, focusing on all types of business, while always maintaining close, long-standing relationships with leading companies in every sector. Both the firm and our lawyers receive prestigious national and international awards year after year, acknowledging our reputation and technical skills. In 2014, *Chambers & Partners* recognised the firm as the "Spain Law Firm of the Year", and in 2016 the firm was considered one of the top five most innovative firms in Continental Europe in the *Financial Times* Innovative Lawyers Awards. Furthermore, we are also highlighted as leading firm for the main law practices by international directories such as *Chambers*, *IFLR* or *The Legal 500*.

Our Finance Practice consists of nearly 70 lawyers based in Madrid, Barcelona, Lisbon New York and London, with expert knowledge and extensive experience in complex national and international financial transactions. The lawyers work seamlessly from different locations, ensuring wide coverage for their clients, wherever they are based. The team has extensive expertise advising sponsors and banks in all types of domestic or foreign, corporate and structured, financial and debt capital markets transactions. Among others, such transactions consist of structured and project financial facilities, refinancing, acquisition finance and other sorts of repackaging, synthetic and mortgaged-backed securitisation, credit assignments, issuance of fixed-interest securities and other financial instruments, and consumer credits. In addition, we deal with bankruptcy issues in order to efficiently ensure the bankruptcy remoteness and an adequate security package structure, extending the scope of our advice to the restructuring of debt. Likewise, we advise on matters and relevant issues related to equity requirements for credit institutions as well as for other entities.

"Ranked as leading Firm (1st tier) in Project Finance, Capital Markets and Debt Restructuring" – (*Chambers & Partners*, 2017).

"Ranked as leading Firm (1st tier) in Banking & Finance, Project Finance, Capital Markets and Debt Restructuring" – (*The Legal 500*, 2017).

"31 lawyers ranked in Finance practices in Spain" – (*Best Lawyers*, 2017).

"Only Iberian law firm among top 10 by volume for syndicated loan transactions (EMEA region)" – (*Bloomberg*, 2016).

"Standout in the category of Finance" – (*FT Innovative Lawyers*, 2013).

Sweden

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1 Overview

1.1 What are the main trends/significant developments in the lending markets in your jurisdiction?

The debt capital markets in Sweden have been very strong during the last couple of years. The local banks remain strong and international banks and financial institutions are showing increasing interest in doing business in Sweden. Competition among lenders is fairly intense, as many Swedish blue-chip companies have limited need for debt funding due to strong balance sheets and plenty of liquidity. Another development that has increased the competition among debt providers is the development of a substantial and growing Swedish bond market where bonds are issued under local law documentation.

2 Guarantees

2.1 Can a company guarantee borrowings of one or more other members of its corporate group (see below for questions relating to fraudulent transfer/financial assistance)?

The general rule under Swedish law is that a limited company (*Sw. Aktiebolag*) is free to guarantee the obligations of one or more other members of its corporate group, subject to certain restrictions described below under questions 2.2 and 4.1.

2.2 Are there enforceability or other concerns (such as director liability) if only a disproportionately small (or no) benefit to the guaranteeing/securing company can be shown?

A guarantee or security interest granted by a limited company may be invalid and unenforceable if the transaction reduces the company's net worth and cannot be commercially justified (i.e. lacking sufficient corporate benefit). Such a transaction is considered to be a value transfer under Swedish law. A value transfer may only take place if the company's restricted equity is fully covered after the transfer and the transfer can be justified in light of any additional funding requirements that might follow from the company's nature of business as well as the company's consolidation requirements, liquidity and financial position in general. The transaction will be considered to be an unlawful value transfer if these requirements are not fulfilled. In the event of an unlawful value transfer, the recipient of such transfer must return what he or she has received if the company shows that the recipient knew or ought to have realised that the transaction constituted a value transfer from the company.

If a deficiency arises when restitution is made as described above, then those involved in the decision to make the value transfer will be liable for such shortfall. The same applies to those involved in implementing the value transfer. A director can therefore be held responsible for any losses incurred by the company as a result of guarantees and security interests being issued or granted without sufficient benefit for the issuing company.

Granting guarantees and security for wholly owned subsidiaries is typically considered to be commercially justified and therefore not subject to the value transfer restrictions referred to above. However, upstream and cross-stream guarantees and security interests, as well as guarantees and security interests for subsidiaries which are not wholly owned, are sensitive and may not be considered to be commercially justified. The value transfer restrictions may therefore be relevant in case of such guarantees and security interests.

2.3 Is lack of corporate power an issue?

Lack of corporate power is generally not an issue when Swedish companies enter into financing arrangements.

2.4 Are any governmental or other consents or filings, or other formalities (such as shareholder approval), required?

No governmental or other consents or filings are required in order for a Swedish limited liability company to provide guarantees or grant security interests. Shareholder approval is generally not required for granting guarantees and security interests, but may sometimes be advisable; for example, in the case of guarantees and security interests granted by companies that are not wholly owned.

2.5 Are net worth, solvency or similar limitations imposed on the amount of a guarantee?

As further described in question 2.2 above, the granting of guarantees and security interests may in certain situations be deemed to constitute value transfers and is as such only allowed if the company's restricted equity is fully covered after the value transfer and the transfer can be justified in light of any additional funding requirements that might follow from the company's nature of business as well as the company's consolidation requirements, liquidity and financial position in general.

Guarantees and security interests granted by an insolvent Swedish company will be subject to clawback risk should the company enter into bankruptcy within certain hardening periods. Any director of an insolvent company that gives preferential treatment to certain creditors of the insolvent company may be held criminally liable as well as liable to pay damages.

2.6 Are there any exchange control or similar obstacles to enforcement of a guarantee?

Sweden has no exchange control provisions or similar obstacles restricting the enforcement of a guarantee issued by a Swedish limited company.

3 Collateral Security

3.1 What types of collateral are available to secure lending obligations?

There are a number of different types of collateral and security interests that can be made available under Swedish law. The most common security interest under Swedish law is the pledge. Under Swedish law, as a general rule, any property or asset can be validly pledged.

3.2 Is it possible to give asset security by means of a general security agreement or is an agreement required in relation to each type of asset? Briefly, what is the procedure?

Swedish law does not recognise the concept of a general security agreement covering all or almost all of the assets of a security provider. Instead, the starting point is that separate security agreements must be entered into in respect of separate assets or separate classes of assets.

Notwithstanding the above, it is possible to grant security over different assets and different types of assets by way of one single security agreement. However, this is often rather impractical, as different perfection and enforcement requirements often apply for different types of assets, which makes all-inclusive security agreements rather extensive and burdensome to draft and apply.

The most common way to take security over assets in general is by way of a floating charge, in accordance with the Floating Charges Act.

3.3 Can collateral security be taken over real property (land), plant, machinery and equipment? Briefly, what is the procedure?

The primary means of taking security over real property (i.e. land and buildings and other fixtures thereon) is by way of real estate mortgages. However, such real estate mortgages may, as described in question 3.9 below, be subject to stamp duty, so alternative security arrangements such as share pledges over ring-fenced property companies are also common.

Certain equipment and machinery which is more or less permanently incorporated into a real property can, subject to the prevailing circumstances, be either included in the real property (and thus covered by a real estate mortgage) or be considered as assets which are separated from the real property and therefore can be subject to other security arrangements besides a real estate mortgage.

Collateral can be taken over machinery in a variety of different ways depending on the type of machinery. Machines that are movable goods can be pledged as collateral, but this requires that the movable goods are handed over to the pledgee or to a third party representing the pledgee. If the security provider needs to continue to use the machinery, then a so-called chattel-sale (*Sw. lösöreköpsregistrering*) can be made whereby a perfected security interest is created by way of a public announcement followed by a registration with the Swedish Enforcement Authority (*Sw. Kronofogdemyndigheten*).

3.4 Can collateral security be taken over receivables? Briefly, what is the procedure? Are debtors required to be notified of the security?

Security can be taken over receivables and such security is established through a notification of the debtor under the receivable which is subject to such security arrangement. In order for the security interest to be perfected, all payments under the receivables must – as a general rule – be paid to the secured party or to a representative of the secured party. This can sometimes be commercially sensitive as well as administratively onerous at least as regards account receivables. It is therefore quite common with delayed perfection so that the notification of the debtor and the re-direction of payments are only made following a certain credit event relating to the security provider.

It should be noted that relying on delayed perfection (in respect of receivables as well as any other security interests) stands the risk of clawback during certain hardening periods should the security provider file for bankruptcy shortly after the completion of delayed perfection.

3.5 Can collateral security be taken over cash deposited in bank accounts? Briefly, what is the procedure?

Security can be granted over cash deposited in bank accounts. Such security is granted by way of the bank account being pledged to the secured party. It should be noted that Swedish law contains very strict perfection requirements regarding bank account pledges. In order for the pledge to be perfected and enforceable, the pledgor must be deprived of all disposal rights to the bank account. Bank account pledges are therefore not suitable for bank accounts used in the day-to-day activities of the pledgor.

Due to the restrictions set out above, the standard approach in Sweden is to take security over deposit accounts rather than current accounts used for daily business. To the extent that current accounts are pledged, it is common to use delayed perfection arrangements so that the pledgor is only deprived of its disposal rights over the pledged current account following certain credit events. As mentioned above, these type of arrangements stand the risk of clawback during certain hardening periods in case the security provider subsequently enters into bankruptcy proceedings.

3.6 Can collateral security be taken over shares in companies incorporated in your jurisdiction? Are the shares in certificated form? Can such security validly be granted under a New York or English law governed document? Briefly, what is the procedure?

Security over shares is one of the most common security interests in Sweden and is established through a pledge agreement. The perfection requirements for a share pledge depend on whether the shares are represented by physical share certificates or the shares are dematerialised (i.e. in register form). Physical share certificates must be handed over to the secured party or to a third party representing the secured party, whereas dematerialised shares are generally pledged via account entries with the Central Securities Depository as further set out in the Swedish Financial Instruments (Accounts) Act.

A share pledge agreement in respect of shares in a Swedish limited company does not have to be governed by Swedish law and can, for example, be governed by English or New York law. However, Swedish law would nevertheless, as a general rule, still apply in respect of perfection requirements. Furthermore, Swedish law contains certain mandatory duty of care provisions that are aimed at protecting a pledgor; for example, in connection with a security enforcement. It is therefore advisable that the share pledge agreement is governed by Swedish law and this is also the prevailing market standard.

3.7 Can security be taken over inventory? Briefly, what is the procedure?

As mentioned above under question 3.1, any property or asset can be validly pledged as long as it meets certain criteria. However, in order for an inventory pledge to be perfected and enforceable, the pledgor cannot remain in the possession of the pledged inventory. Inventory pledges are therefore very impractical. A more common way to take security over a floating asset base such as an inventory is instead to issue a floating charge as further described in question 3.2 above.

3.8 Can a company grant a security interest in order to secure its obligations (i) as a borrower under a credit facility, and (ii) as a guarantor of the obligations of other borrowers and/or guarantors of obligations under a credit facility (see below for questions relating to the giving of guarantees and financial assistance)?

Yes, please see above under questions 2.1 and 2.2 and below under section 4 for further details. The restrictions described above in respect of granting of guarantees also apply to the granting of security.

3.9 What are the notarisation, registration, stamp duty and other fees (whether related to property value or otherwise) in relation to security over different types of assets?

No notarisation or registration costs, stamp duties or other fees are payable in relation to the granting of security over receivables and shares.

An application for new real estate mortgages is subject to a stamp duty of two (2) per cent, payable on the face value of such new real estate mortgages. Existing real estate mortgages can, however, be re-pledged an infinite number of times without incurring any additional stamp duty.

An application for new floating charges is subject to a stamp duty of one (1) per cent, payable on the face value of such new floating charges. As with real estate mortgages, existing floating charges can also be re-pledged an infinite number of times without incurring any additional stamp duty.

Finally, it should be noted that minor application fees are payable when applying for new real estate mortgage or floating charges, as well as when applying for a chattel-sale or security over certain intellectual property to be registered.

3.10 Do the filing, notification or registration requirements in relation to security over different types of assets involve a significant amount of time or expense?

Most security interests can also be established more or less immediately and there are no significant costs for granting security other than the stamp duty referred to in question 3.9 above.

3.11 Are any regulatory or similar consents required with respect to the creation of security?

There are no such consents required.

3.12 If the borrowings to be secured are under a revolving credit facility, are there any special priority or other concerns?

No, there are not.

3.13 Are there particular documentary or execution requirements (notarisation, execution under power of attorney, counterparts, deeds)?

There are no such requirements.

4 Financial Assistance

4.1 Are there prohibitions or restrictions on the ability of a company to guarantee and/or give security to support borrowings incurred to finance or refinance the direct or indirect acquisition of: (a) shares of the company; (b) shares of any company which directly or indirectly owns shares in the company; or (c) shares in a sister subsidiary?

The restrictions on financial assistance are set out in the Swedish Companies Act. According to the Companies Act, a Swedish limited company may not pay an advance, grant loans or provide security for loans to a borrower (or certain affiliates to such borrower) for the purpose of funding such borrower's acquisition of shares in the company or any parent company in the same group as the company granting the financial assistance.

A Swedish limited company can therefore not support borrowings incurred for the purposes of (a) and (b) in the question above. As regards (c), there is some uncertainty under Swedish law. It is clear that the intention of the legislator has been that such financial assistance shall be forbidden, but the relevant provisions of the Companies Act seem to indicate otherwise. Great caution should therefore be exercised when considering such transactions.

It should be noted that Swedish law provides for some opportunities to grant financial assistance after the completion of an acquisition. Furthermore, there is a regime in the Companies Act whereby exemptions can be granted for otherwise unlawful financial assistance.

5 Syndicated Lending/Agency/Trustee/Transfers

5.1 Will your jurisdiction recognise the role of an agent or trustee and allow the agent or trustee (rather than each lender acting separately) to enforce the loan documentation and collateral security and to apply the proceeds from the collateral to the claims of all the lenders?

Lenders may appoint a facility and/or security agent to represent them in all matters relating to the finance documents as well as any security interests. Such agents are allowed to enforce any rights that the lenders might have under the finance documents. Furthermore, the agent may enforce any collateral security and apply the proceeds from such enforcement in order to satisfy the secured claims of the lenders.

5.2 If an agent or trustee is not recognised in your jurisdiction, is an alternative mechanism available to achieve the effect referred to above which would allow one party to enforce claims on behalf of all the lenders so that individual lenders do not need to enforce their security separately?

Please see question 5.1 above.

5.3 Assume a loan is made to a company organised under the laws of your jurisdiction and guaranteed by a guarantor organised under the laws of your jurisdiction. If such loan is transferred by Lender A to Lender B, are there any special requirements necessary to make the loan and guarantee enforceable by Lender B?

A transfer of a loan is perfected and made valid and enforceable against third parties by way of notification of the debtor under the loan that is being transferred.

A guarantee in respect of a loan obligation will continue to apply and may be called upon by any new lender that has validly acquired the loan that is being guaranteed. The guarantor is sometimes notified of the loan transfer in order to avoid the guarantor fulfilling its guarantee obligation by way of payments to the initial holder of the loans.

6 Withholding, Stamp and Other Taxes; Notarial and Other Costs

6.1 Are there any requirements to deduct or withhold tax from (a) interest payable on loans made to domestic or foreign lenders, or (b) the proceeds of a claim under a guarantee or the proceeds of enforcing security?

Swedish law neither contains an obligation to withhold tax as regards interest payable on loans made to a domestic lender or foreign lender, nor on proceeds of a claim under a guarantee or the proceeds following from an enforcement of security interests.

6.2 What tax incentives or other incentives are provided preferentially to foreign lenders? What taxes apply to foreign lenders with respect to their loans, mortgages or other security documents, either for the purposes of effectiveness or registration?

No tax incentives are provided preferentially to foreign lenders.

No taxes apply to foreign lenders, provided that such foreign lenders do not have any permanent establishment in Sweden with which the income from the loan, guarantee or security interest is effectively connected.

6.3 Will any income of a foreign lender become taxable in your jurisdiction solely because of a loan to or guarantee and/or grant of security from a company in your jurisdiction?

No, provided that such foreign lender does not have any permanent establishment in Sweden with which the income from the loan, guarantee or security interest is effectively connected.

6.4 Will there be any other significant costs which would be incurred by foreign lenders in the grant of such loan/guarantee/security, such as notarial fees, etc.?

No. Please see question 3.9 above.

6.5 Are there any adverse consequences to a company that is a borrower (such as under thin capitalisation principles) if some or all of the lenders are organised under the laws of a jurisdiction other than your own? Please disregard withholding tax concerns for purposes of this question.

There are no adverse consequences for a Swedish borrower if some or all of the lenders are non-Swedish, as long as such loans are made on market terms and are not made between related parties.

Swedish legislation does not contain any thin capitalisation rules. However, Swedish legislation does contain interest deduction restriction rules on intra-group loan structures including back-to-back structures involving third-party lenders (e.g. banks). These rules apply both for loan structures involving only Swedish companies as well as loan structures involving both Swedish and non-Swedish companies.

7 Judicial Enforcement

7.1 Will the courts in your jurisdiction recognise a governing law in a contract that is the law of another jurisdiction (a "foreign governing law")? Will courts in your jurisdiction enforce a contract that has a foreign governing law?

The application of foreign law is recognised by Swedish courts, except to the extent that provisions in foreign law are contrary to the *ordre public* (i.e. such provisions that are inconsistent with fundamental principles of the legal system in Sweden).

7.2 Will the courts in your jurisdiction recognise and enforce a judgment given against a company in New York courts or English courts (a "foreign judgment") without re-examination of the merits of the case?

A final and conclusive judgment rendered by a federal or state court located in the State of New York would in principle neither be recognised nor enforceable in Sweden as a matter of right without a retrial on the merits (but will be of some persuasive authority as a matter of evidence before the courts of Sweden or other public authorities). However, according to Swedish Supreme Court case law, judgments (i) that are based on a jurisdiction clause (the Swedish court may assess whether the jurisdiction clause validly appoints the foreign court), (ii) that were rendered under observance of due process, (iii) against which there lies no further appeal, and (iv) the recognition of which would not manifestly contravene fundamental principles of the legal policy of Sweden, can under certain circumstances form the basis for an identical Swedish judgment without a retrial on the merits.

A final, conclusive and enforceable judgment given by an English court would – pursuant and subject to the provisions of the Regulation (EU) No 1215/2012 of the European Parliament and of the Council of 12 December 2012 on Jurisdiction and the Recognition and Enforcement of Judgments in Civil and Commercial Matters (recast) (the "2012 Brussels I Regulation") – be enforceable in Sweden without any declaration of enforceability being required.

Finally, it should be noted that Sweden has acceded to the Convention on the Recognition and Enforcement of Foreign Arbitral Awards, New York, 1958 (the "New York Convention"). A final and conclusive arbitral award, which is enforceable in England or New York and has been duly served on the relevant party, rendered by an arbitral tribunal in England or New York, will be recognised and enforceable by the courts of Sweden, according and subject to the New York Convention and the Swedish Arbitration Act (*Sw. lag (1999:116) om skiljeförfarande*). In order to enforce an arbitral award under the New York Convention in Sweden, the concerned party must submit an application for enforcement (*Sw. exekvatur*) to the Svea Court of Appeal (*Sw. Svea hovrätt*) and comply with the procedures of that court (as required).

7.3 Assuming a company is in payment default under a loan agreement or a guarantee agreement and has no legal defence to payment, approximately how long would it take for a foreign lender to (a) assuming the answer to question 7.1 is yes, file a suit against the company in a court in your jurisdiction, obtain a judgment, and enforce the judgment against the assets of the company, and (b) assuming the answer to question 7.2 is yes, enforce a foreign judgment in a court in your jurisdiction against the assets of the company?

If the 2012 Brussels I Regulation applies (see question 7.2 above), a foreign judgment can, upon application, be enforced by the Enforcement Agency more or less immediately if delay places the applicant's claim at risk and the judgment debtor does not apply for refusal of enforcement with the designated district court.

The application for enforcement (*Sw. exekvatur*) of an arbitral award normally takes approximately three to six months.

7.4 With respect to enforcing collateral security, are there any significant restrictions which may impact the timing and value of enforcement, such as (a) a requirement for a public auction, or (b) regulatory consents?

If the pledge agreement has an enforcement clause, the creditor is free to enforce the collateral according to the regime set out in such enforcement clause. Otherwise, the creditor may seek enforcement (assuming he has a title of execution) with the Swedish Enforcement Authority. The procedure is governed by the Enforcement Execution Act.

Notwithstanding the above, certain security interests, such as, for example, real estate mortgages and floating charges, can only be enforced through the Swedish Enforcement Authority.

There is a general duty of care obligation under Swedish law whereby a secured party must also look after the interests of the security provider when enforcing security interests. Any excess amounts following such enforcement must also be accounted for and paid out to the security provider.

7.5 Do restrictions apply to foreign lenders in the event of (a) filing suit against a company in your jurisdiction, or (b) foreclosure on collateral security?

If required by an EU or EFTA defendant (i.e. including a Swedish defendant), a foreign plaintiff not domiciled in an EU or EFTA country must furnish security for the legal costs that he might be obliged to pay as a result of the proceedings. By virtue of several multilateral treaties to which Sweden is a party, plaintiffs of a large number of countries have been relieved from the obligation to furnish security.

There are no restrictions for foreign lenders in the event of foreclosure on collateral security.

7.6 Do the bankruptcy, reorganisation or similar laws in your jurisdiction provide for any kind of moratorium on enforcement of lender claims? If so, does the moratorium apply to the enforcement of collateral security?

Yes. Please see question 8.1 below.

7.7 Will the courts in your jurisdiction recognise and enforce an arbitral award given against the company without re-examination of the merits?

Yes. Foreign awards based on an arbitration agreement are recognised and enforced in Sweden. In 1972 Sweden ratified the New York Convention without reservation. Its provisions have been incorporated into Swedish law by the Swedish Arbitration Act. Please see questions 7.2 and 7.3 for further information.

8 Bankruptcy Proceedings

8.1 How does a bankruptcy proceeding in respect of a company affect the ability of a lender to enforce its rights as a secured party over the collateral security?

Following a bankruptcy order, no independent enforcement is, as a general rule, available for secured creditors. However, a creditor that has a valid and perfected possessory pledge (*Sw. handpanträtt*) may sell such collateral at a public auction, subject to such auction not occurring earlier than four (4) weeks after the meeting for administration of oaths. Such creditor must also give the administrator the opportunity to redeem the collateral to the bankruptcy estate.

8.2 Are there any preference periods, clawback rights or other preferential creditors' rights (e.g., tax debts, employees' claims) with respect to the security?

The Swedish Bankruptcy Act states that certain transactions can be made subject to clawback, and thus be recovered to a bankruptcy estate. There are several different circumstances that might give rise to such recovery.

There is a general right to clawback addressing *improper transactions* whereby: a creditor has been preferentially treated; the assets of the debtor have been withheld or disposed of to the detriment of the debtor's creditors in general; or whereby the debtor's total indebtedness has been increased. Such transactions can be recovered if the debtor was insolvent, or became insolvent as a result of the transaction, and the benefitting party was aware, or should have been aware, of the debtor's insolvency and the circumstances making the transaction improper. An improper transaction is subject to a five (5)-year hardening period, and a transaction made more than five (5) years prior to the bankruptcy may only be recovered if the transaction was made to a party closely related to the debtor (e.g. a person who has a substantial joint interest with the debtor based on entitlement to a share or financial interest equivalent thereto, or who through a management position has a decisive influence on the business operations conducted by the debtor).

In addition to the general principle of recovery, there are a number of recovery rules addressing specific types of transactions (e.g. gifts, payment of wages, payment of debts, granting of guarantees or granting of security interests). The majority of the specific rules differ from the general recovery rule in that they do not require the debtor to be insolvent or the benefitting party to have any knowledge of the debtor's insolvency. Furthermore, the hardening periods vary depending on the type of transaction and range between three (3) months and three (3) years.

8.3 Are there any entities that are excluded from bankruptcy proceedings and, if so, what is the applicable legislation?

No. All natural persons and legal entities may be subject to bankruptcy proceedings.

8.4 Are there any processes other than court proceedings that are available to a creditor to seize the assets of a company in an enforcement?

Yes. A creditor that has a title of execution (e.g. judgment, an arbitral award or a summary decision under the Summary Proceedings Act) can seek enforcement with the Swedish Enforcement Authority. The procedure is governed by the Enforcement Execution Act. A decision by the Enforcement Authority may be appealed to the district court.

9 Jurisdiction and Waiver of Immunity

9.1 Is a party's submission to a foreign jurisdiction legally binding and enforceable under the laws of your jurisdiction?

Yes. Swedish law permits that parties agree between themselves to have their disputes adjudicated outside Sweden. The parties are free to choose forum. If the agreement is exclusive it will divest the Swedish court of jurisdiction, at least if a foreign court is willing to hear the case. Where one party is a weaker party, e.g. an employee or a consumer, a jurisdiction clause (i.e. an agreement on forum) which limits such party's access to Swedish courts will be disregarded, at least if the submission to foreign jurisdiction leads to the application of a foreign law which is less favourable to the employee or the consumer (than Swedish law).

9.2 Is a party's waiver of sovereign immunity legally binding and enforceable under the laws of your jurisdiction?

Yes. It is, for example, generally accepted under Swedish law that a valid arbitration clause constitutes a waiver of sovereign immunity.

10 Licensing

10.1 What are the licensing and other eligibility requirements in your jurisdiction for lenders to a company in your jurisdiction, if any? Are these licensing and eligibility requirements different for a "foreign" lender (i.e. a lender that is not located in your jurisdiction)? In connection with any such requirements, is a distinction made under the laws of your jurisdiction between a lender that is a bank *versus* a lender that is a non-bank? If there are such requirements in your jurisdiction, what are the consequences for a lender that has not satisfied such requirements but has nonetheless made a loan to a company in your jurisdiction? What are the licensing and other eligibility requirements in your jurisdiction for an agent under a syndicated facility for lenders to a company in your jurisdiction?

Granting of credit to a company (i.e. not to a consumer) does not in itself require a licence or authorisation under Swedish law, but this may be required in case the lender conducts other types of financial activities as well. A Swedish lender might – even if no licence or authorisation is required – be obliged to notify its activities to the Swedish Financial Supervisory Authority pursuant to the Currency Exchange and Other Financial Operations Act (the "**Financial Operations Act**") and may thereby be subject to certain limited supervision, e.g. in the form of ownership assessments. The Financial Operations Act does not apply to non-Swedish entities granting credit to Swedish companies.

There is no specific Swedish regulation applicable to agents or security agents.

11 Other Matters

11.1 Are there any other material considerations which should be taken into account by lenders when participating in financings in your jurisdiction?

The key legal issues to be considered when lending to Swedish entities, and taking security over Swedish assets, have been addressed above.

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Switzerland

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1 Overview

1.1 What are the main trends/significant developments in the lending markets in your jurisdiction?

The Swiss lending market's demand for credit was mainly driven by M&A activities and commodity trading. The negative interest rates introduced by the Swiss National Bank continued to affect the markets as liquidity generally remained high. It also triggered more and more non-bank lenders to become active in the Swiss lending market.

1.2 What are some significant lending transactions that have taken place in your jurisdiction in recent years?

In 2017, one of the biggest lending transactions in Switzerland occurred in relation to the USD 43 billion public tender offer for Syngenta by ChemChina. Other big lenders were Actelion, Orange and Zurich Insurance.

2 Guarantees

2.1 Can a company guarantee borrowings of one or more other members of its corporate group (see below for questions relating to fraudulent transfer/financial assistance)?

Yes, a Swiss company can guarantee borrowings of one or more other members of its corporate group. Guarantees are widely used in secured lending transactions. According to Swiss law, a guarantee is a promise to another person that a third party will perform and that the guarantor will compensate for the damages caused as a result of the third party's failure to perform. There are no specific requirements as to the form of the contract. Once validly concluded, the existence of a guarantee is, in principle, independent from the existence of the obligation guaranteed.

2.2 Are there enforceability or other concerns (such as director liability) if only a disproportionately small (or no) benefit to the guaranteeing/securing company can be shown?

Such concerns exist in certain circumstances.

First of all, a director of a Swiss company must act in the interest of the company. Non-compliance with such duty may lead to director liability. Further, Swiss corporate law does not recognise the overall legal concept of integrated company groups. Consequently, the board of directors of a Swiss group company may not take a consolidated view and fulfil its fiduciary duty merely by considering the overall interests of the entire group. It must rather assess and secure the financial status of the Swiss company on an independent and standalone basis, focusing on the company's distinct identity and status as a legally independent corporate entity.

In case the granting of a guarantee leads to so-called 'financial assistance', guarantees might not be enforceable and directors might become liable. Please refer to section 4 (financial assistance).

2.3 Is lack of corporate power an issue?

Yes, please see the answers to question 2.2 above and section 4 below.

2.4 Are any governmental or other consents or filings, or other formalities (such as shareholder approval), required?

Generally, no. However, in the case of financial assistance, it is customary practice in Switzerland to require formal approval of upstream or cross-stream guarantees (which potentially qualify as constructive dividends) not only by the board of directors, but also by the shareholders of the Swiss guarantor. Please see the answers in section 4.

2.5 Are net worth, solvency or similar limitations imposed on the amount of a guarantee?

This is the case for financial assistance. Please see the answers in section 4. An upstream guarantee may not be given in an amount exceeding the guarantor's so-called 'free equity'.

2.6 Are there any exchange control or similar obstacles to enforcement of a guarantee?

No, there are not.

3 Collateral Security

3.1 What types of collateral are available to secure lending obligations?

The most common types of collateral in Switzerland are security in the form of a pledge or a transfer of ownership (for security purposes) of real estate, tangible moveable property, financial instruments, claims and receivables, cash and intellectual property.

3.2 Is it possible to give asset security by means of a general security agreement or is an agreement required in relation to each type of asset? Briefly, what is the procedure?

Different types of security can theoretically be contained in a single general security document. In practice, each type of security is usually documented in a separate agreement, particularly if a specific security must be documented in a public deed.

3.3 Can collateral security be taken over real property (land), plant, machinery and equipment? Briefly, what is the procedure?

Yes, collateral security can be taken over real property.

The definition of real estate under Swiss law includes: edified and unedified land (that is, land with or without buildings); a flat or floor of a building; and the right to build on a track of land for a limited period of time (*Baurecht*).

The following forms of security are commonly granted over immoveable property:

Mortgage assignment (*Grundpfandverschreibung*). This is to secure any kind of debt, whether actual, future, or contingent. The creditor of a claim secured by a mortgage assignment can demand an extract from the land register.

Mortgage certificate (*Schuldbrief*). A mortgage certificate establishes a personal claim against the debtor and is secured by a property lien. The mortgage certificate constitutes a negotiable security, which can be pledged or transferred for security purposes and is issued either in bearer form, in registered form or as a paperless version. An outright transfer has certain advantages in case of the security provider's bankruptcy and in multi-party transactions. Therefore, practitioners in cross-border banking transactions often prefer granting an outright transfer of a mortgage certificate instead of a pledge.

In both forms of security, the secured party's claims can be backed by property belonging to the borrower or a third party (third party security), subject to the rules on financial assistance and similar limitations (see question 2.2 above).

Mortgage assignments and mortgage certificates are created and perfected by the parties entering into an agreement regarding the creation of the security and finalised by means of a notarised deed and an entry into the land register.

3.4 Can collateral security be taken over receivables? Briefly, what is the procedure? Are debtors required to be notified of the security?

Yes, collateral security can be taken over receivables and rights under contracts in general. Common types of claims and receivables over which security is granted are: rights under contracts in general (existing and future); trade account receivables (existing and future); and balances in bank accounts.

Claims and receivables can be pledged or assigned for security purposes. The granting of security is based on the same principles as for security over moveable property (see question 3.7) and, in particular, requires a valid agreement between the security provider and the security holder.

The security agreement must be in writing. There is no transfer of possession. In addition, an assignment of receivables or other claims requires that the assignor sign the assignment itself and not just the related undertaking in the assignment agreement. Perfection of a first-ranking security also requires that the claims or receivables be assignable under the governing law of those claims or receivables.

If a Swiss bank account (that is, the balance of the account standing to the credit of the security provider) is used as collateral, the Swiss bank's business terms usually provide that the bank has a first-ranking security interest over its client's account. A third party therefore only gets a second-ranking security interest over a Swiss bank account, unless the bank waives its priority rights. To create and perfect a second-ranking security interest, the bank must be given notice.

In the case of assignments, the third party debtors of the receivables are either: immediately notified of the assignment (open assignment (*offene Zession*)); or notified only in case of default of the assignor or other events of default (equitable assignment (*Stille Zession*)).

On notification, the assignee, as the new creditor of the assigned claims, can directly collect the receivables from the third party debtors. Because Swiss law also allows the assignment of future receivables arising before a potential bankruptcy of the assignor, assignments are commonly used in practice. If all of the present and future trade receivables are taken as security, notice of the creation of the security interest is usually only given to the relevant debtor if there is a default. Until this notification, a *bona fide* debtor can validly discharge its obligation to the security provider.

3.5 Can collateral security be taken over cash deposited in bank accounts? Briefly, what is the procedure?

Yes. See question 3.4 above.

3.6 Can collateral security be taken over shares in companies incorporated in your jurisdiction? Are the shares in certificated form? Can such security validly be granted under a New York or English law governed document? Briefly, what is the procedure?

Yes, collateral security can be taken over shares in companies incorporated in Switzerland. Shares can be in bearer, registered or dematerialised form. The perfection formalities depend on the form of the shares. Security can be validly granted under a New York or English law-governed document. This is, however, not recommended due to conflict of law issues.

Shares can be pledged, transferred outright and/or assigned for security purposes.

Creation of a security is always based on a valid security agreement. Perfection of a security, however, differs according to the type of shares: certificated shares require possession of the certificates to be transferred to the security holder. Additionally, registered certificates must be duly endorsed and transferred to the security holder. Uncertificated financial instruments must be pledged, transferred or assigned in writing. Since 1 January 2010, the Federal Intermediated

Securities Act has set out new rules in relation to intermediated securities (including the granting of security over intermediated securities).

A security over intermediated securities can be granted in one of the following ways: (i) by transferring the intermediated securities to the securities account of the secured party. This requires the security provider to give instructions to the bank to effect the transfer; and (ii) by crediting the intermediated securities to the securities account of the secured party. Alternatively, they can be granted by an irrevocable agreement (a so-called control agreement) between a security provider and its intermediary that the intermediary will comply with any instructions from the secured party. The security provider can, through the control agreement, grant a security right in specified intermediated securities, all intermediated securities in a securities account or a certain quota of intermediated securities in a securities account, determined by value.

3.7 Can security be taken over inventory? Briefly, what is the procedure?

Inventory is a form of tangible moveable property. Tangible moveable property comprises all property that is not classified as immoveable. Security over tangible property is commonly granted in the form of a pledge or an outright transfer.

The pledge is the most widely used type of security. A pledge entitles the lender to liquidate the pledged property if the debtor defaults, and to apply the proceeds in repayment of the secured claims.

In case of an outright transfer, the transferee acquires full title in the transferred assets, but can, under the terms of the transfer agreement, only use its title to liquidate the assets on the debtor's default to apply the proceeds to the repayment of debt. Although the transfer has certain advantages over a pledge on the bankruptcy of a Swiss security provider and in multi-party transactions, its use is restricted by increased liability concerns.

Perfection of a pledge or an outright transfer requires both: a valid security agreement; and the secured party to obtain physical possession of the relevant assets. The security holder does not have a security interest over the collateral as long as the security provider retains possession and control over it (certain moveable property, such as aircraft or ships, is not subject to this principle).

Certain moveable assets are subject to particular rules. The most important are aircraft, ships and railroads where the security is perfected by the entry of the security in the respective register. In addition, the Federal Intermediated Securities Act sets out specific provisions for the granting of a security over intermediated securities.

Swiss law generally does not recognise the concept of a floating charge or floating lien. Therefore, taking a security over inventory, machinery or equipment (often used as collateral in other jurisdictions) is not practical under Swiss law, at least in relation to assets necessary for running the pledgor's business. The requirement of physical control over the relevant assets is generally too burdensome, costly and unmanageable.

3.8 Can a company grant a security interest in order to secure its obligations (i) as a borrower under a credit facility, and (ii) as a guarantor of the obligations of other borrowers and/or guarantors of obligations under a credit facility (see below for questions relating to the giving of guarantees and financial assistance)?

There are no particular company law rules on a Swiss company granting collateral to secure debt used to purchase its own shares or the shares of a parent company or of a subsidiary. The company itself must not purchase more than 10% of its own voting shares.

The granting of security by a Swiss company to secure debt used to purchase its own shares can result in Swiss income tax being levied on the party selling the shares. In addition, the restrictions under corporate benefit rules (see section 4) apply to the granting of any upstream security (for the benefit of a direct or indirect parent company) and/or any cross-stream security (for the benefit of another group company not fully owned by the party providing the security). This is irrespective of the purpose of the secured obligations.

3.9 What are the notarisation, registration, stamp duty and other fees (whether related to property value or otherwise) in relation to security over different types of assets?

The granting or enforcement of a guarantee or security does not in itself trigger any Swiss taxes. However, certain transactions may be subject to Swiss tax.

If loans are secured over real estate, the following fees may be payable depending on the transaction: notaries' fees; registration fees (land register); and cantonal and communal stamp duties. The rates depend on the security's face value and the location of the real estate. The rates for fees vary widely from canton to canton.

3.10 Do the filing, notification or registration requirements in relation to security over different types of assets involve a significant amount of time or expense?

Generally, filing, notification or registration of security interests is done within a couple of days. However, in case of a mortgage over real estate, the notarisation and, in particular, the entry into the land registry might take some time. Similarly, in case of registration of a pledge over intellectual property rights, such registration might take some time.

3.11 Are any regulatory or similar consents required with respect to the creation of security?

Generally, there are no regulatory consents required with respect to the creation of security. In case of a regulated entity granting security over certain of its assets, consents might be required.

3.12 If the borrowings to be secured are under a revolving credit facility, are there any special priority or other concerns?

No, there are not.

3.13 Are there particular documentary or execution requirements (notarisation, execution under power of attorney, counterparts, deeds)?

In case of a mortgage, the mortgage agreement needs to be notarised.

4 Financial Assistance

4.1 Are there prohibitions or restrictions on the ability of a company to guarantee and/or give security to support borrowings incurred to finance or refinance the direct or indirect acquisition of: (a) shares of the company; (b) shares of any company which directly or indirectly owns shares in the company; or (c) shares in a sister subsidiary?

Yes, there are general limitations as to such upstream or cross-stream guarantees or security. The respective limitations apply in relation to guarantees or a security interest that guarantees or secures the finance or refinance of an acquisition of the shares of the company or shares of any company which directly or indirectly owns shares in the company or shares in a sister subsidiary.

Under Swiss law, it is market practice to deal with financial assistance as follows:

So-called upstream or cross-stream guarantees, i.e., guarantees granted to parent or affiliated companies (other than its direct and/or indirect subsidiaries), must generally meet arm's length conditions, as they would be requested by an unrelated third party, such as a bank, when granting the same guarantee. This means, generally, that: (a) the Swiss guarantor should carefully consider the third party's creditworthiness, as well as its willingness and ability to fulfil its obligations that shall be guaranteed; (b) the upstream guarantee should have customary terms of duration, termination and amortisation; (c) the upstream guarantee should provide for adequate interest to be paid regularly (and not just accrued); and (d) the upstream guarantee should be adequately secured (e.g., by the borrower providing a pledge or another form of security).

Non-compliance may notably lead to the invalidity of an upstream guarantee, as well as to directors' and officers' personal liability. Further, non-compliance may have adverse tax implications and may even, under certain conditions, qualify as a criminal offence (e.g., creditor preference or disloyal management) or as a fraudulent conveyance under the applicable provisions of Swiss bankruptcy law.

The following issues should be considered when granting a guarantee:

Corporate purpose: As a general rule, a commitment entered into on behalf of a Swiss company is binding on the company, to the extent it falls within the company's corporate purpose as set forth in the articles of incorporation. If that is not the case, the commitment in question could be deemed *ultra vires* (i.e., beyond the scope of its powers) and thus null and void from the outset. The fulfilment of this prerequisite is often questionable for upstream guarantees which are not entirely on arm's length terms. In case of doubt, it is advisable for the Swiss guarantor to amend its articles of incorporation by extending the article on corporate purpose to provide explicitly for the granting of financial assistance to group companies, including through upstream guarantees. In addition, it may be advisable to insert in the articles of incorporation a clear reference to the fact that the Swiss guarantor is part of a particular group of companies.

Adequate risk diversification: As a general rule, the board of directors of a Swiss company must adhere to the principle of adequate risk diversification. When granting an upstream guarantee, the board of directors must thus avoid an undue risk concentration by a substantial portion of the company's balance sheet assets consisting of such a guarantee to the benefit of a third party.

Guarantor's free equity: Unless it clearly meets the arm's length test, an upstream guarantee may not be given in an amount exceeding the guarantor's so-called 'free equity'. Free equity corresponds to the amount of the guarantor's total equity (as shown in the statutory balance sheet), minus 150% (or, in the case of a holding company, 120%) of the nominal issued share capital, minus any remaining special reserves which are not available for dividend distributions, such as any special paid-in surplus reserve.

An upstream guarantee exceeding the free equity threshold could be deemed to be an unlawful return of the shareholder's capital contributions and to violate the statutory limitations on the use of the company's legal reserves. As a consequence, such upstream guarantee could be challenged by any party as being null and void from the outset. This is particularly true where the guarantee was fictitious or where it was clear from the beginning that the borrower would not be in a position to fulfil its obligations when due.

Constructive dividend: Under Swiss corporate law, shareholders and related parties are obliged to return any benefits they receive from a Swiss company if those benefits are clearly disproportionate to the consideration received by the company, as well as to its financial status. An upstream guarantee which does not clearly have arm's length terms could be deemed as a constructive dividend. As a consequence, the board of directors of the guarantor would be forced to demand immediate repayment of the guarantee irrespective of its term. Characterisation as a constructive dividend would also lead to adverse tax consequences.

In this context, it has become customary to require formal approval of upstream guarantees (which potentially qualify as constructive dividends) not only by the board of directors, but also by the shareholders of the Swiss guarantor. However, this formal step as such does not necessarily prevent the upstream guarantee from being deemed as a constructive dividend.

Directors' and officers' duty of care: In general, the directors and the senior management of a Swiss company may become personally liable to the company, as well as to its shareholders and creditors, for any damage caused by an intentional or negligent violation of their duties. Such liability may also be incurred by the Swiss company's parent (and its corporate bodies) if the latter is deemed to be a *de facto* corporate body of the Swiss company. In addition, according to the Swiss Withholding Tax Act, directors and officers may become personally as well as jointly and severally liable for unpaid withholding tax obligations of a Swiss company which is liquidated or becomes bankrupt. This liability is stricter than the general directors' and officers' liability insofar as the officers and directors, in order to avoid liability, must prove that they have done everything which could reasonably be expected from them to ascertain and fulfil the company's payable taxes.

Withholding and income tax implications: Ordinary, as well as hidden, profit distributions by resident companies are subject to Swiss withholding tax (currently at 35%) at source. Subject to certain conditions and upon request, the tax may be fully or partially refunded to the recipient of the profit distribution. For non-Swiss recipients, a refund may only be granted based on a double tax treaty between Switzerland and the country of residence of the recipient. Further, profit distributions are not income tax deductible – they are added back to the taxable profit of the distributing company and thus become subject to corporate income tax. From a tax standpoint, a constructive dividend is always assumed when a company executes non-arm's length transactions with related parties. This is also the case with regard to upstream guarantees.

5 Syndicated Lending/Agency/Trustee/Transfers

5.1 Will your jurisdiction recognise the role of an agent or trustee and allow the agent or trustee (rather than each lender acting separately) to enforce the loan documentation and collateral security and to apply the proceeds from the collateral to the claims of all the lenders?

In Switzerland, the agent concept is recognised and frequently used for syndicated facilities and agency arrangements governed by Swiss or foreign law.

As for trustees, a substantive trust law does not exist in Switzerland. Therefore, it is not possible to set up a trust under Swiss law. Since July 2007, the Hague Convention on the Law Applicable to Trusts and on their Recognition 1985 (Hague Trust Convention) is applicable in Switzerland. Certain provisions of the Swiss Private International Law Act (PILA) transpose the Hague Trust Convention into national law. These provisions essentially allow recognition of foreign trusts (as defined in the Hague Trust Convention) in Switzerland. The relevant PILA provisions grant a settlor unfettered freedom to choose the law applicable to the trust. The trust can also contain a choice of jurisdiction, which must be evidenced in writing or in any equivalent form. A Swiss court cannot decline jurisdiction if either a party, the trust or a trustee has their domicile, place of habitual residence or a place of business in the canton of that court or a major part of the trust assets is located in Switzerland.

A decision by a foreign court on trust-related matters is recognised in Switzerland if it is made in any one of the following cases: (i) by a validly selected court; (ii) in the jurisdiction in which the defendant has its domicile, habitual residence or establishment; (iii) in the jurisdiction where the trust has its seat; and (iv) in the jurisdiction whose laws govern the trust. The decision is recognised in the country where the trust has its seat, provided the defendant was not domiciled in Switzerland.

Generally, a security trustee can enforce its rights; however, this depends on the nature of the security:

Pledge: Swiss law is based on the doctrine of accessory (*Akzessorietätsprinzip*), meaning that the secured party must be identical to the creditor of the secured claim. A pledge cannot be vested in a third party acting as a security holder in its own name and right; instead, the pledge must be granted to the lender or, in the case of syndicated loans, all of the lenders as a group. The lender(s) can, however, be represented by a third party acting in the name and on behalf of the lender(s).

Security transfer or security assignment: The doctrine of accessory (see above) does not apply. For this type of security, therefore, a security trustee can enter into the security agreement and hold the security in its own name and on its own account for the lender(s).

Intermediated securities: It is not clear yet whether the doctrine of accessory applies under the Federal Intermediated Securities Act. It is probable that it will not apply where securities are transferred to the secured party's account, but it may apply where a control agreement is entered into.

5.2 If an agent or trustee is not recognised in your jurisdiction, is an alternative mechanism available to achieve the effect referred to above which would allow one party to enforce claims on behalf of all the lenders so that individual lenders do not need to enforce their security separately?

The agent and/or the trust concept is recognised in Switzerland.

5.3 Assume a loan is made to a company organised under the laws of your jurisdiction and guaranteed by a guarantor organised under the laws of your jurisdiction. If such loan is transferred by Lender A to Lender B, are there any special requirements necessary to make the loan and guarantee enforceable by Lender B?

A transfer from Lender A to Lender B is only possible if such transfer is not prohibited under the guarantee. Legally, such transfer will be effected by an assignment.

6 Withholding, Stamp and Other Taxes; Notarial and Other Costs

6.1 Are there any requirements to deduct or withhold tax from (a) interest payable on loans made to domestic or foreign lenders, or (b) the proceeds of a claim under a guarantee or the proceeds of enforcing security?

The granting of security upstream or cross-stream on terms other than arm's length may trigger a 35% dividend withholding tax which must be deducted from the gross payment made.

Dividend withholding tax is fully recoverable if the recipient is a Swiss-resident entity. Non-resident companies with a permanent establishment in Switzerland can claim a full refund, if the relevant asset is attributable to the Swiss permanent establishment. Non-resident companies can claim a full or partial refund of the dividend withholding tax, based on an applicable double tax treaty between their country of residence and Switzerland. If no double tax treaty applies, the dividend withholding tax may become a final burden for the recipient (subject to any measures required in the country of residence of the recipient).

The Swiss Confederation and the cantons or communes levy an interest withholding tax on interest which is secured by a mortgage on Swiss real estate. The combined rate of the tax varies between 13 and 33%, depending on which canton the real estate is located in. This interest withholding tax is reduced to zero under many double tax treaties, including the ones with the US, the UK, Luxembourg, Germany and France.

Further, the transfer of ownership of a bond, note or other securities to secure a claim may be subject to securities transfer stamp tax of up to 0.3%, calculated on the transaction value, if a Swiss bank or other securities dealer as defined in the Swiss stamp tax law is involved as a party or intermediary. The tax is paid by the securities dealer and may be charged to parties who are not securities dealers. If no securities dealer is involved, no transfer stamp tax will arise.

In addition to this stamp tax, the sale of bonds or notes by or through a member of the SIX Swiss Exchange may be subject to a minor SIX Swiss Exchange levy on the sale proceeds.

The sale of goods for consideration in the course of a business is generally subject to VAT. The standard tax rate is currently 8%. Most banking transactions, including interest payments and transactions regarding the granting of security, are exempt from VAT. However, corresponding input taxes on related expenses are not recoverable.

VAT on the sale of real estate is only chargeable if the seller opts for tax. The option is permissible for buildings (but not for land) unless the new owner uses the buildings only for private purposes.

6.2 What tax incentives or other incentives are provided preferentially to foreign lenders? What taxes apply to foreign lenders with respect to their loans, mortgages or other security documents, either for the purposes of effectiveness or registration?

There are no specific incentives of such types and no specific taxes that apply to foreign lenders.

6.3 Will any income of a foreign lender become taxable in your jurisdiction solely because of a loan to or guarantee and/or grant of security from a company in your jurisdiction?

Generally, the granting or taking of security between related parties must be at arm's length. This may mean that a security commission or guarantee fee is payable to the security provider. This commission or fee can be subject to income tax for a Swiss security provider as part of his overall earnings. The transfer of ownership of an asset to secure a loan may trigger corporate income taxes on the net income as part of the overall earnings of a Swiss security provider. Income tax rates depend, among other things, on the place of incorporation or residence of a person, entity or permanent establishment.

6.4 Will there be any other significant costs which would be incurred by foreign lenders in the grant of such loan/guarantee/security, such as notarial fees, etc.?

Please see question 3.9.

6.5 Are there any adverse consequences to a company that is a borrower (such as under thin capitalisation principles) if some or all of the lenders are organised under the laws of a jurisdiction other than your own? Please disregard withholding tax concerns for purposes of this question.

No, there are not.

7 Judicial Enforcement

7.1 Will the courts in your jurisdiction recognise a governing law in a contract that is the law of another jurisdiction (a "foreign governing law")? Will courts in your jurisdiction enforce a contract that has a foreign governing law?

Yes. Subject to certain reservations, courts in Switzerland will generally recognise a governing law clause in a contract and will generally enforce a contract that has a foreign law governed contract.

The rules relating to conflicts of law applicable in Swiss courts are set out in the PILA. Generally, a contract is governed by the law chosen by the parties. The choice of law must be expressly and clearly evident from the terms of the contract or the circumstances.

These rules apply to different forms of security in the following ways:

Acquisitions or losses of rights *in rem* in moveable goods. These are governed by the *lex rei sitae*, that is, the law of the country of the asset's location at the time of the event giving rise to that acquisition or loss. The PILA allows the parties to subject the acquisition and loss of those rights to the law governing the underlying legal transaction (see above). However, that choice of law cannot be invoked against third parties who can rely on the *lex rei sitae*.

Outright transfers of a claim and/or of uncertificated securities are effected by way of security. These assignments are subject to the law (PILA) chosen by the parties or governing the claim, in the absence of a choice. However, that choice of law cannot be invoked against the debtor of the claim and the issuer of uncertificated securities without the debtor's prior consent.

Pledges of securities and debts. If the parties have not chosen the applicable law, the pledge of securities and debts is not governed by the *lex rei sitae* but by the law of the pledgee's domicile. (However, if the parties make a choice of law, it cannot be invoked against third parties (see above).) Irrespective of the law applicable between the parties, the only law which can be invoked against the issuer of a security or the debtor of a claim is the law governing the pledged security or right.

Specific rules apply to intermediated securities. The law applicable to dispositions over intermediated securities, as well as further rights to such intermediated securities, is the law chosen by the parties to the relevant account agreement (Hague Convention on Intermediated Securities). However, this law can only apply if the relevant intermediary has an office (as described in the Hague Convention on Intermediated Securities) in that jurisdiction at the time the agreement is entered into. Otherwise, the applicable law is the law of the jurisdiction in which the intermediary's office, with which the relevant account agreement was entered into, is located.

7.2 Will the courts in your jurisdiction recognise and enforce a judgment given against a company in New York courts or English courts (a "foreign judgment") without re-examination of the merits of the case?

A final judgment obtained in New York or English courts is amenable to recognition and enforcement in the courts of Switzerland according to (i) the Convention on Jurisdiction and Enforcement of Judgments in Civil and Commercial Matters dated 30 October 2007, (ii) such other international treaties under which Switzerland is bound, or (iii) PILA, provided that the prerequisites of the Lugano Convention, such other international treaties or the PILA, as the case may be, are met.

7.3 Assuming a company is in payment default under a loan agreement or a guarantee agreement and has no legal defence to payment, approximately how long would it take for a foreign lender to (a) assuming the answer to question 7.1 is yes, file a suit against the company in a court in your jurisdiction, obtain a judgment, and enforce the judgment against the assets of the company, and (b) assuming the answer to question 7.2 is yes, enforce a foreign judgment in a court in your jurisdiction against the assets of the company?

In case the guarantor is in possession of a so-called '*Rechtsöffnungstitel*', i.e. if the debtor recognised in a written document that it owes the amount to the guarantor, the guarantor's rights might get enforced in summary proceedings which may take two to three months. In the more likely case that no such '*Rechtsöffnungstitel*' is available, the guarantor will have to go through normal court proceedings. A judgment might be rendered within one year (first instance).

The latter is true also in case (b) if a foreign judgment needs to be enforced.

7.4 With respect to enforcing collateral security, are there any significant restrictions which may impact the timing and value of enforcement, such as (a) a requirement for a public auction, or (b) regulatory consents?

Under Swiss law, it is possible that in the security agreement the parties mutually agree that a pledgee take over the pledge in case of enforcement ('*Selbsteintritt*') and/or that the pledgee is entitled to sell the pledge ('*Privatverwertung*'). In case there is no such agreement and/or in case of formal bankruptcy proceedings, the enforcement of collateral will take place by public auction in accordance with the Swiss procedural rules. The Swiss bankruptcy law foresees several different time lines depending on the type of collateral (moveables, real estate, etc.).

7.5 Do restrictions apply to foreign lenders in the event of (a) filing suit against a company in your jurisdiction, or (b) foreclosure on collateral security?

No, they do not.

7.6 Do the bankruptcy, reorganisation or similar laws in your jurisdiction provide for any kind of moratorium on enforcement of lender claims? If so, does the moratorium apply to the enforcement of collateral security?

Generally, in the case of bankruptcy, pledged assets form part of the bankrupt estate. As a result, the private enforcement of pledged assets is no longer permitted and enforcement can only occur according to the Debt Enforcement Act. Intermediated securities traded on a representative market are not subject to this restriction, and private enforcement remains possible.

The pledgee's priority rights remain effective, and the proceeds from the sale of the pledged assets in the bankruptcy proceedings are first used to cover the claims secured by the pledge. If the proceeds from the sale of the pledged assets exceed those secured claims, the surplus is available for distribution to other creditors.

All claims against the bankrupt company become due at the time the bankruptcy is declared and the enforcement of all claims occurs in accordance with the procedures prescribed by the Debt Enforcement Act.

As to moratorium, Swiss law provides for company rescue procedures (*Nachlassverfahren*) in the Debt Enforcement Act. The rescue proceedings can be started by the company or in certain circumstances by a company's creditor. In those proceedings, the competent court can grant a moratorium (*Nachlassstundung*). A moratorium may, if certain conditions are fulfilled, lead to a composition agreement (*Nachlassvertrag*) that is binding on all creditors and affects the creditors' unsecured claims. For a composition agreement to be effective, it must be approved by at least a majority of the creditors holding two-thirds of all the debts or a quarter of the creditors holding three-quarters of the debt, and the competent bankruptcy court.

If a moratorium is granted by the competent court, the security granted by the company is not directly affected. However, as a rule, enforcement proceedings for the security cannot be started or continued as long as the moratorium is in effect. Private enforcement (see question 8.4) should still be possible and not be affected by a moratorium. If the rescue proceedings result in a composition agreement, the security granted by the company will not be affected by this. A composition agreement does not affect security granted by the company.

7.7 Will the courts in your jurisdiction recognise and enforce an arbitral award given against the company without re-examination of the merits?

An arbitration award rendered against a Swiss company in an arbitration proceeding is generally enforceable in Switzerland according and subject to the New York Convention of 10 June 1985 on the recognition and enforcement of foreign arbitral awards.

8 Bankruptcy Proceedings

8.1 How does a bankruptcy proceeding in respect of a company affect the ability of a lender to enforce its rights as a secured party over the collateral security?

All claims against the bankrupt company – as well as claims resulting from a guarantee – become due at the time the bankruptcy is declared and the enforcement of all claims occurs in accordance with the procedures prescribed by the Debt Enforcement Act.

8.2 Are there any preference periods, clawback rights or other preferential creditors' rights (e.g., tax debts, employees' claims) with respect to the security?

The Debt Enforcement Act provides, in connection with bankruptcy and composition of a security provider, that a transaction is voidable if any of the following apply:

The security provider or the guarantor disposes of assets for free or for inadequate consideration (not at arm's length) in the year before the adjudication of bankruptcy or an equivalent event.

The security provider repays debts before they become due, settles a debt by an unusual means of payment or grants collateral for previously unsecured liabilities, which the security provider was not obliged to secure, in the year before the adjudication of bankruptcy or an equivalent event, provided that both the security provider was overindebted (i.e., its liabilities exceeded its assets) at that time and the secured party was aware of the overindebtedness of the security provider. A *bona fide* secured party is therefore protected. However, the law presumes the secured party's knowledge of the security provider's overindebtedness, so the secured party bears the burden of proof in relation to his good faith.

The granting of security by the security provider (or the granting of the guarantee) occurred in the five years before the adjudication of bankruptcy proceedings or an equivalent event, provided that the security provider intended to disadvantage or favour certain creditors or should reasonably have foreseen that result and the security provider's intent was, or must have been, apparent to the secured party.

8.3 Are there any entities that are excluded from bankruptcy proceedings and, if so, what is the applicable legislation?

Under Swiss law, it is not possible to start debt enforcement proceedings against Swiss municipalities ('*Gemeinden*') with the aim of inducing bankruptcy. In accordance with the applicable ordinance on debt enforcement, only enforcement proceedings on the enforcement of collateral are possible against Swiss municipalities.

8.4 Are there any processes other than court proceedings that are available to a creditor to seize the assets of a company in an enforcement?

The conditions under which security (including guarantees) can be enforced are determined by general principles of law, as well as by the specific provisions of the security agreement. This applies to loans, guarantees, pledged assets and assets transferred by way of security. For a secured party to be permitted to enforce security, the secured party must have a secured claim, and this claim must be due. The relevant security agreement may set out additional conditions for the enforcement of the security. Usually, security agreements refer to the occurrence of an event of default, as specified in the credit agreement governing the secured loan, as a condition for enforcing the security.

Guarantees under Swiss law are basically independent from the underlying claim. Therefore, it is not a requirement for the enforcement of a guarantee that an underlying claim must exist or be due (in contrast to pledges). It is sufficient that the conditions for enforcement set out in the guarantee are fulfilled. However, depending on the circumstances, the enforcement of a guarantee where there is no underlying claim may constitute an abuse of rights, which is not protected under Swiss law.

In the case of pledged assets, there are two main forms of enforcement, namely by way of a private enforcement and under the rules of the Debt Enforcement Act. Private enforcement is generally only permitted where the parties have agreed to this in advance, for example, in the security agreement. Private enforcement is possible in relation to all forms of assets, but in practice mainly occurs in connection with moveable assets. Private enforcement can take place by a private sale or a public auction or, in relation to assets, the value of which can be objectively determined (for example, listed securities), the pledgee itself purchasing the pledged assets, and applying the proceeds to its claims (*Selbsteintritt*). For securities over intermediated securities, as a matter of law, private enforcement does not need to have been agreed between the parties but is only permitted in respect of intermediated securities that are traded on a representative market. Pledges over intermediated securities can also be enforced privately on the bankruptcy of the security provider. This is in contrast to pledges over any other assets.

In all forms of private enforcement the pledgee must protect the interests of the pledgor and, in particular, must obtain the best price possible in the sale of the pledged assets, fully document the enforcement and provide the documentation to the pledgor and return any surplus remaining after the application of the proceeds to the secured debt to the pledgor.

9 Jurisdiction and Waiver of Immunity

9.1 Is a party's submission to a foreign jurisdiction legally binding and enforceable under the laws of your jurisdiction?

Basically, yes.

9.2 Is a party's waiver of sovereign immunity legally binding and enforceable under the laws of your jurisdiction?

A sovereign entity is either acting with its so-called administrative assets or with its financial assets. The administrative assets are the assets that directly serve the administrative tasks of an administration. The financial assets do not directly serve such purpose. If a sovereign entity is entering into agreements concerning its financial assets, it may validly waive sovereign immunity because in such cases the sovereign entity is acting as a normal third party. In the case of administrative assets, a sovereign entity may also waive sovereign immunity; however, in extreme cases (e.g. public policy issues) such waiver might be doubtful.

10 Licensing

10.1 What are the licensing and other eligibility requirements in your jurisdiction for lenders to a company in your jurisdiction, if any? Are these licensing and eligibility requirements different for a "foreign" lender (i.e. a lender that is not located in your jurisdiction)? In connection with any such requirements, is a distinction made under the laws of your jurisdiction between a lender that is a bank *versus* a lender that is a non-bank? If there are such requirements in your jurisdiction, what are the consequences for a lender that has not satisfied such requirements but has nonetheless made a loan to a company in your jurisdiction? What are the licensing and other eligibility requirements in your jurisdiction for an agent under a syndicated facility for lenders to a company in your jurisdiction?

No, there are no licensing or eligibility requirements in Switzerland for a lender to a company. Any person can lend to a third party. Lending is not an activity that requires a licence. However, given that lending is typically an activity done by a bank, it is noteworthy that the banking business does require a licence, even if not the lending activity. A bank that is not domiciled in Switzerland and does not have any physical presence in Switzerland is entitled to do banking activities on a cross-border basis into Switzerland, which includes the lending business. Note that Swiss law will change and such cross-border exemptions will no longer be possible without a licence. The change in law is expected to occur in 2017/2018.

11 Other Matters

11.1 Are there any other material considerations which should be taken into account by lenders when participating in financings in your jurisdiction?

No, there are not.

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Chapter 75

Taiwan

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1 Overview

1.1 What are the main trends/significant developments in the lending markets in your jurisdiction?

Given that the global economy is recovering steadily, Taiwanese enterprises seemed more optimistic in 2017 than in 2016. The total loan amount in 2017 increased by around 1,000 billion New Taiwan dollars compared to the total loan amount in 2016. However, since the interest rate is still low, right now many Taiwanese companies look for loan funding from individual banks, commercial paper and bond offerings instead of syndication loans, which has made the syndication loan market relatively inactive in 2017. The size of syndication loan transactions are also small.

Regarding loan by industry, for private enterprises, manufacturing, wholesale and retail trade and real estate are the top three industries which have the most loans outstanding in 2017 and this trend should remain the same in 2018. Further, in order to stimulate economic growth and drive industrial transformation, the Taiwanese government approved the Special Act for Forward-Looking Infrastructure in July 2017. The Forward-Looking Infrastructure Development Program (2017–2024) will expand investments in major infrastructure (including railways, aquatic environments, green energy, digital technology, and urban and rural facilities). The government investment in this large-scale infrastructure programme will total NT$882.49 billion (US$28.56 billion), and is expected to spur public and private enterprise investment of NT$1.78 trillion (US$57.53 billion). Among the infrastructure projects, green energy is being invested in the most, especially wind-powered energy plans. The Ministry of Economic Affairs (“MOEA”) has formulated a Four-year Wind Power Promotion Plan for 2017 to 2020. The plan contains short-term goals to solidify industry foundations and increase installed wind power capacity to 1.334 GW within four years, as well as medium and long-term measures to improve the installation environment and increase total installed capacity to 4.2 GW (1.2 GW land-based, 3 GW offshore) by 2025.

Due to such green energy policy, the Financial Supervisory Commission (“FSC”) has positioned green finance as one of the most important policies and encouraged domestic funds to invest in the green energy industry. The implemented measures of green finance include: (1) assisting the green energy industry in obtaining financing; (2) guiding insurance industry capital to be channelled into investment in domestic public construction, including the green energy industry; (3) providing diverse channels for fund raising and obtaining financing; and (4) enhancing green finance talent nurturing. The FSC has also publicly pledged to support facilitating private sector investments in offshore wind farms.

Based on such policy-oriented support and assistance, several significant syndicated loan cases in relation to investments in offshore wind farms have taken place or are currently under discussion. For example, it was reported that Dong Energy (whose company name was changed to Ørsted in October 2017), with its joint venture partner Macquarie Capital, plans to seek syndicated financing, of about NTD60 million, from local banks in relation to its offshore wind sites in the Changhua area.

1.2 What are some significant lending transactions that have taken place in your jurisdiction in recent years?

(1) On January 24, 2017, Taiwan High Speed Rail Corporation (“THSR”) signed a joint underwriting agreement with an underwriting syndicate comprising 10 financial institutions, including the arranger, The International Bills Finance Corporation. Within the two-year period, THSR may issue an unsecured commercial paper with a maturity period ranging from 90 days to one year. The total amount of the revolving underwriting facility is NT$20 billion (US$666.67 million).

(2) On March 27, 2017, General Energy Solutions Inc. (“GES”) secured a three-year NT$800 million (US$26.67 million) revolving syndicated loan led by Yuanta Commercial Bank as the facility agent. The loan is to be used for development and construction of GES’s global solar system project. The syndicated loan shows that the Taiwan banking industry foresees the downstream solar industry with a promising future.

(3) On July 12, 2017, Swancor Holding Co. Ltd. (“Swancor”), a resin manufacturer and wind farm developer, secured a NT$1.72 billion (US$57.33 million) syndicated loan from eight domestic banks led by First Commercial Bank, to refinance its debt and bolster its operating capital. According to Swancor, its offshore wind farm in Miaoli County is expected to deliver 128MW when fully commissioned by the end of 2019. Swancor’s wind power subsidiary, Formosa I Wind Power Co., in April 2017 obtained a commercial operating licence for a wind farm from the Ministry of Economic Affairs.

(4) On July 17, 2017, AU Optronics Corp. (“AUO”) secured a total of NT$23 billion (US$766.67 million) five-year facility from a banking consortium led by Bank of Taiwan. According to local news release, AUO originally planned to raise only NT$20 billion through the new financing project, but increased the amount to NT$23 billion due to enthusiastic participation of local and foreign banks. AUO will use the new funds to finance the second-phase expansion project of

its 8.5 GW plant in Houli, central Taiwan. The company aims to ramp up the production capacity at the plant to 100,000 panels a month when the new facilities come online in the second half of 2018.

(5) On August 23, 2017, Yieh United Steel Corporation ("YUSC"), focusing on production and sales of stainless steel products in Southeast Asia, entered into a five-year NT$12.65 billion (US$421.67 million) syndicated loan agreement with Mega International Commercial Bank as the facility agent. It was reported that YUSC was initially targeting NT$11 billion, while such fundraising attracted more than NT$15.6 billion from other local banks.

(6) On October 30, 2017, Grand River Development Ltd. ("Grand River") entered into a NT$20.55 billion (US$685 million) syndicated loan agreement with Yuanta Commercial Bank as facility agent. According to Yuanta Commercial Bank, the syndicated loan closed 195 percent oversubscribed, attracting NT$40.05 billion (US$1.326 billion) in total from nine other local lenders and financial institutions, exceeding the original target of NT$20.55 billion. This syndicated loan is to finance the construction project to be built on the site of CTBC Financial Holding Co.'s former headquarters in its premium location, and the new landmark building is named Taipei Sky Tower.

2 Guarantees

2.1 Can a company guarantee borrowings of one or more other members of its corporate group (see below for questions relating to fraudulent transfer/financial assistance)?

According to the Company Act, no company can act as a guarantor of any nature, unless otherwise permitted by law or by the company's Articles of Incorporation. Thus, if permitted by its Articles of Incorporation, the company may provide guarantees for other members of its corporate group.

If the company is a public company, there will be additional restrictions. Pursuant to the Regulations Governing Loaning, Endorsement or Guarantees of Public Companies ("Guarantee Regulation"), a public company may provide guarantees only for the following companies: (1) a company with which the public company conducts business; (2) a company in which the public company directly and indirectly holds more than 50% of the voting shares; and (3) a company that directly and indirectly holds more than 50% of the voting shares in the public company. In addition, the guarantee provided by a public company should comply with the internal rules adopted in accordance with the Guarantee Regulation.

2.2 Are there enforceability or other concerns (such as director liability) if only a disproportionately small (or no) benefit to the guaranteeing/securing company can be shown?

Generally, there is no concern about the enforceability under this circumstance so long as all legal requirements are satisfied. However, if a company provides guarantees for others for only a disproportionately small benefit or without benefit in return in the absence of a justifiable cause, there may be concern that the directors resolving the guarantees may breach their fiduciary duties. Further, the creditors of the guarantor may apply to the court to revoke the guarantee if, due to the guarantee, the guarantor does not have sufficient assets to repay the debts owed to its creditors.

2.3 Is lack of corporate power an issue?

Please refer to our answer to question 2.1. If a company's Articles of Incorporation do not permit the company to provide guarantees to others, but the company's responsible person, such as a director, still provides guarantees to others on behalf of the company, the responsible person alone should be liable for the guarantees. The guarantee does not constitute a valid obligation of the company.

2.4 Are any governmental or other consents or filings, or other formalities (such as shareholder approval), required?

No governmental approval is required for a company to provide guarantees. As for due authorisation, a board resolution adopted by the board of directors of the company to provide guarantees normally would suffice, unless the Articles of Incorporation provide otherwise. In practice, however, it is not common for a company's Articles of Incorporation to require that the provision of guarantees be approved by a shareholders' meeting.

However, where a Taiwanese company provides a guarantee to its overseas affiliate (incorporated in a jurisdiction other than Mainland China) who borrows funds to make investment in Mainland China, the guarantor will require a prior approval of the Investment Commission ("IC"), the MOEA with respect to investment in Mainland China.

2.5 Are net worth, solvency or similar limitations imposed on the amount of a guarantee?

The Guarantee Regulation and a company's internal rules adopted in accordance therewith impose certain limitations on the aggregate amount of the company's guarantees to all counterparties and the amount of the company's guarantees to a single counterparty. If the internal rules are incorporated into the company's Articles of Incorporation, the violation of the internal rules and the Articles of Incorporation by the company in providing a guarantee may affect the enforceability of the guarantee. By contrast, if the company only violates the internal rules in providing the guarantee, it is generally considered that violation of such limitations will only result in an administrative fine imposed by the Financial Supervisory Commission or breach of fiduciary duty by the directors, but will not affect the enforceability of the guarantees.

2.6 Are there any exchange control or similar obstacles to enforcement of a guarantee?

A Taiwanese corporate entity or individual has an annual foreign exchange quota of US$50 million (or its equivalent) or US$5 million (or its equivalent), respectively. No prior approval from the CBC is required if the Taiwanese onshore guarantor converts New Taiwan Dollars into foreign currency for remittance to the offshore creditor and the conversion does not exceed the above quota. The CBC has the sole discretion to grant or withhold its approval on a case-by-case basis if the onshore Taiwanese guarantor's quota would be exceeded for such conversion.

3 Collateral Security

3.1 What types of collateral are available to secure lending obligations?

Among other things, the following types of collateral are commonly seen in secured lending transactions:

(1) a mortgage over real property, such as land and buildings;

(2) a chattel mortgage over a movable asset, such as machinery and equipment;

(3) a pledge over movable assets or securities, or a pledge over the pledgor's property rights which are transferable, such as the pledgor's rights in bank accounts, accounts receivable or patents; and

(4) an assignment of property rights, which are transferable.

3.2 Is it possible to give asset security by means of a general security agreement or is an agreement required in relation to each type of asset? Briefly, what is the procedure?

As a general rule, the security provider and the security interest holder should enter into an agreement to identify the specific asset subject to the security interest. A general security agreement without identifying such specific asset, such as a floating charge, is not enforceable under Taiwanese law. In addition, different types of assets may be subject to different requirements, such as registration or filing with the competent authorities, on the perfection of the security. We will briefly advise on such requirements in our answers to questions 3.3 to 3.7.

3.3 Can collateral security be taken over real property (land), plant, machinery and equipment? Briefly, what is the procedure?

Yes. In order to create a valid mortgage over the land, buildings and plants, the mortgagor and the mortgagee should enter into a written agreement, and a registration with the competent authority is required.

As for machinery and equipment, the security to be created may be a pledge or a chattel mortgage. The machinery and equipment on which a chattel mortgage can be created are subject to the list promulgated by the authority. Both security interests (pledge and chattel mortgage) give the security interest holder first priority over the machinery and equipment. To create a pledge, the pledgor and the pledgee have to enter into a written agreement and the pledgor should deliver the possession of the machinery and equipment to the pledgee, but registration with the competent authority is not required. To create a chattel mortgage, the mortgagor need not deliver the possession thereof to the mortgagee; however, registration with the competent authority is necessary in order for the mortgagee to claim the chattel mortgage against a *bona fide* third party.

3.4 Can collateral security be taken over receivables? Briefly, what is the procedure? Are debtors required to be notified of the security?

Yes. To create a pledge over receivables, the pledgee and the pledgor must enter into a written agreement. In addition, the receivables must be identifiable according to the content of the pledge agreement. Further, the obligor should be notified of the creation of the pledge in order for the pledgee to be able to claim the pledge against the obligor.

3.5 Can collateral security be taken over cash deposited in bank accounts? Briefly, what is the procedure?

Yes. To create a pledge over cash deposits, the pledgee and the pledgor must enter into a written agreement. The pledge shall not become effective against the account bank taking the cash deposits unless the account bank is notified of the creation of the pledge. Nevertheless, please note that the concept of a floating charge is not recognised under Taiwanese law. In other words, the pledge covers only the cash in the bank account when such pledge is created and notified to the bank at which the account was opened. The pledge will not cover the cash deposited in the bank account after the account bank is notified of the pledge. To deal with this issue, the pledgor, in practice, will be required to periodically confirm with the account bank the amount of cash in the bank account to ensure that the pledge also covers the cash deposited after the creation of the pledge.

3.6 Can collateral security be taken over shares in companies incorporated in your jurisdiction? Are the shares in certificated form? Can such security validly be granted under a New York or English law governed document? Briefly, what is the procedure?

Yes. According to the Company Act, a company should issue shares in certificated form if its issued capital reaches a certain amount specified by the competent authority. Currently, the threshold amount is NT$500 million. In addition, a public company may issue shares in scripless form. To create a pledge over shares in certificated forms, a written agreement is required. The certificates of the pledged shares shall be duly endorsed and delivered by the pledgor to the pledgee. Furthermore, the company issuing the shares shall be notified of the creation of a pledge in order to register such pledge on the shareholders' roster. The creation of a pledge is valid between the pledgee and the pledgor when the certificates of the shares have been endorsed and delivered to the pledgee. However, the creation of the pledge cannot be claimed against the company unless the company is notified of the creation of the pledge.

To create a pledge over listed shares which are traded and transferred through the book-entry system of Taiwan Depository and Clearing Corporation ("TDCC"), the pledgor and the pledgee have to sign a form prescribed by the TDCC and have the pledge registered with the TDCC.

A pledge over shares can also be created based upon the document governed by New York or English law, as long as the creation and perfection of the pledge follow the procedures and requirements described above.

3.7 Can security be taken over inventory? Briefly, what is the procedure?

A floating charge over the inventory is not enforceable under Taiwanese law. Please refer to our answer to question 3.2.

3.8 Can a company grant a security interest in order to secure its obligations (i) as a borrower under a credit facility, and (ii) as a guarantor of the obligations of other borrowers and/or guarantors of obligations under a credit facility (see below for questions relating to the giving of guarantees and financial assistance)?

(i) Yes, it can.

(ii) This issue is whether a company may provide guarantees for others. Please refer to our answer to question 2.1.

3.9 What are the notarisation, registration, stamp duty and other fees (whether related to property value or otherwise) in relation to security over different types of assets?

No notarisation or stamp duty is required for the creation of security over different types of assets, mentioned in our answer to question 3.1. The registration fee for creating a chattel mortgage over a movable asset is NT$900. The registration fee for creating a mortgage over real property is equivalent to 1/1,000 of the total amount secured by the mortgage.

3.10 Do the filing, notification or registration requirements in relation to security over different types of assets involve a significant amount of time or expense?

Regarding the registration fee, please refer to our answer to question 3.9. The authority in charge of the registration will only conduct a formality review and it is not expected that the registration will take a significant amount of time.

3.11 Are any regulatory or similar consents required with respect to the creation of security?

In addition to the requirement of registration for certain types of security interests as mentioned above, generally the creation of the security interests does not require a regulatory or similar consent.

However, it is worth noting that, according to the interpretation of the MOEA, a foreign company having no branch office in Taiwan, the Republic of China is not allowed to be registered as a security interest holder. In local practice, the competent authorities will not permit such a foreign company to be registered as a mortgagee of real property or a chattel mortgagee of a movable asset.

3.12 If the borrowings to be secured are under a revolving credit facility, are there any special priority or other concerns?

Take a real property mortgage, for example. The mortgage can be divided into a general mortgage and a maximum amount secured mortgage. As for a general mortgage, the obligations to be secured should exist upon the creation of the mortgage. Otherwise, the mortgage will be held unenforceable. By contrast, a maximum amount secured mortgage is to secure the obligations created and owed to the mortgagee for a period of time. So long as the secured obligations exist at the end of the mortgage period, the mortgagee may foreclose the real property. Since the obligations under a revolving credit facility may arise and be satisfied from time-to-time according to the borrower's drawdown and repayment, the mortgage to secure such obligations should be a maximum amount secured mortgage instead of a general mortgage. The above also applies to a chattel mortgage and a pledge.

3.13 Are there particular documentary or execution requirements (notarisation, execution under power of attorney, counterparts, deeds)?

No, there are not.

4 Financial Assistance

4.1 Are there prohibitions or restrictions on the ability of a company to guarantee and/or give security to support borrowings incurred to finance or refinance the direct or indirect acquisition of: (a) shares of the company; (b) shares of any company which directly or indirectly owns shares in the company; or (c) shares in a sister subsidiary?

Regarding the prohibitions and restrictions on the provision of guarantees by a company, please refer to our answer to question 2.1. The provision of security other than a guarantee generally will be deemed as providing a guarantee as well, and is subject to the same prohibitions and restrictions.

In addition, according to the Company Act, a company cannot redeem or buy back any of its outstanding shares unless permitted by law. For instance, a company may purchase up to 5% of its outstanding shares and transfer the same to its employees. To give another example, a listed company may buy back its outstanding shares in the circumstances permitted under the Securities and Exchange Act. The restriction on a company's ability to buy back its outstanding shares extends to the company's controlled company; in addition, the violation of such restriction may cause the buy-back to be void. A subsidiary of the parent company cannot purchase the shares of the parent company. Nevertheless, the Company Act does not prohibit a sister subsidiary from purchasing the shares of another sister subsidiary if the other sister company, together with its parent company, does not directly or indirectly hold more than 50% of the sister company.

5 Syndicated Lending/Agency/Trustee/Transfers

5.1 Will your jurisdiction recognise the role of an agent or trustee and allow the agent or trustee (rather than each lender acting separately) to enforce the loan documentation and collateral security and to apply the proceeds from the collateral to the claims of all the lenders?

As a general practice for a syndicated loan, syndicated banks will appoint an agent bank to act for and on behalf of the syndicated banks, including registering the agent bank as, for instance, a mortgagee and foreclosing the mortgaged property. In addition, there will be a clause in the syndicated loan agreement to the effect that the syndicated banks' claims against the borrower under the syndicated loan agreement are joint and several. Given this, the agent bank may claim the whole amount of the loan from the borrower and distribute the proceeds obtained therefrom to the syndicated banks in accordance with their proportion of participation in the loan.

Nevertheless, under Taiwan law, it is questionable whether or not a third party, who is not a creditor/lender, could validly hold the collateral as a trustee or a security agent for other creditors/lenders. Pursuant to the Civil Code, a mortgage/pledge would not be validly created in favour of the creditor/mortgagee/pledgee if there is no underlying credit owned by the mortgagee/pledgee against the debtor.

5.2 If an agent or trustee is not recognised in your jurisdiction, is an alternative mechanism available to achieve the effect referred to above which would allow one party to enforce claims on behalf of all the lenders so that individual lenders do not need to enforce their security separately?

As advised in question 5.1 above, in practice, if the lenders' claims against the borrowers are joint and several, one of the lenders may be appointed as the agent bank by syndicated banks to act for and on behalf of all the syndicated banks, including registering the agent bank as, for instance, a mortgagee and foreclosing the mortgaged property.

5.3 Assume a loan is made to a company organised under the laws of your jurisdiction and guaranteed by a guarantor organised under the laws of your jurisdiction. If such loan is transferred by Lender A to Lender B, are there any special requirements necessary to make the loan and guarantee enforceable by Lender B?

The transfer of the loan from Lender A to Lender B will not be effective against the borrower and the guarantor until either Lender A or Lender B has notified the borrower and the guarantor of such transfer.

6 Withholding, Stamp and Other Taxes; Notarial and Other Costs

6.1 Are there any requirements to deduct or withhold tax from (a) interest payable on loans made to domestic or foreign lenders, or (b) the proceeds of a claim under a guarantee or the proceeds of enforcing security?

(a) For a domestic non-bank lender, who is a Taiwan resident or a profit-seeking enterprise with a fixed place of business in Taiwan, the withholding tax rate for interest is 10% but such withholding tax is applicable to corporate borrowers only. Individual borrowers are not required to withhold tax on interest.

For a foreign lender, who is a non-Taiwan resident or a profit-seeking enterprise without a fixed place of business in Taiwan, the withholding tax rate for interest applicable to a corporate borrower is 20%, but if the interest derives from short-term commercial papers, securitised instruments, government/corporate/financial institution bonds, or conditional transactions, the withholding tax is 15%. Moreover, most of the tax treaties provide a reduced income tax withholding rate of 10%. Taiwan has signed tax treaties with 32 jurisdictions; namely, Australia, Austria, Belgium, Canada, Denmark, France, Gambia, Germany, Hungary, India, Indonesia, Israel, Italy, Japan, Kiribati, Luxembourg, Macedonia, Malaysia, the Netherlands, New Zealand, Paraguay, Poland, Senegal, Singapore, Slovakia, South Africa, Swaziland, Sweden, Switzerland, Thailand, the United Kingdom and Vietnam.

(b) Where the portion of the proceeds is to indemnify the principal of the loan made by the lender, it will not be subject to income tax. If the portion of the proceeds is to indemnify the default interest sustained by the lender, it may be subject to income tax as mentioned above. Moreover, in the event that the proceeds include a penalty pursuant to an agreement between the lender and the borrower, such penalty will be subject to income tax unless the lender may prove that the penalty is to indemnify losses suffered by the lender.

6.2 What tax incentives or other incentives are provided preferentially to foreign lenders? What taxes apply to foreign lenders with respect to their loans, mortgages or other security documents, either for the purposes of effectiveness or registration?

(1) Income tax on the following categories of income shall be exempted:

- Interest derived from loans offered to the Taiwanese government or legal entities within the territory of Taiwan by foreign governments or international financial institutions for economic development, and interest derived from the financing facilities offered to their branch offices and other financial institutions within the territory of Taiwan by foreign financial institutions.
- Interest derived from loans extended to legal entities within the territory of Taiwan by foreign financial institutions for financing important economic construction projects under the approval of the Ministry of Finance.
- Interest derived from favourable-interest export loans offered to or guaranteed for the legal entities within the territory of Taiwan by foreign governmental institutions and foreign financial institutions which specialise in offering export loans or guarantees.

Moreover, some of the tax treaties provide an exemption from income tax withholding for interest payment. For example, the Netherlands-Taiwan Tax Treaty provides that the interest which is paid in respect of a bond, debenture or other similar obligations of a Taiwanese public entity, or of a subdivision or local authority of Taiwan, should be taxed only in Netherlands.

(2) For the purposes of effectiveness or registration, there is no tax applicable to foreign investments, loans, mortgages or other security documents.

6.3 Will any income of a foreign lender become taxable in your jurisdiction solely because of a loan to or guarantee and/or grant of security from a company in your jurisdiction?

No, a foreign lender (except for a foreign entity's Taiwan branch) will not be subject to Taiwan income taxes solely because of a loan to or guarantee and/or grant of security from a Taiwanese company.

6.4 Will there be any other significant costs which would be incurred by foreign lenders in the grant of such loan/guarantee/security, such as notarial fees, etc.?

Please refer to our answer to question 3.9.

6.5 Are there any adverse consequences to a company that is a borrower (such as under thin capitalisation principles) if some or all of the lenders are organised under the laws of a jurisdiction other than your own? Please disregard withholding tax concerns for purposes of this question.

A thin capitalisation rule was incorporated into the Income Tax Act effective from January 28, 2011. That is, retroactively from January 1, 2011, if the ratio of a company's debts (to its related party) to its equity exceeds a certain ratio, the interest expense arising out of the portion of the debts exceeding said ratio is not deductible, except for financial institutions (including banks, cooperatives, financial

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holding companies, bills finance companies, insurance companies, and securities firms). The Ministry of Finance, by referring to international practices, has set a safe harbour debt-equity ratio of 3:1.

The same treatment in respect of the thin capitalisation rule applies to both domestic and foreign lenders.

7 Judicial Enforcement

7.1 Will the courts in your jurisdiction recognise a governing law in a contract that is the law of another jurisdiction (a "foreign governing law")? Will courts in your jurisdiction enforce a contract that has a foreign governing law?

Generally, the choice of a foreign governing law to govern a contract would be recognised as a valid choice of law and given effect by the courts of Taiwan, provided that the relevant provisions of the foreign governing law would not be applied to the extent such courts hold that: (i) the application of such provisions would be contrary to the public order or good morals of Taiwan; or (ii) such provisions would have the effect of circumventing mandatory and/or prohibitive provisions of Taiwan law. However, where the contract is about the creation/perfection of a security interest, such as a pledge and mortgage, the choice of law will be subject to the conflicts of law of Taiwan.

7.2 Will the courts in your jurisdiction recognise and enforce a judgment given against a company in New York courts or English courts (a "foreign judgment") without re-examination of the merits of the case?

Any final judgment rendered by a foreign court shall be recognised and enforceable in Taiwan without review of the merits, provided that the court of Taiwan in which the enforcement is sought is satisfied that:

(i) the foreign court rendering the judgment has jurisdiction over the subject matter according to Taiwan law;

(ii) the judgment and the court procedures resulting in the judgment are not contrary to the public order and good morals of Taiwan;

(iii) if a default judgment was entered into against the losing party, the losing party was (a) duly served within a reasonable period of time within the jurisdiction of such court in accordance with the laws and regulations of such jurisdiction, or (b) process was served upon the losing party with the judicial assistance of Taiwan; and

(iv) judgments of the Taiwan court are recognised by the foreign court on a reciprocal basis.

To our knowledge, there is reciprocity for enforcement of judgments between Taiwan and New York/England.

7.3 Assuming a company is in payment default under a loan agreement or a guarantee agreement and has no legal defence to payment, approximately how long would it take for a foreign lender to (a) assuming the answer to question 7.1 is yes, file a suit against the company in a court in your jurisdiction, obtain a judgment, and enforce the judgment against the assets of the company, and (b) assuming the answer to question 7.2 is yes, enforce a foreign judgment in a court in your jurisdiction against the assets of the company?

(a) Depending on the complexity of the case in dispute, it could take half a year to one year or longer for each of the district court, the high court and the Supreme Court to render a judgment. Regarding the enforcement of the final judgment against the assets of the company, it also depends on the value and types of the company's assets. For example, to foreclose a mortgaged real property, it may take from several months to one year or longer to conduct the auctions for the real property if there is no bidder or if the bid price is below the set auction price.

(b) Depending on whether the Taiwan court or the counterparty has raised any objections to the elements set forth in our answer to question 7.2, it may take months or one year or longer for the Taiwan court to render a judgment recognising the foreign judgment. In addition, as mentioned in point (a) above, the enforcement of a final judgment against the assets of the company depends on the value and types of the company's assets.

7.4 With respect to enforcing collateral security, are there any significant restrictions which may impact the timing and value of enforcement, such as (a) a requirement for a public auction, or (b) regulatory consents?

(a) Depending on the types of collateral security, foreclosure of collateral security through a court proceeding may require a public auction. For instance, if the real property is foreclosed through a court proceeding, the court will designate an expert to assess the value of the real property and hold a public auction to sell it. If the real property has not been sold due to the fact that no bidder attended the auction or the bidding price is below the auction price set by the court, the court will have to reduce the auction price and repeat similar exercises to sell the real property in accordance with the Mandatory Execution Act. Accordingly, foreclosing the real property may take longer through a public auction than by other means of enforcement such as a private agreement between the mortgagor and the mortgagee to settle debts by transferring ownership of the real property to the mortgagee.

(b) Generally, no regulatory consent is required in order for the security interest holder to enforce the collateral interest.

7.5 Do restrictions apply to foreign lenders in the event of (a) filing suit against a company in your jurisdiction, or (b) foreclosure on collateral security?

(a) Generally, no. However, according to the Code of Civil Procedure, if a plaintiff has no domicile, office, or place of business in Taiwan, the court shall, by a ruling on motion filed by the defendant, order the plaintiff to provide a security for the litigation expenses. Such requirement will not apply in cases where either the portion of the plaintiff's claim is not disputed by defendant or the plaintiff's assets in Taiwan are sufficient to compensate the litigation expenses.

(b) Please refer to our answer to question 3.11.

7.6 Do the bankruptcy, reorganisation or similar laws in your jurisdiction provide for any kind of moratorium on enforcement of lender claims? If so, does the moratorium apply to the enforcement of collateral security?

Regarding bankruptcy, all enforcement actions against the debtor will be stayed by the bankruptcy of the debtor and all unsecured creditors must follow the bankruptcy proceeding administered by the court to file their claims against the debtor. Nevertheless, if a creditor, such as a lender, has a mortgage, pledge or right of retention over the debtor's assets, the lender may enforce such collateral security without going through the bankruptcy proceeding.

As for reorganisation, all enforcement actions against the debtor subject to reorganisation will be stayed no matter whether the lender is a secured (such as a mortgagee or a pledgee) or unsecured creditor. The lender may not foreclose the collateral security regardless of other stakeholders and should follow the reorganisation proceeding administered by the court.

7.7 Will the courts in your jurisdiction recognise and enforce an arbitral award given against the company without re-examination of the merits?

According to the Arbitration Law, a foreign arbitration award would be recognised and enforceable by the courts of Taiwan without reviewing the merits, provided that none of the following exist:

(i) where the recognition or enforcement of the arbitral award is contrary to the public order or good morals of Taiwan; or

(ii) where the dispute is not arbitrable under the laws of Taiwan.

In addition, if there is no reciprocity in the recognition and enforcement of an arbitral award between Taiwan and the country in which the arbitral award is made or the country whose arbitration rules are applicable, the Taiwanese court may dismiss the petition for the recognition of a foreign arbitral award.

8 Bankruptcy Proceedings

8.1 How does a bankruptcy proceeding in respect of a company affect the ability of a lender to enforce its rights as a secured party over the collateral security?

Please refer to our answer to question 7.6 regarding foreclosure of the collateral interest by a lender. In addition, if a lender's claims cannot be fully satisfied by foreclosing the collateral security, the lender may still participate in the bankruptcy proceeding as an unsecured creditor to seek possible repayment.

8.2 Are there any preference periods, clawback rights or other preferential creditors' rights (e.g., tax debts, employees' claims) with respect to the security?

There are no preference periods with respect to the security. The bankruptcy administrator may, within six months of the bankruptcy adjudication, apply to the court for the invalidation of the following acts of the debtor: (1) provision of security for outstanding debts within six months prior to the bankruptcy adjudication; and (2) repay the debts not yet due. In addition, the bankruptcy shall, within two years after declaration of the bankruptcy proceeding, file with the court to rescind the transaction which the bankrupt conducted with or without consideration before the bankruptcy proceeding if such transaction is deemed detrimental to the rights of the bankrupt's creditor and is revocable under the Civil Code.

As for preferential creditors' rights, below are certain examples:

(i) land value increment tax, land value tax and house tax levied on the sale of the real property which will rank prior to the mortgagee and the unsecured creditors;

(ii) the following labour claims will rank prior to unsecured creditors: (a) labour wages due and payable by the employer but overdue for a period of fewer than six months; (b) retirement payments payable by the employer pursuant to the Labour Standards Act but not yet paid; and (c) severance payable by the employer pursuant to the Labour Standards Act or Labour Pension Act but not yet paid; and

(iii) fees and debts incurred for the benefit of the bankruptcy estate which will rank prior to unsecured creditors.

8.3 Are there any entities that are excluded from bankruptcy proceedings and, if so, what is the applicable legislation?

The following may apply for bankruptcy adjudication: (1) natural persons; (2) juristic persons; and (3) partnerships and any other incorporated association with a representative or an administrator. An unincorporated association without a representative or administrator is excluded from a bankruptcy proceeding, and there is no special legislation applicable to such entity. Banks and insurance companies are excluded from bankruptcy proceedings and will be subject to the proceedings provided under the Banking Act, Deposit Insurance Act and Insurance Act.

8.4 Are there any processes other than court proceedings that are available to a creditor to seize the assets of a company in an enforcement?

According to the Civil Code, the creditor may initiate certain self-help remedies to seize the debtor's property and will not be liable therefor, provided that: (i) the assistance of the court or of other relevant authorities is not accessible in time and the satisfaction of the creditor's claim will be impossible or manifestly difficult without the self-help remedy; and (ii) the creditor shall apply for the court's assistance immediately after the self-help remedy is exercised. A creditor and the security provider may sign an agreement whereby the ownership of the mortgaged or pledged security will be transferred to the mortgagee or pledgee automatically when the debtor defaults. However, in the case of a mortgaged security, such agreement to transfer cannot be enforced against a *bona fide* third party, unless the mortgage is registered with the competent authorities.

9 Jurisdiction and Waiver of Immunity

9.1 Is a party's submission to a foreign jurisdiction legally binding and enforceable under the laws of your jurisdiction?

The Judicial Yuan of Taiwan has held an internal conference and reached a conclusion that a submission to jurisdiction clause will be valid in the absence of any of the following circumstances: (1) it would be unfair for the subject matter to be adjudicated by the chosen jurisdiction; (2) the consent of a party to submit to the chosen jurisdiction was obtained by fraud, duress or other unlawful means; (3) the parties were not equal-footed when they entered into the submission to jurisdiction agreement; (4) it would be inappropriate or inconvenient for the chosen jurisdiction to adjudicate the subject matter; and (5) the country of the chosen jurisdiction does not recognise and enforce judgments of Taiwan courts on a reciprocal basis. The conclusion made by the Judicial Yuan is, however, subject to test in court.

9.2 Is a party's waiver of sovereign immunity legally binding and enforceable under the laws of your jurisdiction?

Yes, it is. It will be binding upon that party under Taiwan law unless (i) the waiver would be contrary to the public order or good morals of Taiwan, or (ii) the waiver would have the effect of circumventing mandatory and/or prohibitive provisions of Taiwanese law.

10 Licensing

10.1 What are the licensing and other eligibility requirements in your jurisdiction for lenders to a company in your jurisdiction, if any? Are these licensing and eligibility requirements different for a "foreign" lender (i.e. a lender that is not located in your jurisdiction)? In connection with any such requirements, is a distinction made under the laws of your jurisdiction between a lender that is a bank *versus* a lender that is a non-bank? If there are such requirements in your jurisdiction, what are the consequences for a lender that has not satisfied such requirements but has nonetheless made a loan to a company in your jurisdiction? What are the licensing and other eligibility requirements in your jurisdiction for an agent under a syndicated facility for lenders to a company in your jurisdiction?

There is no particular licensing or other eligibility requirement to lend money to a company in Taiwan. However, the Company Act provides that the capital of a Taiwanese company shall not be lent to any person unless the lending arrangement is due to business transaction or is necessary for short-term financing and the aggregate amount of such short-term financing should not exceed 40% of the company's net value. As a result, in local practice, no company in Taiwan except banks, securities firms, insurance companies or pawn shops may engage in lending as an ordinary business. Taiwan has not opened the establishment and operation of lending/finance companies. Accordingly, currently it is not possible to set up a company to operate a lending business in Taiwan.

Since there is no particular licensing or eligibility requirement, the main distinction under the laws of Taiwan between a lender that is a bank versus a lender that is a non-bank, would be the application of the above lending restriction under the Company Act to a non-bank lender.

There is no particular licensing or other eligibility requirement or restriction on a foreign lender for making a loan to Taiwanese borrowers outside of Taiwan, regardless of whether the foreign lender is licensed or not. Nevertheless, a foreign company is not allowed to operate any business in Taiwan without being recognised and setting up a branch in Taiwan. Thus, if lending is the foreign company's business, making a loan to Taiwanese borrowers by the foreign company may violate the Company Act. Furthermore, as advised in our answer to question 2.6, in the case of a foreign loan to a Taiwanese borrower, the foreign exchange control would apply unless such foreign debts have been registered with the CBC by the Taiwanese borrower.

There are no licensing and other eligibility requirements in Taiwan for an agent under a syndicated facility for lending to a company in Taiwan. However, in practice, an agent is normally a member of the syndication and the credit rights of the syndicate members are joint and several in order to allow the agent to claim the repayment/payment and the collateral on behalf of the other syndicate members.

11 Other Matters

11.1 Are there any other material considerations which should be taken into account by lenders when participating in financings in your jurisdiction?

For foreign lenders who will participate in financing in Taiwan, please refer to our answer to question 3.11 regarding the MOEA's ruling on the ability of a foreign entity without a local presence to take collateral security.

If a foreign lender provides a loan with a term of more than one year to a Taiwanese company in which it owns shares or capital, or a Taiwanese partnership in which it is one of the partners, or a Taiwanese business of which it is the sole proprietor or a branch created by it, please note that a prior approval from the Investment Commission of the MOEA is required.

As to foreign exchange control, please refer to our answer to question 2.6.

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Chapter 76

United Arab Emirates

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1 Overview

1.1 What are the main trends/significant developments in the lending markets in your jurisdiction?

Based on our observations, as well as feedback from bankers, financiers and market leaders, the lending market in the UAE made slow progress during most of 2017. Factors such as a decline in oil prices, the delay in certain infrastructure projects and a more cautious approach to global trade had an effect on investor confidence and market liquidity. However, economic activity seems to be improving gradually. Attempts are being made to create a "knowledge economy" following the decrease in oil prices and a focus on non-oil growth in the market; for example, a focus on domestic public investment which is set to continue as the Dubai Expo 2020 draws closer. Banks have attempted to adjust to the higher interest rates and lower credit demand as the banks continue to be sufficiently capitalised but the cost of funding for banks remains high.

When reading this chapter it is important to note that the UAE provides the option for companies to incorporate either "onshore" (for which 51% of the company must be owned by a UAE national or 100% by a Gulf Cooperation Council ("GCC") national), or "offshore" (in one of over 35 free zones, including, but not limited to, the Dubai International Financial Centre ("DIFC")). Each free zone typically has its own laws and regulations (with the exception of criminal law) and crucially, companies may be 100% owned by foreign investors. The focus of this chapter will be on onshore UAE companies and companies incorporated in the DIFC (as the DIFC is the most relevant insofar as financial institutions and their activities are concerned).

Practitioners should also be aware that UAE onshore law is influenced by *Shari'a* (Islamic law); this is confirmed by its constitution, which provides that: "*Islamic Shari'a is a main source of legislation in the UAE*." However, the UAE (and certain individual Emirates) have decreed that free zones (such as the DIFC) may enact their own civil and commercial laws, in parallel to UAE onshore law. Nevertheless, any companies operating, lending or taking security in the UAE should be sensitive to UAE law and customs. A key example of this relates to the language used in underlying transaction documentation. Terms such as "lender", "borrower", "debt" and "loan", although used within this chapter to assist the reader, are not *Shari'a*-compliant and should be interpreted as (and used when working on *Shari'a*-compliant deals) "financier", "obligor", "facility" or "financing", as applicable.

On 29 December 2016, Federal Decree Law No. 9 of 2016 on bankruptcy (the "New Bankruptcy Law") came into effect, repealing the former insolvency regime and introducing the UAE's first standalone bankruptcy legislation. The law has sought to introduce restructuring and modernise insolvency procedures in the UAE, and applies more widely than the former regime, covering companies governed by the Commercial Companies Law (Federal Law No. 2 of 2015 concerning Commercial Companies) (the "CCL 2015"), some free zone companies, sole establishments and civil companies conducting professional business.

The New Bankruptcy Law has also introduced three main procedures for a business in financial difficulty: a protective composition; a restructuring scheme; and insolvency and liquidation. The implications of the New Bankruptcy Law on the lending market in the UAE are touched upon in this chapter, particularly with regards to the rights of secured creditors in enforcing their security interests during bankruptcy proceedings. The New Bankruptcy Law remains largely untested and we watch with interest how the legislation will apply in practice.

On 15 December 2016, Federal Law No. 20 of 2016 on the pledge of moveables as security for debt (the "New Pledge Law") was issued in the Official Gazette and came into effect on 15 March 2017. This is a significant new legislative development which substantially changes or regularises the manner in which a charge can be created over moveable assets. The New Pledge Law provides lenders with the ability to register effective pledges over tangible or intangible moveable assets that exist in the present or in the future, a problem both lenders and debtors have struggled with for some time. However, it is not yet clear to what extent the New Pledge Law will replace the current use of commercial mortgages, which also secures an interest over tangible and intangible assets.

The New Pledge Law changes the position of taking a pledge over moveable assets by removing the need to transfer the possession to the mortgagee or third party as bailee. A new electronic security register (the "Security Register") will be set up to record the rights of the parties under the pledge and to establish priority *vis-à-vis* competing creditors. Further detail on the practical effect and operation of the New Pledge Law should be clarified by executive regulations (the "Executive Regulations") which are due to come into effect imminently. At the time of writing, no information has been released regarding the scope and effect of the Executive Regulations and the date on which we can expect the Security Register to be operational. We anticipate that the New Pledge Law will provide greater confidence to both lenders and borrowers in the UAE lending market, although we still have little insight as to how the Security Register will operate and to what extent the Executive Regulations will impact the legislation in its current form.

From an Islamic finance perspective, many leading Islamic banks and financial institutions, including Dubai Islamic Bank, Emirates Islamic Bank and Abu Dhabi Islamic Bank, announced increased profits in 2017 largely due to increased *sukuk* issuance and innovative new banking technology. The asset-based nature of asset financing is well suited to the principles of Islamic financing, and there is a growing trend of *Shari'a*-compliant financing in the aviation, shipping and infrastructure industries. *Ijara* arrangements are often used to replicate conventional lease agreements, providing a viable *Shari'a*-compliant alternative to conventional aircraft and shipping financing. *Istisna*' contracts are also useful in circumstances where aircraft are purchased directly from the manufacturer and the financing is put in place before such aircraft are delivered. In addition, we have witnessed and are witnessing tangible interest by Islamic financial institutions in gaining exposure to asset-backed or asset-based lending in non-Islamic jurisdictions including the United States of America, the United Kingdom, and the European Union.

1.2 What are some significant lending transactions that have taken place in your jurisdiction in recent years?

In October 2016, Noor Bank PJSC and a syndicate of Gulf Cooperation Council financial institutions made an upsize facility of $230 million available to Ajman Bank PJSC. The deal was structured as a commodity *murabaha* financing and involved complex mechanics to ensure *Shari'a* compliance. It is significant due to the growth of the market for interbank Islamic liquidity management at a time of tightening liquidity and the increasingly cross-border nature of these deals.

In July 2017, Al Ahli Holding Group/Dubai Outlet Mall was advised on *Shari'a*-compliant project financing facilities, structured as a *Wakala* facility and an *Istisna*/forward lease, the proceeds of which are to be applied to corporate purposes and to the financing of the expansion of the Dubai Outlet Mall. The facility is secured by real estate mortgages, assignments of leases and insurances and account pledges. The facility was made available by a syndicate of banks including Noor Bank and Al Hilal Bank and was arranged by Dubai Islamic Bank.

2 Guarantees

2.1 Can a company guarantee borrowings of one or more other members of its corporate group (see below for questions relating to fraudulent transfer/financial assistance)?

A company can generally guarantee the borrowings of members of its corporate group in the UAE, subject to certain restrictions as set out in the response to question 4.1.

For both onshore and offshore entities, authority to provide guarantees is predominantly governed by its constitutional documents and obtaining the relevant corporate authorisations (see the response to question 2.3). Guarantees must be in writing and specify the amount secured by the guarantee.

Generally, guarantees provided under certain Islamic financing structures that are subject to *Shari'a* principles may not be permitted, if their objective is to guarantee a specified return to the lenders or investors. The purpose of the guarantee must be clearly defined from the outset, as per the laws of the UAE. Further, all documents relating to a *Shari'a*-compliant transaction must be pre-approved in writing by *Shari'a* scholars who issue compliance certificates (each a *Fatwa* and collectively *Fatawa*) per transaction and are expected to audit the transaction on a regular, often annual, basis to ensure that it continues to comply with *Shari'a* and its requirements, as interpreted by the relevant *Shari'a* scholars and documented in the relevant *Fatwa*.

2.2 Are there enforceability or other concerns (such as director liability) if only a disproportionately small (or no) benefit to the guaranteeing/securing company can be shown?

Whilst no specific restrictions are identifiable, the main concern revolves around a director's fiduciary duties to the relevant company.

Onshore

A director of an onshore company in the UAE is required to act in the company's best interests, as set out in the CCL 2015.

The directors of an onshore company must have regard to the legislative requirement for the pursuit of profit (CCL 2015 Article 8), and to further the company's objectives (CCL 2015 Article 22). With those interests in mind, there are also some distinct provisions to which directors should adhere, including a restriction on guaranteeing any loan agreement with a board member and third party (CCL 2015 Article 153) and entering into any loan agreements (typically interpreted as including guarantees) for a term that exceeds three years (CCL 2015 Article 154) (see the response to question 2.3).

Offshore

Similarly, free zone entities place similar responsibilities on the directors. The DIFC's Companies Law (DIFC Law No. 2 of 2009) (the "DCL") states that directors must, amongst other things, "act honestly, in good faith and lawfully with a view to the best interests of the Company" (DCL Article 53).

Directors for both onshore and offshore companies should therefore take care when committing a company to guarantee the financial risk of another entity, and should conduct appropriate due diligence to ensure the company is able to meet its payment obligations and that the company is not insolvent or likely to become insolvent.

2.3 Is lack of corporate power an issue?

Similar to the Western markets, the first step for both onshore and offshore companies is to review their constitutional documents to ensure that the company can provide a guarantee.

Onshore

By way of its constitutional documents, an onshore company may grant management with broad powers that enable it to run the company without involving its board of directors and shareholders (subject to certain restrictions for public companies – explored in more detail below).

In respect of onshore public joint stock companies ("PJSC"), directors may not enter into a loan agreement (which is interpreted by most practitioners and based on most court rulings to include guarantees) for a term that exceeds three years (CCL 2015 Article 154), unless the constitutional documents expressly permit this. If not expressly permitted, shareholder approval should be obtained. For onshore limited liability companies ("LLC"), which had previously avoided hefty regulation, directors should be aware that CCL 2015 now includes an article (Article 104) that states that the provisions therein, which apply to PJSC and private joint stock companies ("PrJSC"), shall now also apply to an LLC unless otherwise stated. On 29 April 2016, the UAE Ministry of Economy published Ministerial Resolution No. 272 of 2016 (the "Resolution"). The Resolution seeks to clarify which provisions regarding joint stock companies also apply to LLCs. Although the Resolution clarified many provisions in the CCL, certain provisions remain unaddressed, for example, whether Article 153, which prohibits providing loans to directors and their relatives, also applies to LLCs.

Offshore

Offshore companies must similarly act in accordance with their articles, though notably they need not comply with the CCL 2015, except to the extent they also operate onshore within the UAE.

2.4 Are any governmental or other consents or filings, or other formalities (such as shareholder approval), required?

In general, no governmental consents or filings are required in order to give effect to a guarantee in the UAE. However, a guarantee should be properly authorised by the company's constitutional documents and authorisations as previously stated. For onshore companies, a guarantee's form and substance should satisfy the requirements of the Civil Transactions Law (Federal Law No. 5 of 1985, as amended) (the "Civil Transactions Law") and the Commercial Transactions Law (Federal Law No. 18 of 1993) (the "Commercial Transactions Law"), as applicable. Practitioners should also consider that offshore companies may have their own legislation that governs such form and substance.

Additionally, if a transaction needs to comply with *Shari'a* principles, the pre-approval of *Shari'a* scholars is required as more fully described in the response to question 2.1.

2.5 Are net worth, solvency or similar limitations imposed on the amount of a guarantee?

As mentioned above, depending on the *Shari'a* structuring of the transaction, certain guarantees that assure a specified return for the lender may be restricted, and specific advice should be sought in this regard.

Onshore

For onshore companies, the Civil Transactions Law (Article 1061) requires that guarantees must be issued with respect to a specified debt or certain amount. In addition, the guarantee should be within the capacity of the guarantor to discharge. Therefore, whilst there is not a limit *per se*, a guarantor should not guarantee more than it can afford to repay. Guarantees should also be specific in nature, and whilst judgments have been made in the UAE that have recognised 'all-monies' guarantees, the above restrictions should be carefully considered on a case-by-case basis.

Offshore

There are no such limitations placed on DIFC companies, other than those outlined in the response to question 2.2.

2.6 Are there any exchange control or similar obstacles to enforcement of a guarantee?

There are no exchange controls in the UAE that would restrict the enforcement of both onshore and offshore guarantees, aside from certain restrictions arising under international sanctions or local boycott regulations.

Onshore

The interpretation of the limitation period for onshore companies may affect enforcement of guarantees. UAE law states that in relation to surety, a creditor should claim the debt within six months of the date on which payment fell due. Dubai's Court of Cassation interpreted this as applying to all guarantees; however, Abu Dhabi's Supreme Court has suggested that the applicable period may be 10 years for commercial guarantees. It is therefore common practice to disapply the provision that states the limitation period is six months in the relevant transactional documents, though it is not clear if this would succeed in ensuring that the provision would not have effect.

Offshore

Offshore companies will be governed by their own laws. For example, the legislation in the DIFC states that, excluding fraud, a claim cannot be commenced more than six years after the date of the events that gave rise to the claim. However, should the free zones' legislation be silent regarding limitation, the period will be the same as under UAE law.

3 Collateral Security

3.1 What types of collateral are available to secure lending obligations?

Although there are differences between the types of collateral available to onshore and offshore companies, both allow (with certain restrictions and limitations) security over: (i) real estate/land; (ii) tangible movable property (e.g., machinery or stock); (iii) shares; (iv) receivables; and (v) cash deposits.

The New Pledge Law is intended to govern the taking of security over a wide variety of moveable property located onshore in the UAE, both tangible and intangible. The law has alleviated the more cumbersome aspects of taking security over movable property, which was previously governed by the Civil Transactions Law and the Commercial Transactions Law. The old system will continue to apply to the taking of security over assets which do not fall within the parameters of the New Pledge Law, including land and shares.

For each free zone, the Federal or Emirate decree that created the free zone should be reviewed, as it may grant authority for that free zone to regulate matters relating to taking and enforcing security. Most free zones will only have the power to regulate and promulgate laws regarding the incorporation of companies, and therefore the relevant Federal laws of the UAE and specific Emirate will continue to apply to all aspects not expressly regulated by the free zone. In relation to the DIFC, the creation, perfection and enforcement of security is governed by the DIFC Law of Security (DIFC Law No. 8 of 2005) and the Security Regulations, and the DIFC Real Property Law (DIFC Law No. 4 of 2007). Such regulations more closely mimic common law-based regulations governing the taking of security.

Foreign lenders should also bear in mind that ownership of land may be restricted to UAE (or GCC) nationals in certain Emirates. Dubai, however, is generally more progressive in this regard as it permits foreign ownership of land in certain designated areas (Regulation No. 3 of 2006 Determining Areas for Ownership by Non-UAE Nationals of Real Property in the Emirate of Dubai). Such restrictions may affect the perceived value placed on any such security by lenders; the ability of a foreign lender to enforce its security package over, for example, real estate in an area that is not designated as freehold, or over shares in a company incorporated onshore up to a percentage that exceeds the maximum that foreigners are entitled to own, should be borne in mind when negotiating the security package for any given transaction. This often triggers the need to consider a structured solution, or the involvement of a security agent or trustee.

3.2 Is it possible to give asset security by means of a general security agreement or is an agreement required in relation to each type of asset? Briefly, what is the procedure?

Whilst general over-arching security agreements can be provided in the UAE, the general practice and advisable approach is to have separate agreements wherever possible. Further, as certain security documents may have to be notarised and registered with different government entities, particularly in relation to land and shares, it may create uncertainty and result in additional costs if they were to be included in the same agreement.

Additionally, in *Shari'a*-compliant transactions *Shari'a* scholars will insist on the separation of subject matters in documentation to ensure there is a reduced chance of material ambiguity (*Gharar*) in the agreements.

The procedures for the relevant security agreements vary from asset to asset (see the response to questions 3.3 and 3.8).

3.3 Can collateral security be taken over real property (land), plant, machinery and equipment? Briefly, what is the procedure?

Onshore

A person or company owning property in the UAE (with the legal capacity to sell) can create a mortgage in favour of a mortgagee licensed by the UAE Central Bank. The mortgage can be over: (i) land and buildings; (ii) a leasehold interest; and/or (iii) a building erected on leased land.

In order to perfect a valid mortgage in the UAE, the land mortgage agreement (generally pre-printed documents prescribed by the relevant authorities) must be: (i) executed in writing in the presence of a public notary or the relevant land department in Arabic; and (ii) provided to the mortgage registrar with the land department or the local municipality of the relevant Emirate. A fee, which is usually payable, is dependent on the specific Emirate; however, it can commonly be linked to a percentage of the mortgage amount (see the response to question 3.9). This can be onerous on the borrower if they are covering the costs of the transaction. Furthermore, enforcement of such security can incur additional fees and expenses which may be prohibitive to the lending entity when it comes to an enforcement scenario and transferring title.

As discussed in the response to question 3.1, foreign lenders should also bear in mind that ownership of land, onshore companies and other assets may be restricted to UAE (or GCC) nationals in certain Emirates and as such, the involvement of a local bank or a local/regulated security agent or trustee may be necessary. Furthermore, regardless of foreign ownership restrictions, certain types of security can only be given in favour of a bank licensed by the UAE Central Bank.

Lenders should also be aware that it is possible to take mortgages over ships and aircraft under the laws of registration of the relevant assets. In the case of mortgages over aircraft, the mortgage instrument may be filed with the General Civil Aviation Authority and a UAE pledge will also typically be taken over these assets. It is also worth noting that, in 2008, the UAE ratified the Convention and Aircraft Protocol on International Interests in Mobile Equipment on Matters Specific to Aircraft Equipment, commonly known as the Cape Town Convention.

Offshore

Interests in land in free zones are normally subject to their own regulations. The DIFC, for example, is governed by the DIFC Real Property Law, which outlines that land transactions must be registered in a central register administered by the DIFC and should include: i) a description to identify the property; ii) a description to identify the interest to be mortgaged; and iii) a description of the secured debt or liability.

As with land, security over machinery and equipment in free zones may be subject to its own regulation, and the relevant Federal or Emirate decree which created the free zone should be consulted. The DIFC, for example, unlike UAE law, generally allows for the registration and enforcement of a floating charge (see the response to question 3.7).

3.4 Can collateral security be taken over receivables? Briefly, what is the procedure? Are debtors required to be notified of the security?

Yes, typically security over receivables is taken by an assignment of the contractual rights under the agreement giving rise to the receivables.

Onshore

The New Pledge Law will apply to the creation of security over receivables from third parties. The law provides that security may be created over receivables so long as the parties enter into a written agreement that complies with the requirements of the Executive Regulations, which are due to be introduced and become effective imminently. The security interest will be effective against third parties upon registration on the Security Register, which is also yet to be established. At the date of writing, there has been no information on when the Security Register will be set up. In addition to registration, it will also be necessary to notify any possessor of the secured property of the security interest being created if the relevant property is not in the possession of the security provider.

Offshore

Such an assignment is permissible in offshore transactions. Specifically, security in the DIFC is governed and permitted by the DIFC Law of Security. Notably, the DIFC does not provide different rules depending on the asset to be secured (excluding land); hence all security to be taken in the DIFC must 'attach' to be effective. For 'attachment' to occur:

(i) a value must be given;

(ii) the debtor must have rights in the collateral or the power to transfer its rights in the collateral to a security party; and

(iii) one of the following: (a) the obligor must be bound by a security agreement that provides a description of the collateral; or (b) the collateral must be a negotiable document of title, a negotiable instrument, money, deposit account or financial property and the secured party must have control pursuant to the obligor's security agreement.

Perfection of the relevant security is attained once: (i) it is 'attached'; and (ii) a 'financing statement' is filed with the DIFC Security Registrar. The 'financing statement' should be filed within 20 days of the date of the security agreement and will lapse five years from the date it is filed (notwithstanding the term of the security agreement itself), pending a continuation statement.

However, it should be noted that a financing statement is not appropriate for security taken over the assignment of certain receivables (as set out in the DIFC Security Regulations) and monies held in an investment account (as defined in DIFC Personal Property Law).

3.5 Can collateral security be taken over cash deposited in bank accounts? Briefly, what is the procedure?

Onshore

The New Pledge Law will govern the taking of security over funds deposited in a UAE licensed bank. The law provides that the security shall be created by the parties entering into a written agreement which complies with the requirements of Executive Regulations. The security will need to be registered on the Security Register once it is established. The New Pledge Law provides that future property may be secured, which is particularly relevant in respect of security over cash deposits. The previous position was that the credit balance had to be fixed and identifiable, i.e. no floating charge, which in effect meant that the borrower had to maintain a blocked account. This resulted in some foreign lenders also requiring that additional security be taken over offshore accounts where floating security is recognised and enforceable. The New Pledge Law should therefore be a welcome development to banks when taking local law account pledges.

Non-resident foreign banks should also be aware that, under UAE law, a pledge over funds in a bank account can only be granted in favour of another bank or financial institution licensed in the UAE.

Offshore

Currently, the only free zone permitted to regulate banks is the DIFC, and any relevant account charges are regulated by the DIFC Security Law. The procedure and restrictions (including monies held in an investment account) are set out in the response to question 3.4. For any other free zone, UAE law applies.

3.6 Can collateral security be taken over shares in companies incorporated in your jurisdiction? Are the shares in certificated form? Can such security validly be granted under a New York or English law governed document? Briefly, what is the procedure?

Security can be taken over shares in the form of a share pledge in relation to all onshore types of companies, including onshore LLCs and most offshore companies. The pledge documentation should always be governed by the relevant jurisdiction of the pledgor, which would typically be UAE onshore law, or in the case of the DIFC, DIFC law. Security can be granted under a different jurisdiction; however, it is not advisable as the merits of any dispute would have to be looked at again, in accordance with and by the courts of the jurisdiction where the pledgor is located if the security was ever enforced upon (see the response to question 7.1).

Onshore

The procedure for pledging shares in a PJSC or PrJSC is by the physical delivery of the share certificates to the pledgee and entry of the pledge in the company register (though if the shares are not in certificated form, physical delivery is not required). A PJSC will usually be required to be listed at one of the UAE's stock exchanges and the pledge should be recorded in the share register maintained by the relevant exchange. A PJSC will appoint a share register keeper (such as the Dubai Financial Market ("DFM") or Abu Dhabi Securities Exchange ("ADX")) to record the pledge. Upon such registration the pledgee typically has the right to collect dividends and entitlements attached to the shares, though in most cases these are returned to the borrower (with certain limitations) unless the borrower defaults.

Onshore LLCs did not previously have any clear legal guidance on how their shares could be pledged, and the pledge perfected. However, the CCL 2015 implements a new system (under Article 79) that allows pledges of shares in an LLC to be made in accordance with such company's articles, and under an official notarised document to be registered at the companies registrar, for which the Minister of Economy intends to issue specific regulation. It is anticipated in the market in Dubai that pledges over shares will have to be registered with the DED to be effective, which is an important development which may facilitate the extension of credit to SMEs, start-ups and family businesses.

As indicated before, lenders should also bear in mind that foreign investors are still restricted in their ownership of capital regarding onshore companies (at least 51% should be owned by a UAE national) therefore enforcement can be difficult; and typically, a local security agent or trustee will need to be employed.

Offshore

Most offshore companies (including the DIFC) have physical share certificates that can be pledged and delivered, although this is not always the case. Most free zones also have their own registration requirements for such security, which may include execution of certain forms and filing of executed documents with the relevant free zone registrar.

3.7 Can security be taken over inventory? Briefly, what is the procedure?

Onshore

The New Pledge Law is intended to govern the validity and enforceability of security over, *inter alia*, raw and primary products and commodities, equipment machinery and work tools. The formalities of registration are as set out above, and the security will have to be registered on the Security Register once established. As the law remains untested, we have yet to understand how the enforceability of such security shall operate.

Currently, security can be taken over machinery and trading stock by way of a commercial mortgage. To register a commercial mortgage, it has to be executed in writing and the agreement has to be notarised and registered in the commercial register of the relevant Emirate's Department of Economic Development. Notice of the mortgage is to be given in two local Arabic newspapers two weeks prior to such registration. The registered mortgage will only be valid for a period of five years unless renewed and updated (notwithstanding the term in the underlying agreement). It is not yet clear to what extent pledges under the New Pledge Law will replace the current use of commercial mortgages.

Offshore

Security over such assets in free zones is permitted but subject to the relevant free zone requirements. In the DIFC, for example, it is possible to create a security interest over future assets/advances, acquired assets and the debtor's right to use, or dispose of all or part of the relevant items in line with the procedure set out in the response to question 3.4.

3.8 Can a company grant a security interest in order to secure its obligations (i) as a borrower under a credit facility, and (ii) as a guarantor of the obligations of other borrowers and/or guarantors of obligations under a credit facility (see below for questions relating to the giving of guarantees and financial assistance)?

Both onshore and offshore companies should be able to grant security to secure their own borrowings and those of other borrowers subject to the requirements and restrictions set out herein.

3.9 What are the notarisation, registration, stamp duty and other fees (whether related to property value or otherwise) in relation to security over different types of assets?

Stamp duty and taxes are not applicable for either onshore or offshore companies given the nil rate of direct tax applicable to most sectors in the UAE (see the response to question 6.1). However, transfers of land may incur registration fees akin to stamp duty, payable to the relevant Emirates' land registry. These costs vary from Emirate to Emirate.

Notarisation is commonplace in the UAE and, even if not expressly required, may be used in order to add authority to documents. Fees in relation to this are normally charged at a very low percentage (approximately 0.25% and subject to a cap) of the secured amount, and importantly notarisation for onshore documentation is always in Arabic.

We have yet to know if the Executive Regulations, once issued, will provide further information on fees in relation to security over moveable property.

Onshore

Onshore mortgage registration varies between Emirates; the Dubai Land Department, for example, currently charges 0.25% of the value of the mortgage amount. The fees for registration of other types of security vary depending on which Emirate the security is registered in, but commonly involve a percentage of the amount secured and are subject to a cap.

Offshore

Registration varies in the DIFC; for example, a mortgage fee is US$100 (or US$273 for an Islamic mortgage), and if the property has not yet been registered with the DIFC Registrar of Real Property an additional fee (currently 5% of the total value of the property) is also payable. The cost of filing a 'financing statement' (see the response to question 3.4) is currently at a cost of US$1 per US$1,000 secured, subject to a minimum of US$250 and a maximum of US$5,000.

3.10 Do the filing, notification or registration requirements in relation to security over different types of assets involve a significant amount of time or expense?

In comparison to the United Kingdom and United States, the process of securing assets is generally more complex and expensive. Arguably, the relevant free zones have a more straightforward approach, although it is still more uncertain than the established Western systems. This is somewhat due to a lack of formalised or standard structure of registrars for registration of each type of security in the relevant Emirates. It is hoped that the introduction of the Security Register for the registration of security over moveable property will alleviate some of this uncertainty. Furthermore, a lack of established case law and clarity regarding the perfection of security, and which department security should be registered with, can make it difficult to assess what registration steps to take next.

3.11 Are any regulatory or similar consents required with respect to the creation of security?

Typically, no regulatory or similar consents prior to the creation of a security are required. However, to the extent that a regulatory or government-owned body must accept registration of a certain security, this may be deemed a form of consent. Moreover, in circumstances where the secured assets are equities or other forms of securities, certain approvals may be required and structural considerations may need to be taken into account. Further, any security against government-owned assets or certain individuals within government organisations will require consent.

3.12 If the borrowings to be secured are under a revolving credit facility, are there any special priority or other concerns?

There are no specific concerns or case law relating to such matters that are apparent.

3.13 Are there particular documentary or execution requirements (notarisation, execution under power of attorney, counterparts, deeds)?

The procedures and requirement for security are set out in the answers to the questions above. For both onshore and offshore companies it should be noted that signing in counterparts is generally accepted practice; however for enforcement purposes, there should always be a 'counterparts' provision in the documentation.

For onshore entities executing specific security documents, including power of attorneys, it may need to be executed in front of the relevant notary public and/or registrar. Notably, the concept of deed is not recognised in the UAE outside the DIFC and therefore security will be by contract. In addition, certain assets will require registration in a form as required by the relevant government or regulatory authority. Though counterparts are generally accepted, it is also advisable, based on judicial precedents, to encourage the signing parties to initial every page and clearly identify themselves and their authorities. In the case of corporate signatories, a company stamp should be affixed. Offshore entities will follow their own relevant execution requirements.

4 Financial Assistance

4.1 Are there prohibitions or restrictions on the ability of a company to guarantee and/or give security to support borrowings incurred to finance or refinance the direct or indirect acquisition of: (a) shares of the company; (b) shares of any company which directly or indirectly owns shares in the company; or (c) shares in a sister subsidiary?

Onshore

There are currently no express provisions regarding the restrictions on a company's ability to guarantee or give security to support the acquisition of itself, its parent, or its subsidiary company.

However, the CCL 2015 states that a PJSC or PrJSC or any of its subsidiaries "*may not provide financial aid to any shareholder to enable the shareholder to hold any shares, bonds or Sukuk issued by the company*" (Article 222). The definition of such financial aid includes any security, guarantee or providing company assets as security. On 28 April 2016, the UAE Ministry of Economy issued guidance, by way of Ministerial Resolution No. 272 of 2016, confirming that the financial prohibition will not apply to LLCs.

Offshore

The relevant rules and regulations of the applicable free zone would need to be reviewed to understand their position in respect of financial assistance, but typically parties tend to err on the side of caution in such matters.

By way of example, within the DIFC, a company limited by shares is prevented from providing financial assistance by granting security and providing guarantees by a company limited by shares in relation to the acquisition of shares in itself or in a holding company unless: (i) such assistance would not materially prejudice the interests of the company or its shareholders or the company's ability to discharge its liabilities as they fall due and must be approved by the shareholders (90% in share value); (ii) finance or financial assistance is part of the company's ordinary business and is on ordinary commercial terms; or (iii) it is specified in DIFC Company Regulations (2009) as exempt. However, in relation to point (iii), should such financial assistance not fall under these exemptions, companies may consider using DIFC-incorporated special purpose vehicles to provide financial assistance, if permitted by the DIFC Special Purpose Company Regulations.

5 Syndicated Lending/Agency/Trustee/Transfers

5.1 Will your jurisdiction recognise the role of an agent or trustee and allow the agent or trustee (rather than each lender acting separately) to enforce the loan documentation and collateral security and to apply the proceeds from the collateral to the claims of all the lenders?

The concept of 'trusts' and 'trustees' are more commonly referred to in the UAE as 'agent', 'security agent' or 'security trustee'. They are widely recognised concepts and often utilised in onshore, offshore (including DIFC) and Islamic finance structures. In Islamic transactions, if the deal is structured in compliance with *Shari'a*, the addition of an agent is not uncommon, in order for them to represent a group of lenders and protect their interests.

Further, as outlined in the response to question 3.6, onshore and offshore (including DIFC) entities in the region may require that a security agent is employed, particularly in the context of security which is granted in the region and can only be enforced by local institutions or entities that have specific licences. For example: (i) security over accounts – where a bank or financial institution should be the beneficiary of the security; and (ii) a lender who funds an organisation which has a teaching licence and is granted security by way of shares in itself – security can only be enforced over the shares if the lender itself has a teaching licence. Typically, this only becomes an issue upon enforcement; however, lenders should be mindful of this as it may affect the value they place on such types of security.

If a foreign lender is taking security over shares of an onshore entity, it may become difficult for them to enforce their security unless they are represented by a UAE national to ensure they do not contravene any ownership restrictions. This is not an issue for offshore entities for which 100% foreign ownership is permitted.

5.2 If an agent or trustee is not recognised in your jurisdiction, is an alternative mechanism available to achieve the effect referred to above which would allow one party to enforce claims on behalf of all the lenders so that individual lenders do not need to enforce their security separately?

Agency is recognised, and in the DIFC both agency and trustee roles are, as more fully described in the response to question 5.1.

5.3 Assume a loan is made to a company organised under the laws of your jurisdiction and guaranteed by a guarantor organised under the laws of your jurisdiction. If such loan is transferred by Lender A to Lender B, are there any special requirements necessary to make the loan and guarantee enforceable by Lender B?

The UAE is a relatively new financial centre, and the practitioners based here are keen to emulate a system as advanced as those established in the United Kingdom and the United States. Thus, many of the practices and customs for financing transactions (especially for certain advanced offshore entities, including the DIFC to a much larger degree) are similar to those utilised in the Western markets, albeit occasionally with an additional tier of Islamic structuring. Hence, similar to Western markets an amended and restated facility would typically be entered into and the guarantee would be reaffirmed with the new parties.

Nonetheless, the practices for onshore entities and certain free zones are often not as structured or stringent, and a simple side letter or amendment may suffice.

6 Withholding, Stamp and Other Taxes; Notarial and Other Costs

6.1 Are there any requirements to deduct or withhold tax from (a) interest payable on loans made to domestic or foreign lenders, or (b) the proceeds of a claim under a guarantee or the proceeds of enforcing security?

Whilst the UAE has tax laws, the governmental authorities do not currently impose corporate taxes on companies other than on branch offices of foreign banks and certain energy companies (e.g. oil, gas and petrochemical). However, a value-added tax ("VAT") regime of 5% is due to be introduced to the UAE on 1 January 2018 pursuant to Federal Decree Law No. 8 of 2017, (the "VAT Law"). The VAT Law is based on the principles contained in the Unified GCC Agreement for VAT, which was published in the Saudi Arabia Official Gazette in April 2017. Other GCC countries may implement the 5% VAT at the same time, or by 1 January 2019 at the latest. Companies with annual supplies in the UAE above AED 375,000 will have to register for VAT. If a company has annual supplies above AED 187,500, they can voluntarily register. VAT registration will be compulsory from the final quarter of 2017. Similar to Western markets, it is intended that if a company is engaged in the supply of goods or services that are subject to VAT (including at the zero rate), the company will be entitled to reclaim VAT that it incurs on its costs. Where the company is engaged in activities that are exempt from VAT and it cannot reclaim VAT incurred on costs, VAT will be a cost to its business (as suppliers will charge VAT that cannot be reclaimed). A number of regional experts have been unable to predict the impact the VAT introduction will have on economic growth, the outcome remains to be seen.

No withholding tax is currently payable in relation to principal, interest payments and other fees associated with the granting of loans. Currently, customs duties are typically very low, and personal income tax is not applicable; however, there are municipality service charges on individuals in the UAE by way of hotel and service (food) charges.

Various fees are payable for transferring property or land from one name to another (akin to stamp duty), registration and notarisation fees (see the response to question 3.9). Notably, no income tax regime is in place, which makes the region an attractive market for both individuals and corporations.

6.2 What tax incentives or other incentives are provided preferentially to foreign lenders? What taxes apply to foreign lenders with respect to their loans, mortgages or other security documents, either for the purposes of effectiveness or registration?

No preference is given to foreign lenders or financiers; however, the nil tax rate (subject to some exceptions as outlined in the response to question 6.1) is viewed as an incentive to invest in the region.

See the response to question 3.3 in respect of costs of registration. It should be noted that some free zones do not recognise the registration of security; hence the lenders have to rely on their contractual remedies in a default situation.

6.3 Will any income of a foreign lender become taxable in your jurisdiction solely because of a loan to or guarantee and/or grant of security from a company in your jurisdiction?

See the response to question 6.1.

6.4 Will there be any other significant costs which would be incurred by foreign lenders in the grant of such loan/guarantee/security, such as notarial fees, etc.?

Other than as outlined in the response to question 3.9, the costs to the lender are those that are imposed on them in their own jurisdiction of incorporation, if any.

Additionally, if a transaction is to be structured Islamically in accordance with the principles of *Shari'a*, this may also increase costs due to the document-heavy nature of such transactions and the need to involve *Shari'a* advisory boards.

6.5 Are there any adverse consequences to a company that is a borrower (such as under thin capitalisation principles) if some or all of the lenders are organised under the laws of a jurisdiction other than your own? Please disregard withholding tax concerns for purposes of this question.

No, there are not.

7 Judicial Enforcement

7.1 Will the courts in your jurisdiction recognise a governing law in a contract that is the law of another jurisdiction (a "foreign governing law")? Will courts in your jurisdiction enforce a contract that has a foreign governing law?

Onshore

Yes, both the UAE Civil Procedures Law (Federal Law No. 11 of 1992, as amended) (the "Civil Procedures Law"), and the Civil Transactions Law provide for the recognition of foreign governing law in contracts, provided that the conditions set out in the Civil Procedures Law are satisfied. However, if a UAE Court accepts jurisdiction, especially in an enforcement scenario where assets are located in the UAE, it may ignore the choice of foreign governing law in a contract and apply UAE law insofar as enforcement relates to the domicile of the parties, and the location of assets in the UAE. There are some claims where the parties cannot contract out of the application of UAE law, for example real estate disputes where the real estate is onshore in the UAE.

Offshore

In the DIFC, Article 6 of the DIFC Judicial Authority Law (Dubai Law No. 12 of 2004 (as amended)) provides that the DIFC Courts may apply the laws of another jurisdiction where the parties to a dispute have explicitly agreed that such laws shall govern a dispute between the parties, provided that such law does not conflict with the public policy and morals of the UAE.

7.2 Will the courts in your jurisdiction recognise and enforce a judgment given against a company in New York courts or English courts (a "foreign judgment") without re-examination of the merits of the case?

Onshore

The UAE Civil Procedures Law sets out in its Article 235 the basis upon which UAE Courts will recognise and enforce foreign judgments or orders.

Article 235 provides that a foreign judgment may be recognised and enforced if:

(i) the law of the country in which the judgment was issued would recognise and enforce a UAE Court judgment. This usually means that the two countries either have a bilateral treaty providing for recognition and enforcement of judgments. As neither the United States nor the United Kingdom have such treaties with the UAE, judgments would not be automatically enforceable without re-examination of the merits;

(ii) the UAE Courts have no grounds for jurisdiction to try the case in which the order or judgment was made;

(iii) the foreign court had jurisdiction in accordance with the rules governing international judicial jurisdiction within that country's own laws;

(iv) the parties to the action in which the foreign judgment was issued received proper notice;

(v) the judgment is final and not subject to appeal in the jurisdiction in which it was issued;

(vi) the judgment does not conflict with a judgment already made by a UAE Court; and

(vii) enforcement of the judgment does not conflict with the morals or public order of the UAE.

As a result, although a UAE Court may enforce a foreign judgment if it satisfies all of the conditions set out in Article 235, it is usually difficult for these requirements to be met. The fact that an applicant is seeking to enforce a judgment in the UAE implies that there is a nexus to the UAE in the factual circumstances underlying the case. On that basis, it is likely that a UAE Court may assert jurisdiction and reopen the merits of the case. A common pitfall for potential enforcement is to prove that the UAE Courts did not have jurisdiction to try the case, and even if all the other conditions set out in Article 235 are satisfied, the courts may refuse to enforce the foreign judgment on these grounds.

The UAE is signatory to many bilateral treaties and international conventions for the mutual recognition of judicial and arbitral awards.

Offshore

The DIFC Courts Law (DIFC Law No. 10 of 2004 (as amended)) provides the DIFC Courts with discretion to ratify judgments of foreign courts. The DIFC Courts Law also requires that the DIFC Courts abide by any mutual enforcement or judicial cooperation treaties entered into between the UAE and other countries. The DIFC Courts have entered into a Memorandum of Guidance with each of the United States District Court for the Southern District of New York, and the Commercial Court, Queen's Bench Division, England and Wales, Australia and Singapore (amongst others). These memoranda address only money judgments, are not legally binding, and set out guidelines to be followed by the respective jurisdictions when assessing whether to enforce the judgments of the courts of the other jurisdiction.

However, a decision in the DIFC could impact the manner in which foreign judgments are enforced onshore going forward. The DIFC Court of Appeal in the case of *DNB Bank ASA v Gulf Eyadah* [CA-007-2015] (25 February 2016) held that a foreign judgment which has been granted recognition in the DIFC Courts becomes a judgment of the DIFC Courts and therefore should be treated as such by the Dubai Courts (onshore Courts). This case involved the recognition of an English Commercial Court judgment in the DIFC Courts using the Memorandum of Guidance between the English Commercial Court, Queen's Bench Division, England and Wales and the DIFC Courts. There is also a system for enforcement between the DIFC Courts and the Dubai Courts (onshore) without review of the merits of the claim. This decision has therefore made apparent the potential for the DIFC Courts to be used as a "conduit" for an enforcement action in the Dubai Courts (onshore) against assets which are also onshore even where the parties have no connection with the DIFC. However, the practical effect of this decision will not be understood until the enforcement stage and there is currently no certainty as to how the Dubai Courts (onshore) would respond with respect to an enforcement action against assets if this process was followed. A subsequent DIFC Courts case of *Barclays Bank & Others v Essar Global Fund Limited* confirmed that where a claimant has received a foreign court judgment, it can be enforced against a Dubai-based party. This is done by virtue of the DIFC Courts acting as a conduit jurisdiction.

A further development has been the creation of the Judicial Committee under Dubai Decree No. 19 of 2016 forming the Judicial Committee of the Dubai Court and the DIFC Courts. The Decree came into immediate effect on 9 June 2016. The Judicial Committee has been created to resolve conflicts of jurisdiction between the DIFC Courts and Dubai Courts (onshore). The Judicial Committee determines any jurisdictional disputes between the Courts and also conflicting judgments of the DIFC and Dubai Courts (onshore) involving the same parties on the same subject matter. The Judicial Committee can also suggest rules and regulations to avoid jurisdictional conflicts arising. The Head of the Judicial Committee is the Chief Justice of the Court of Cassation in the Dubai Courts (onshore) and the other six members of the Judicial Committee are made up of judges from both the DIFC Courts and Dubai Courts (onshore). Where there is a conflict between the DIFC Courts and the Dubai Courts (onshore), either a party to the dispute or the public prosecutor can make a request for the Judicial Committee to decide which court should hear the case or, if there are conflicting judgments, rule on which judgment should be enforced. Once a case has been referred to the Judicial Committee both courts must stay proceedings, and the Judicial Committee's decisions will be binding and cannot be appealed.

7.3 Assuming a company is in payment default under a loan agreement or a guarantee agreement and has no legal defence to payment, approximately how long would it take for a foreign lender to (a) assuming the answer to question 7.1 is yes, file a suit against the company in a court in your jurisdiction, obtain a judgment, and enforce the judgment against the assets of the company, and (b) assuming the answer to question 7.2 is yes, enforce a foreign judgment in a court in your jurisdiction against the assets of the company?

Onshore

(i) Commencing an action for default is a relatively straightforward process. However, seeking a money judgment at the lower courts and enforcing such a judgment upon assets is usually a lengthy process that requires trying a case on the merits, and defending appeals if any are filed by an interested party. This process may in some instances, and depending upon the form of security and nature of the assets, take up to 24 months or even longer, even if there are no legitimate legal defences to non-payment.

(ii) The enforcement of a non-appealable judgment requires the filing of a separate "execution" case. Execution cases are subject to appeal. If the specific assets of the debtor in the UAE are undetermined, a series of inquiries with various UAE government authorities such as the land registries of the respective Emirate(s), the UAE Central Bank, the Securities and Commodities Authority, and the financial markets (the DFM and the ADX) must be made through the courts to identify assets. Real estate, securities, and (subject to the provisions of the New Pledge Law) certain moveable assets such as vehicles and machinery will be subject to a public auction process.

Offshore

The enforcement of a security interest over assets located in the DIFC does not require a court order. The DIFC Law of Security governs the creation and enforcement of security over collateral located in the DIFC. The secured party must first notify the defaulting party to make payment or otherwise discharge its obligation to the secured party. The secured party must also notify any other priority creditors of which it is aware. If there is no objection by a priority secured creditor, the secured party may take steps to enforce its security interest over assets located within the DIFC. If the collateral is real property located within the DIFC, the secured party may record with the DIFC Security Registrar a written statement that a default has occurred and that the secured party is entitled to enforce the security interest.

7.4 With respect to enforcing collateral security, are there any significant restrictions which may impact the timing and value of enforcement, such as (a) a requirement for a public auction, or (b) regulatory consents?

Yes.

(i) Whilst enforcement of security previously required a court order, the New Pledge Law also introduces the concept of self-help remedies in relation to certain types of security (for example, secured bank accounts and bonds or endorsable instruments). Articles 28 to 33 of the New Pledge Law provide additional mechanisms that will allow the secured party to enforce its security without recourse to a public auction through the courts. The court does, however, have the right to choose the method of sale or to stipulate a minimum limit to the sale price. Certain collateral that does not fall within the parameters of the New Pledge Law, such as real estate and shares, must be liquidated through a public auction procedure in accordance with the UAE Civil Procedures Law.

(ii) The attachment and liquidation of publicly listed securities must be conducted in accordance with the procedures prescribed by the UAE Securities and Commodities Authority.

In relation to the enforcement of collateral security in the DIFC, see the response to question 7.3.

7.5 Do restrictions apply to foreign lenders in the event of (a) filing suit against a company in your jurisdiction, or (b) foreclosure on collateral security?

There are no foreign lender-specific restrictions relating to filing suit against a company in the UAE or initiating security enforcement proceedings in the UAE.

7.6 Do the bankruptcy, reorganisation or similar laws in your jurisdiction provide for any kind of moratorium on enforcement of lender claims? If so, does the moratorium apply to the enforcement of collateral security?

Onshore

On 29 December 2016, the long-awaited New Bankruptcy Law came into effect. The new law introduces a protective composition process (where the debtor is in financial difficulty but not insolvent) and a restructuring scheme (as part of bankruptcy procedure), both of which are court-driven processes. Once the court has agreed to initiate proceedings for either the protective composition or the restructuring scheme, a moratorium applies to prevent claims against the creditors. Secured creditors will thereafter have to obtain the court's permission to commence enforcement proceedings.

Offshore

The DIFC's Insolvency Law (DIFC Law No. 3 of 2009) governs insolvency proceedings in the DIFC. The Insolvency Law allows the DIFC Courts to grant a moratorium, including in relation to the enforcement of collateral, to an eligible applicant (see question 1.1).

7.7 Will the courts in your jurisdiction recognise and enforce an arbitral award given against the company without re-examination of the merits?

Onshore

Article 236 of the UAE Civil Transactions Law stipulates that the same conditions set out in Article 235 for the enforcement of foreign judgments are applicable to foreign arbitral awards, which are set out in the response to question 7.2. The UAE is also a signatory to the Convention on the Recognition and Enforcement of Foreign Arbitral awards (New York, 1958), as well as other bilateral treaties and Conventions dealing with the mutual recognition of arbitral awards.

Offshore

In the DIFC, an arbitral award, irrespective of the jurisdiction in which it was made, is recognised as binding within the DIFC and upon application to the DIFC Court, is enforceable. A party may challenge enforcement under certain circumstances including when: a party to an arbitration was under some type of incapacity; the underlying arbitration agreement is invalid under the laws which the parties have subjected it to; the party against whom an award was granted was not provided with proper notice; the dispute in relation to which the award was granted falls outside the scope of issues contemplated by the parties to be submitted to arbitration; the composition of the arbitral tribunal or the arbitration procedures was inconsistent with the agreement of the parties or laws of the jurisdiction in which the arbitration took place; the award is not yet binding or has been suspended by a court of the jurisdiction in which it was made; the subject matter of the underlying dispute would not have been capable of settlement by arbitration under the laws of the DIFC; or if enforcement would be contrary to public policy in the UAE.

Where the UAE has entered into a mutual enforcement of judgments treaty, the DIFC Courts (as a Court of Dubai) will uphold the terms of the treaty.

8 Bankruptcy Proceedings

8.1 How does a bankruptcy proceeding in respect of a company affect the ability of a lender to enforce its rights as a secured party over the collateral security?

Onshore

Enforcement actions over secured assets prior to the initiation of the protective composition or restructuring scheme (or the issuance of a bankruptcy judgment) are permissible if: (i) the underlying debts are due; and (ii) the court approves such enforcement. However, once the court has approved the composition or the plan, the trustee becomes entrusted with the sale of assets in line with the restructuring plan. The New Bankruptcy Law clarifies that sale proceedings must be used first to prepay the debts due to secured creditors. However, if a secured asset is essential to the continuance of the business, the court may provide that the secured assets be substituted with other assets, provided that it does not prejudice the rights or interests of the secured creditors.

Should the preventive composition or restructuring scheme prove unsuccessful and the debtor is declared bankrupt, all debts become due and the debtor's assets must be sold in order to repay the secured creditors. If the sale does not occur within one month from the date of the bankruptcy judgment, the secured creditor may request to approve the enforcement over the secured assets.

Offshore

In the DIFC, the Insolvency Law allows the DIFC Courts to grant a moratorium, including in relation to the enforcement of collateral, to an eligible applicant.

Dubai World – Decree 57

The Special Tribunal related to Dubai World ("Tribunal") was established by Dubai Decree No. 57 of 2009 issued by His Highness Sheikh Mohammed Bin Rashid Al Maktoum, in his capacity as the Ruler of Dubai. The Tribunal was established to hear claims against Dubai World, a Dubai Government-owned holding company, and its subsidiaries. The Tribunal was established following Dubai World's November 2009 announcement of its intention to seek the rescheduling of its debt obligations. The Tribunal applies the DIFC's Insolvency Laws and, as such, allows the granting of moratoria including in relation to the enforcement of collateral.

8.2 Are there any preference periods, clawback rights or other preferential creditors' rights (e.g., tax debts, employees' claims) with respect to the security?

Yes. Secured creditors will have priority to be paid from the proceeds of the liquidation of the subject assets. It should be noted that the New Pledge Law provides that the date and time of recording the pledge in the Security Register will be effective as against all parties and seek to establish priority *vis-à-vis* competing creditors.

Following payment to secured creditors, costs and expenses incurred in respect of the liquidation process will be payable, prior to unpaid end of service gratuity, wages and salaries of employees of the debtor.

In the DIFC, the Law of Security ranks conflicting perfected security interests according to priority in time of perfection. The Law of Security grants perfected security interest priority over a conflicting, unperfected security interest, and provides for priority of the first security interest to attach if conflicting security interests are unperfected.

8.3 Are there any entities that are excluded from bankruptcy proceedings and, if so, what is the applicable legislation?

The New Bankruptcy Law applies to all commercial companies (except for certain financial free zones), traders/merchants and civil partnerships (set up in accordance with the Civil Transactions Law). Individuals remain outside the scope of the New Bankruptcy Law.

In the DIFC, the Insolvency Law applies to any company that falls under the jurisdiction of the DIFC and has been incorporated pursuant to the DIFC Companies Law (DIFC Law No. 2 of 2009 (as amended)).

8.4 Are there any processes other than court proceedings that are available to a creditor to seize the assets of a company in an enforcement?

As mentioned in the response to question 7.4, the New Pledge Law introduces the concept of self-help remedies in relation to certain types of security. The direct enforcement of moveable assets is generally permissible by private sale, subject to prior agreement, notification by relevant parties and no other security interest existing. A pledge over claims and receivables may be set off if the pledgee is a bank, and by claim if the account is held at another bank. Bonds and certain written instruments may be directly enforced through delivery or endorsement if their value is equal to the right of pledge, while written papers (e.g. bills of lading) may be directly enforced by application to the summary judge for the issuance of an urgent order.

In order to initiate direct enforcement, the pledgee must notify all concerned parties. There is currently no time limit for such notice. The New Pledge Law also grants authority to summary judges to issue orders for enforcement of a registered pledge.

In the DIFC, a secured party may take steps to enforce its security interest over assets located within the DIFC without a court order.

9 Jurisdiction and Waiver of Immunity

9.1 Is a party's submission to a foreign jurisdiction legally binding and enforceable under the laws of your jurisdiction?

Yes. However, if there are grounds for a UAE Court to assert jurisdiction, the UAE Courts are likely to do so. See the responses to questions 7.1 and 7.2 for more background on this topic.

9.2 Is a party's waiver of sovereign immunity legally binding and enforceable under the laws of your jurisdiction?

There are no laws in the UAE specifically addressing the issue of waiver of sovereign immunity. The UAE Courts may consider a variety of factors, including public policy issues, before accepting jurisdiction in a case involving a foreign sovereign government or government entity. Insofar as the Federal and local governments of the UAE are concerned, the Civil Procedures Law contains a prohibition on the seizure of "public property" belonging to the UAE Federal Government or the governments of any of the individual Emirates to satisfy a judgment debt.

Some Emirates may also require written consent, and approval of the respective Emirate's Ruler's court or legal department are obtained prior to the filing of a claim against an Emirate's Ruler, government, or government entity. For example, in the Emirate of Dubai, the Dubai Government Lawsuits Law (Dubai Law No. 3 of 1996, as amended) requires the prior approval of the Ruler of Dubai before filing a lawsuit against the Ruler or a Dubai Government entity. Article 3*bis* explicitly states that no debt or financial obligation against the Ruler or the Government may be collected by means of detainment, public auction sale or possession by any other legal procedures of the properties and assets of the Ruler or of the Government, whether such debt or financial obligation has received a final and conclusive judgment or not. The requests for such approvals must be made to the Dubai Government's legal department.

10 Licensing

10.1 What are the licensing and other eligibility requirements in your jurisdiction for lenders to a company in your jurisdiction, if any? Are these licensing and eligibility requirements different for a "foreign" lender (i.e. a lender that is not located in your jurisdiction)? In connection with any such requirements, is a distinction made under the laws of your jurisdiction between a lender that is a bank *versus* a lender that is a non-bank? If there are such requirements in your jurisdiction, what are the consequences for a lender that has not satisfied such requirements but has nonetheless made a loan to a company in your jurisdiction? What are the licensing and other eligibility requirements in your jurisdiction for an agent under a syndicated facility for lenders to a company in your jurisdiction?

Onshore

Licensing requirements in the UAE:

The Central Bank and the Securities and Commodities Authority ("SCA", also known as "ESCA") are the main regulatory bodies for financial services in the UAE. Pursuant to Federal Law No. 10 of 1980 (the "Banking Law"), the Central Bank regulates the financial institutions, including those who wish to provide financing in or from the UAE.

Whilst there are no local licensing requirements for foreign lenders which lend to UAE companies, if such entity wishes to be based in the UAE, it must be appropriately licensed. UAE lenders including commercial banks, investment banks, investment companies, finance companies, Islamic banks, Islamic finance companies and real estate finance companies based in the UAE are regulated by the Central Bank and require a licence. Each of the institutions listed above must be 51% owned by a UAE national if incorporated in the UAE; however, for finance companies, commercial banks and investment banks, the minimum UAE national shareholding is 60%. Branches of foreign banks can also be licensed as commercial banks in the UAE.

In order to obtain a licence from the Central Bank, a letter of application, certain corporate documents of the applicant and a business plan are submitted to the Central Bank. The specific documents required for the licence are not listed by the Central Bank but the applicant should expect to be notified if additional documents are necessary for the process to be finalised.

UAE lenders who enter into financial arrangements with a borrower in the UAE without a licence may face imprisonment for up to three months and/or be fined up to AED 2,000. Additionally, the institution may be liable for civil and criminal claims.

Additionally, an agent for a syndicate of foreign lenders is also not required to be licensed unless it is operating from and based in the UAE. Please note the requirements in respect of local agents relating to security as addressed in sections 3 and 5.

Offshore

Licensing requirements in the DIFC:

The principal regulator for regulating financial services within the DIFC is the Dubai Financial Services Authority ("DFSA"). An individual or entity based in the DIFC which provides a financial service must be authorised by the DFSA by obtaining the appropriate licence. If both the lender and the borrower are based in the DIFC, a Category 2 licence must be obtained, whereas if the lender is foreign, providing a credit facility to a borrower in the DIFC, licensing requirements do not exist.

An entity who wishes to satisfy the eligibility requirements in the DIFC must be structured as any one of the following forms of business: limited liability company; company limited by shares; limited liability partnerships; protected cell company; investment company; branch of foreign company or partnership; or special purpose company.

The consequences of licensing violations can be severe. If a lender does not satisfy the requirements, DFSA, under the Regulatory Law and DFSA's Enforcement (ENF) Rulebook, can enforce the following actions as punishment: a fine of US$100,000 per contravention; damages or restitution; injunctions and restraining orders; corporate penalties – unlimited fines through the Financial Markets Tribunal (the FMT); and a banning order through the FMT. As a consequence of violating the Financial Services Prohibition section of the Regulatory Law, lenders will also face censure by way of publication of any enforcement action leading to critical reputational damage and the loan agreement will be considered unenforceable.

11 Other Matters

11.1 Are there any other material considerations which should be taken into account by lenders when participating in financings in your jurisdiction?

The UAE banking market is still relatively young, and whilst there is extreme wealth and numerous opportunities in the region, obligors or borrowers may often be limited in the types of transactions and financings they can enter into, particularly in cases where the relevant funding transaction is highly structured and involves the issuance of debt securities. Nonetheless, the New Pledge Law, although untested, should attract more foreign investment to the region and instil more confidence in lenders, as the once grey area of taking security onshore should now be more akin to more developed jurisdictions' security perfection regimes in protecting lenders' interests.

Further, limitations arise when the relevant financiers and/or borrowers are *Shari'a*-compliant. However, most of the major international lenders now have their own Islamic banking desks and many retain *Shari'a* advisory boards. Such institutions are growing more comfortable with the main Islamic financing mechanisms, and view Islamic finance assets, which are forecast to reach US$3.2 trillion by 2020, as an area of major opportunity and growth notwithstanding the additional costs.

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1 Overview

1.1 What are the main trends/significant developments in the lending markets in your jurisdiction?

The corporate lending markets in the United States are broad and deep. Market trends are often associated with certain segments of the lending markets, and market segmentation in the United States is based on a number of factors. These factors include: the size of the borrower (from so-called "large-cap" borrowers, to those in the "middle-market" to "small-cap"); the credit profile of the borrower (from investment-grade to below investment-grade or "leveraged"); the type of lender (banks, *versus* non-bank lenders, please see the discussion regarding "Alternative Lenders" below); the number of holders of the debt (from syndicated loans, to "club" and bilateral facilities); whether the loan is secured, and the relative positions of the lenders *vis-à-vis* one another (from senior unsecured, to senior secured, mezzanine and second-lien loans); the basis on which the loan is made and repayment is (hopefully) assured (from a company's general credit rating, to cash flow loans, to asset-based loans); and the purpose of the loans (from acquisition finance, asset finance, to general working capital loans, to the development of specific projects). While there are trends within each of these market segments, there are also some broad trends which impact multiple segments. For example:

Rising Interest Rates. After keeping interest rates low for many years, the Federal Reserve reversed course by raising interest rates in late 2015 (the first increase since the start of the financial crisis in the United States) and again raising interest rates in late 2016. The Federal Reserve had kept interest rates low during and after the financial crisis in an effort to strengthen economic growth and curb unemployment by making it cheaper for companies to borrow. This low interest rate environment contributed to a borrower-friendly market: lower rates and higher leverage levels, with lenders and loan investors seeing lower yields and weaker covenants and structures. Improving economic conditions in the United States, including a considerable improvement in the labour market since prerecession levels and continued overall growth in the United States economy, led the Federal Reserve to start raising short-term interest rates in December of 2015, with an initial increase in the benchmark interest rate by 0.25 percentage points and then another such increase in December of 2016 by 0.25 percentage points. The Federal Reserve continued this trend throughout 2017, raising the benchmark interest rate by 0.25 percentage point increments in March, June, and December of 2017. Short-term rate increases are expected to continue through 2018. Such interest rate moves by the Federal Reserve suggest a gradual decline of the "easy-money" conditions that resulted from the United States financial crisis.

Certain Trends in Loan Documentation. One of the most vibrant and innovative segments of the loan markets in the US is the fast-paced leveraged loan market. "What is market" on a variety of points, including leverage levels, spreads and covenants changes from month-to-month. Drivers of these changes include the demands of determined and resourceful borrowers and sponsors, the ebb and flow of the demand for leveraged loans, ambitions to command greater market share, due regard for credit risk and the other factors described below. Some broader trends in the market in recent years can be identified.

Convergence. The same investors often invest in leveraged loans and high-yield bonds. Leveraged loans typically have more restrictive covenants than high-yield bonds (although the gap has narrowed substantially) and are generally secured, so recoveries on leveraged loans after default are generally better. Investors judge the relative values of each of these instruments on a company-by-company basis. With each of these asset classes "competing" with the other, over the years many leveraged loans have taken on more bond-like characteristics, including incurrence-based covenants, no caps on dispositions, and greater flexibility for restricted payments.

Covenant-Lite Loans. When demand for leveraged loans is high (and borrowers have more leverage in negotiations) the trend is toward "looser" bond-like covenants, otherwise known as "covenant-lite". In covenant-lite loans, the borrower generally pays a premium in exchange for less restrictive covenants and no financial maintenance covenants (similar to high-yield bonds). While financial maintenance covenants test the borrower on a periodic basis, covenant-lite loan agreements typically only include "incurrence" covenants (which test the borrower upon a specific activity such as the incurrence of liens or debt, the making of acquisitions or restricted payments, etc.). Covenant-lite loans are viewed as having a greater risk of loss after default; with a covenant-lite loan, the first default is often a payment default, occurring long after a financial covenant default would have occurred. By that time, the borrower's financial condition is likely to have deteriorated substantially. Covenant-lite loans were popular before the financial crisis, dried up during the crisis and its aftermath, but have made a comeback in recent years and are now seen with greater frequency in middle market deals. In the third-quarter of 2017, according to Moody's Investors Service, the overall covenant quality of leveraged loans in the United States decreased to the weakest levels on record, due to increased investor demand during 2017 for leveraged loans.

The Power of Equity Sponsors. Equity sponsors drive much of the volume of leveraged loans and continue to exercise their market power and push the market towards more borrower-favourable terms. "SunGard" provisions continue to be standard in commitment papers. SunGard provisions allow equity sponsors who require acquisition financing to compete with strategic buyers who do not need such financing, by aligning closely the conditions in financing commitments to the conditions in the acquisition agreement. Equity sponsors increasingly require loan arrangers to use the sponsor's form of commitment letter so the sponsor can more easily compare the proposals of different financing sources. It has also become common for sponsors to prepare initial drafts of loan documentation. But perhaps no development is more controversial than sponsors "designating" acceptable counsel for arrangers and lenders. As discussed in more detail below, increased regulatory pressure in recent years has made it more difficult for bank lenders to make and hold highly leveraged loans and such regulatory pressure, when combined with other factors, has created a market environment in which lenders began to see somewhat increased leverage in loan documentation negotiation with equity sponsors. However, with non-bank lenders increasingly replacing bank lenders (as discussed below) combined with high demand for leveraged loans in 2017, many equity sponsors remained successful during 2017 in negotiating for borrower-friendly provisions in loan documents, including continuing to negotiate for middle-market borrowers to have the benefit of less restrictive loan document provisions which had previously only been offered by the market to large-cap borrowers.

The Borrower's Desire for Flexibility: Unrestricted Subsidiaries, Equity Cures, Builder Baskets, Incremental Facilities and Reclassification. Equity sponsors and borrowers desire flexibility in their financing documents. This comes in many forms. The "unrestricted subsidiary" concept is consistent with features seen in bond indentures and this feature has become common in leveraged loan documentation. These provisions exclude specified subsidiaries from coverage in the representations, covenants and events of default, thus allowing a borrower to use an unrestricted subsidiary to incur indebtedness and liens or make investments without being subject to loan agreement restrictions. In effect, the lender loses the ability to monitor or restrict the unrestricted subsidiaries. A trade-off is that financial attributes of the unrestricted subsidiaries are excluded from the loan agreement provisions (including any benefit the borrower may have otherwise realised from cash flow generated by such subsidiaries for purposes of loan agreement financial ratios). "Equity cures" remain common. An equity cure allows a borrower's shareholders to make an additional equity investment in the borrower to cure breaches of its financial covenants. Loan agreements also continue to give borrowers more flexibility around so-called "builder baskets" which provide the borrower with more alternatives for using its excess cash flow. Typically, borrowers are permitted to use builder baskets for capital expenditures, permitted investments and acquisitions, and sometimes for equity distributions and repayment of subordinated debt (subject to leverage governors). Non-committed incremental facilities also remain common fare in loan agreements, permitting in an increasing number of cases (and now even in certain middle-market credit facilities) an uncapped amount of additional debt, so long as certain *pro forma* leverage ratios are satisfied. Borrowers are also requesting the ability to first utilise fixed dollar baskets in the context of certain negative covenants (for instance, debt, lien, investment and restricted payment negative covenants) and, if the borrower's financial condition later improves, to subsequently reclassify amounts incurred or paid under a fixed dollar basket such that these amounts are deemed incurred or paid under a leverage-based basket instead. The result of such a reclassification is that the borrower's fixed dollar basket for a negative covenant is then freed-up, so that the borrower can then incur or pay additional amounts under the fixed dollar basket, even if the borrower's financial performance should subsequently decline.

The Regulatory Environment. While the Federal Reserve kept interest rates low to boost economic activity, other federal regulators with a mandate to protect the US economy from excessive risk-taking associated with the financial crisis have helped push the needle in the opposite direction by increasing the cost of making loans. For example, the "Guidance on Leveraged Lending" issued by federal regulators, and which became effective in May 2013, applies to all federally supervised financial institutions that are substantively engaged in leveraged lending activities. The guidance outlines high level principles to assist institutions in establishing safe and sound leveraged finance activities and increases lending costs as lenders re-evaluate their internal policies and programs and tighten their underwriting standards. "Risk retention rules" and the "Volcker Rule" impact CLO managers and banks that structure, warehouse and make markets in CLOs. The final Volcker Rule was released on December 10, 2013, and limits certain investing and trading operations of banking entities. In addition, banking entities engaged in permitted fund activities and permitted trading will be required to create extensive compliance programs and meet new reporting requirements. Although the Federal Reserve extended the Volcker compliance period to July 2017, the new reporting requirements became effective in June 2014. The foregoing, combined with CLO capital requirements under Basel III, had a chilling effect on CLO issuances in the United States, with CLO issuance declining through 2016. This trend reversed in 2017, with a substantial increase in CLO issuance, nearly matching the record-setting levels of 2014. The new Republican administration has generally indicated that it will loosen various federal regulations that curbed the participation by CLOs and traditional bank lenders in the United States loan markets from 2014 through 2016, and while it remains not entirely certain at the time of the writing of this article to what degree all such regulations will be rolled-back, US regulators have indicated that they will be more lenient in 2018 with traditional banks in connection with leveraged lending activities.

Sanctions and Anti-Corruption Laws. Federal regulators have in recent years increased their enforcement of sanctions, anti-terrorism and anti-corruption laws, meting out record fines. In addition to being more strident in their due diligence of borrowers, lenders are requiring stronger provisions in loan agreements to try and address these issues (and to demonstrate to regulators that they are doing the same). These provisions typically require the borrower and its affiliates to comply with sanctions regulations enacted by the US and other applicable authorities, to not use any borrowed proceeds in restricted countries or in doing business with restricted entities, and to comply with and have policies to comply with anti-bribery laws. Borrowers sometimes attempt to negotiate these provisions, including by adding materiality or knowledge qualifiers, with some limited success.

Federal Income Taxes. The Foreign Account Tax Compliance Act ("FATCA"), which became effective with respect to interest payments on July 1, 2014, was a major revamp of the US withholding tax regime. FATCA imposes a 30% gross withholding tax on certain amounts, including interest and, effective January 1, 2019, principal, paid by US borrowers to a foreign lender unless that lender (i) enters into an agreement with the IRS to identify and report specified information with respect to its US account holders and investors, or (ii) is resident in a jurisdiction that has entered into an intergovernmental agreement (an "IGA") with the United States pursuant to which the government of that jurisdiction agrees to report similar information to the United States. This sweeping law has a potentially significant impact on loan payments and receipts where it applies and has prompted loan parties to manage FATCA risk (express allocation of risk set forth in loan documentation, operation of gross-up clauses, etc.). In the US loan market, for example, loan agreements now almost universally contain provisions whereby any FATCA withholding is exempt from a borrower's gross-up obligation, and a borrower may request information from a lender to determine whether such lender is in compliance with FATCA.

Moreover, the Tax Cuts and Jobs Act of 2017 (the "2017 Act") enacted sweeping changes to the Internal Revenue Code of 1986, as amended (the "Code"), including numerous provisions that may impact the US federal income tax treatment of participants in the US lending markets. Many of the provisions in the 2017 Act may be the subject of regulatory clarification as to their scope and import.

Continued Innovations and Ongoing Trends in the Loan Markets. Given the depth and breadth in the loan markets in the US, many loan market innovations originate or are further developed here (consider, for example, the development of a sophisticated secondary trading market, certain mezzanine and second-lien structures, the securitisation of loans and CLOs). Some innovations include the following:

The Unitranche Facility. One innovation that continued to remain popular in 2017 (and which is now firmly established in middle-market lending in the United States and is also now much more prevalent in European markets) is the so-called "unitranche" facility. Unitranche loans combine what would otherwise be separate first/second-lien or senior/mezzanine facilities into a single debt instrument, where all the debt is subject to the same terms, and with a blended interest rate. Lenders in unitranche facilities typically enter into a so-called "agreement among lenders" ("AAL") which legislates payment priorities among lenders in a manner that may not be visible to the borrower. One advantage of unitranche loans for a borrower is speed and certainty of closing (important in a competitive acquisition process), since negotiation of an intercreditor agreement is not a condition to funding. Another advantage for the borrower is the simplicity of decision-making during the life of the loan since there is no "class voting" from the perspective of the borrower (though the AAL may impact voting issues in ways not visible to the borrower). The use of these facilities has so far been restricted to the middle-market, and lenders of unitranche loans are typically finance companies and hedge funds (and not banks). In 2017, the United States loan markets continued to see increased complexity in unitranche structures and in the terms of AALs. Borrowers and their equity sponsors have had some success in requiring disclosure of terms of AALs, especially with respect to voting, and in some instances the borrower now executes the AAL by signing an acknowledgment to the document. The United States Bankruptcy Court for the District of Delaware implicitly recognised the court's ability to construe and enforce the provisions of an AAL (to which the borrower is not a party) in March 2015 in the *In re RadioShack Corp.* bankruptcy, positively signalling to lenders that AALs should be enforceable in bankruptcy.

Bank Lenders Versus Alternative Lenders. The Guidance on Leveraged Lending has curbed the leveraged lending activities of traditional banks in recent years (but as indicated above, at the time of the writing of this article, US regulators have indicated that they are open to loosening restrictions, or at least the enforcement thereof, with respect to leveraged lending by traditional banks). At the same time, it helped to open the door wider for non-bank lenders (commonly known as "Alterative Lenders") to become a "go to" source of capital for equity sponsors and borrowers in the leveraged-lending markets, especially for middle-market borrowers, given that such Alternative Lenders are not subject to the same regulatory constraints. Alternative Lenders are typically speciality finance companies, organised as business development companies ("BDCs") or funds, and also include the "direct lending" business of large alternative asset managers. Alternative Lenders have greater flexibility than banks to hold leveraged loans on their balance sheets, which provides borrowers with greater deal certainty, since Alternative Lenders, unlike banks, may not need to condition deal terms based on their ability to syndicate a loan. Alternative Lenders also often invest at different levels of a borrower's capital structure, such as by making an equity investment at the same time as providing a credit facility, which provides added benefit to equity sponsors and borrowers seeking to raise capital. Alternative Lenders appear to be winning the battle with traditional banks for market share, especially in the middle-market leveraged lending space. However, some market participants point out that the relationship is actually more symbiotic in nature; for example, banks provide debt financing to Alternative Lenders and underwrite equity issuances by Alternative Lenders and also have analysis that "follow" equity of BDCs.

Litigation Finance. While more commonplace in countries such as Australia, the business of litigation finance has gained traction in the United States and is growing rapidly. A common type of litigation finance occurs when a third party investor provides funds to a plaintiff (or plaintiff's attorney) in exchange for a contractual commitment to receive a share of the award or settlement (or contingency fee) resulting from litigation. Such financing is typically limited recourse, and the investor is only repaid if the plaintiff (or plaintiff's attorney) wins an award, though investors can realise significant returns, usually a multiple of their initial investment. Litigation finance has its share of critics, including those who characterise such finance as "turning the court system into a stock exchange". Other legal observers argue litigation finance helps to "level the playing field" when parties in litigation have unequal financial or bargaining positions. In recent years, established financial institutions and new investment firms have raised hundreds of millions of dollars to invest in litigation finance and the US market will likely see an increase in this form of financing in the future.

1.2 What are some significant lending transactions that have taken place in your jurisdiction in recent years?

Given the large number of transactions in the US corporate loan markets, it is difficult to differentiate certain lending transactions as being more significant than others. Any such comparison necessarily excludes transactions for which documentation is not publicly available and therefore favours large corporate deals filed with the SEC compared to those in the middle-market, where much loan product innovation takes place. Nevertheless, some transactions that illustrate some of the concepts discussed above include: *Covenant-Lite*: The Sherwin-Williams Company (September 11, 2017) and Columbus McKinnon Corporation (January 31, 2017); *Equity Cures*: Ulta Salon, Cosmetics & Fragrance, Inc. (August 23, 2017) and AP Gaming I, LLC (June 6, 2017); *Builder Baskets*: Blue Bird Body Company (December 12, 2016) and Revlon Consumer Products Corporation (September 7, 2016); *Unrestricted Subsidiaries*: Michaels Stores, Inc. (May 27, 2016) and Claire's Stores, Inc. (September 20, 2016); *Incremental Facilities*: Golden Entertainment, Inc. (October 20, 2017) and Dave & Buster's, Inc. (August 17, 2017); and *Reclassification:* AdvancePierre Foods, Inc. (June 2, 2016) and Ball Corporation (March 18, 2016).

2 Guarantees

2.1 Can a company guarantee borrowings of one or more other members of its corporate group (see below for questions relating to fraudulent transfer/financial assistance)?

Generally, yes. In the US, guarantees are commonly referred to as one of three types: (a) "downstream" guarantees, whereby a parent company guarantees the debt of a subsidiary; (b) "upstream" guarantees, whereby a subsidiary guarantees the debt of a parent; and

(c) "cross-stream" guarantees, whereby a subsidiary guarantees the debt of a "sister company". Generally, "upstream" and "cross-stream" guarantees may be subject to increased scrutiny given enforceability issues in the context of a bankruptcy, as further described below.

2.2 Are there enforceability or other concerns (such as director liability) if only a disproportionately small (or no) benefit to the guaranteeing/securing company can be shown?

First, as a matter of contract law, some "consideration" (bargained-for contractual benefit to the guarantor) must be received for the guarantee to be enforceable, though this contract law threshold is typically easy to meet.

As a matter of insolvency law, certain types of enforceability issues arise in the context of a bankruptcy. These issues are analogous to, but not the same as, contractual concepts of "consideration". With downstream guarantees, there is typically little concern, since the parent will indirectly realise the benefit of a loan through the value of its equity ownership of the subsidiary (unless the subsidiary is already, or is rendered, insolvent). However, "upstream" and "cross-stream" guarantees should be subject to increased analysis since the benefit to the guarantor is less evident.

For example, a guarantee or other transaction may be voided by a bankruptcy court in the US if it is found to be a "fraudulent transfer". Very generally, under the federal Bankruptcy Code, a guarantee may be considered a fraudulent transfer if, at the time the guarantee is provided, (a) the guarantor is insolvent (or would be rendered insolvent by the guarantee), and (b) the guarantor receives "less than reasonably equivalent value" for the guarantee. (Note that both prongs of the test must occur in order for the guarantee to be voided as a fraudulent transfer; if the guarantor receives "less than reasonably equivalent value" though is nevertheless solvent at the time the guarantee is provided (after giving effect to the guarantee), then the guarantee should not be voided as a fraudulent transfer.) As mentioned above, in a downstream guarantee context, the parent would more likely receive "reasonably equivalent value", therefore fraudulent transfer is less of a concern for these types of guarantees. In addition to the federal Bankruptcy Code fraudulent transfer test, under state laws there exist similar fraudulent transfer statutes and a federal bankruptcy trustee may also use these tests to void the guarantee in a bankruptcy.

Loan documentation will often provide for solvency representations from borrowers and guarantors in order to address fraudulent transfer concerns. In some high-risk transactions (such as acquisition loans or loans provided so the borrower can make a distribution to shareholders), a third party is required to provide a solvency opinion in order to provide protection from fraudulent transfer attack, though the more common practice today is for lenders to do their own analysis given the expense of such outside opinions.

Under relevant corporate law, if a guarantee or similar transaction is structured in such a way that it would be tantamount to a distribution of equity by a company while the company is insolvent (or is rendered insolvent), or would impair the company's capital, the transaction may be improper under the corporate law and could result in director liability. See also question 2.3 below for a general discussion of corporate power issues.

2.3 Is lack of corporate power an issue?

Entity power to enter into a guarantee is generally governed by the corporation (or equivalent) law in the state in which the company is organised, as well as the company's charter and bylaws (or equivalent documentation).

For corporations, the corporation law of most states provides a broad range of permitted business activities, so few activities are considered to be *ultra vires* or beyond the power of a corporation (note that certain special purpose or regulated entities, such as banks, insurance companies, and utility companies, may be subject to additional statutes which impact corporate power). In a lending context, however, many state corporation statutes limit the power of subsidiaries to guarantee the indebtedness of a corporate parent or a sister company, and a guarantee may be *ultra vires* if not in furtherance of the guarantor's purposes, requiring analysis of the purpose of the guarantee and the benefit to the guarantor. If the benefit to the guarantor is intangible or not readily apparent, this may provide additional concern. Many corporate power statutes, however, provide safe harbours for certain types of guarantees, irrespective of corporate benefit, including if the guarantor and the borrower are part of the same wholly owned corporate family, or if the guarantee is approved by a specified shareholder vote, for the guarantor entity. For limited liability companies, state statutes are usually more generous, with a limited liability company generally able to engage in any type of legal activity, including entering into guarantees, unless the charter provides otherwise.

In lending transactions in the US, the analysis that a company has the corporate or other requisite power to enter into a guarantee is often provided in a legal opinion provided by the guarantor's internal or external counsel (though these opinions will typically assume away the tough factual issues, such as the level of corporate benefit).

2.4 Are any governmental or other consents or filings, or other formalities (such as shareholder approval), required?

In addition to having "corporate power" (or equivalent power for other types of entities) to enter into a guarantee, the guarantee must be properly authorised, which generally means that the procedural rules of the corporation, as set forth in its charter or by-laws, must be followed and that the stockholders or the governing board take the proper measures to authorise the transaction. These procedures are customary and also typically covered in a legal opinion provided by the guarantor's counsel.

One situation that requires special attention in a guarantee context is when a guarantor is providing an upstream or cross-stream guarantee, and the guarantor has minority shareholders. In this context, often the consent of the minority shareholders would be required in order for the guarantee to be provided in order to address fiduciary duty concerns.

Generally, no governmental consents, filings or other formalities are required in connection with guarantees (though, as noted above, certain special purpose companies and regulated entities may be subject to additional requirements).

2.5 Are net worth, solvency or similar limitations imposed on the amount of a guarantee?

Yes, please see question 2.2.

2.6 Are there any exchange control or similar obstacles to enforcement of a guarantee?

Generally, no. Though there are a few other issues worth mentioning that do not relate to "enforcement" *per se*. For example, there may be withholding tax issues if the payment is to a foreign lender (please see question 6.1).

Also, there may be adverse US tax consequences for a US borrower resulting from the involvement of any foreign subsidiary guaranteeing or otherwise providing credit support for the debt of a US borrower. Under US tax rules, such a guarantee could be construed to result in a "deemed dividend" from the foreign subsidiary to the US parent in the full amount of the guaranteed debt, and this deemed dividend would generally be subject to US tax. The same result could apply if collateral at the foreign subsidiary is used to secure the loan to the US parent, or if the US parent pledges more than 66% of the voting stock of a first-tier foreign subsidiary. Recently enacted changes to the Code pursuant to the 2017 Act may impact the scope of taxpayers affected by these rules including, for instance, by broadening the class of foreign subsidiaries subject to them. These types of tax issues are important to consider when structuring a transaction with credit support from foreign subsidiaries of US companies. There are many ways to address these types of issues, including having the loans made directly to the foreign subsidiary.

3 Collateral Security

3.1 What types of collateral are available to secure lending obligations?

A wide variety of assets (including land, buildings, equipment, inventory, accounts, contract rights, investment property, deposit accounts, commercial tort claims, etc.) are available for use as security for loan obligations with many of the most common types of collateral described more fully below. Assets used as security are often divided into two broad categories: (a) "personal property" which generally refers to property other than real property (land and buildings); and (b) real property.

The Uniform Commercial Code ("UCC") provides a well-developed and predictable framework for providing security interests in a wide variety of personal property assets. The UCC is a state law statute rather than a federal one, but the UCC has been adopted by all 50 states in the US and the District of Columbia, with only a few non-uniform amendments of significance.

Under the UCC, when a security interest "attaches", it becomes enforceable as a matter of contract by the lender against the borrower. "Attachment" typically occurs when credit is extended to the borrower, the borrower has ownership or other rights in the collateral in which to grant a security interest, and the borrower signs and delivers to the lender a written security agreement describing the collateral.

After attachment, the security interest must be "perfected" by the lender in order for the lender's security interest to have priority over the rights of an unsecured creditor who later uses judicial process to obtain lien on the collateral. Since a federal bankruptcy trustee has the same status as a state law judicial lien creditor under US law, a bankruptcy trustee will be able to set aside the security interest if the security interest is not perfected.

The method of perfecting a security interest under the UCC depends on the type of collateral in question. The most common method of perfecting a security interest is by "filing" a financing statement in the appropriate state filing office. The UCC provides specific rules for where to file a financing statement, with the general rule that the filing takes place in the jurisdiction where the borrower is located. A borrower organised under a state law in the United States as a corporation, limited partnership, limited liability company or statutory trust is considered to be located in the state in which it is organised. The filing contains only brief details including the name of the borrower, the name of the secured party and an indication of the collateral, and the filing fee is generally fairly nominal. Security interests in some collateral may be perfected by "possession" or "control" (including directly-held securities, securities accounts and deposit accounts). A security interest in certain collateral may be perfected by more than one method.

If two or more lenders have perfected security interests in the same collateral, the UCC provides rules for which lender has "priority" over the other security interest. This is usually determined by a "first-in-time" of filing or perfection rule, but there is a special rule for acquisition finance ("purchase-money") priority and special priority rules also apply to certain collateral (e.g., promissory notes, investment securities and deposit accounts) if a security interest is perfected by possession or "control".

In addition, security interests in certain types of personal property collateral may to some extent be governed by federal statutes and pre-empt the UCC rules. For example, the perfection of a security interest in an aircraft is governed by the Federal Aviation Act and the perfection of a security interest in a ship above a certain tonnage is governed by the federal Ship Mortgage Act.

The requirements for taking a security interest in real property (referred to as a "mortgage" or "deed of trust" in the US) are determined by the laws of the state where the real property is located. Typically the office in which to file the mortgage or deed of trust is in the county of the state where the land is located. These statutes are fairly similar from state to state, but less consistent than the rules for personal property. As a result, mortgage documents from state to state appear quite different, while security agreements with respect to personal property (governed by the more consistent UCC of each state) are more uniform. Lenders often obtain a title insurance policy in order to confirm the perfection and priority of their security interest in real property.

A security interest in fixtures (personal property that permanently "affixes" to land) is generally perfected by filing in the place where the real property records are filed. A security interest in fixtures may be perfected under the UCC or under the local real estate law.

3.2 Is it possible to give asset security by means of a general security agreement or is an agreement required in relation to each type of asset? Briefly, what is the procedure?

In general, a single security agreement can cover all UCC personal property which is taken for security as a loan, no matter where the personal property is located.

With respect to real property, generally a separate mortgage or deed of trust document is used for each state where real property is located, given that the mortgage document is typically governed by the laws of that particular state.

3.3 Can collateral security be taken over real property (land), plant, machinery and equipment? Briefly, what is the procedure?

Yes. Please see question 3.1.

3.4 Can collateral security be taken over receivables? Briefly, what is the procedure? Are debtors required to be notified of the security?

Yes. Receivables are considered personal property, and a security interest in the receivables granted under a security agreement would typically be perfected by filing a financing statement in the appropriate filing office. If the receivable is evidenced by a promissory note or bond or by a lease of or loan and security interest in specific goods, the receivable may also be perfected by the lender's possession or "control". Debtors on the receivables are not required to be notified of the security interest in order for perfection to occur.

The security agreement can grant a security interest in future receivables. An already filed financing statement will be effective to perfect a security interest in a future receivable when it arises.

3.5 Can collateral security be taken over cash deposited in bank accounts? Briefly, what is the procedure?

Yes. A security interest granted under a security agreement in a deposit account as original collateral must be perfected by control (not by filing). To obtain control of the deposit account, a secured lender typically enters into a control agreement with the borrower and the institution that is the depositary bank by which the bank agrees to follow the lender's instructions as to the disposition of the funds in the deposit account without further consent of the borrower. Many depositary banks have forms of control agreements which they will provide as a starting point for negotiations. (However, if the secured lender is also the depositary bank or the lender becomes the depositary bank's customer on the deposit account, control is established without the need for a control agreement to perfect the security interest.)

3.6 Can collateral security be taken over shares in companies incorporated in your jurisdiction? Are the shares in certificated form? Can such security validly be granted under a New York or English law governed document? Briefly, what is the procedure?

Yes. Companies are typically incorporated under the laws of individual states in the US, and usually not under federal law. Shares may be issued in either certificated or uncertificated form.

A security interest may be created by either a New York law or English law-governed security agreement. If the security agreement is governed by English law, the UCC in New York requires that the transaction bear a reasonable relationship to England for the choice of law clause to be enforceable. (Please also see question 7.1 as to the extent a court in New York will enforce a contract that has a foreign governing law.)

In general, a security interest in such directly-held shares can be perfected either by filing or by control, though perfection by control has priority. The law governing perfection of such security interest in certificated securities depends on whether perfection is achieved by filing (location of debtor) or by control (location of collateral).

If the shares are credited to a securities account at a bank or broker and are therefore indirectly held, a borrower's interest in the securities account can be perfected either by filing or control. Once again, perfection by control has priority. The law governing perfection of a security interest in a securities account depends on whether perfection is achieved by filing (location of debtor) or by control (location of bank or broker as determined usually by the law governing the securities account relationship).

3.7 Can security be taken over inventory? Briefly, what is the procedure?

Yes. Please see question 3.1. A security interest may be granted under security agreement and may be perfected by the filing of a financing statement in the appropriate UCC filing office. Perfection may also be achieved by possession, though this method is seldom practical from a secured lender's perspective.

The security agreement can grant a security interest in future inventory. An already filed financing statement will be effective to perfect a security interest in a future inventory when it is created or acquired.

3.8 Can a company grant a security interest in order to secure its obligations (i) as a borrower under a credit facility, and (ii) as a guarantor of the obligations of other borrowers and/or guarantors of obligations under a credit facility (see below for questions relating to the giving of guarantees and financial assistance)?

Yes to both (i) and (ii). Note that with respect to item (ii), a guarantor would be subject to the same fraudulent transfer analysis discussed in question 2.2.

A security agreement may also secure obligations relating to future loans. An already filed financing statement perfecting a security interest securing existing loans will be effective to perfect a security interest in a future loan when the loan is made.

3.9 What are the notarisation, registration, stamp duty and other fees (whether related to property value or otherwise) in relation to security over different types of assets?

With respect to personal property governed by the UCC, and the filing of financing statements, there are typically no material costs and UCC filing fees are usually minimal.

With respect to real property, there may be significant recording taxes and fees. These taxes and fees will depend on the state and local laws involved. A number of practices are used in loan transactions in an attempt to minimise such costs. For example, in the case of refinancings, lenders may assign mortgages rather than entering into new mortgages; and in the case of mortgage tax recording states, lenders may limit the amount secured by the mortgage, so that the mortgage tax payable is set at a level commensurate with the value of the property as opposed to the overall principal amount of the loans.

3.10 Do the filing, notification or registration requirements in relation to security over different types of assets involve a significant amount of time or expense?

Please see question 3.9. In terms of a time-frame, UCC personal property security interests may be perfected in a matter of days. Real property security interests typically take longer, though they can usually be completed in a couple of weeks.

3.11 Are any regulatory or similar consents required with respect to the creation of security?

Generally no, except in the case of certain regulated entities where consent of the regulatory authority may be required for the grant or enforcement of the security interest.

Also, please see question 2.6 for a quick summary of tax issues that may arise in connection with foreign subsidiaries providing guarantees or collateral to secure loans to US borrowers.

3.12 If the borrowings to be secured are under a revolving credit facility, are there any special priority or other concerns?

Under the UCC, many traditional concerns under revolvers have been addressed by the "first to file or perfect" rule, though lenders should be aware of certain priority issues. For example, with respect to secured creditors who each have perfected security interests in UCC collateral, as stated previously certain "purchase-money" security interests and security interest in certain collateral perfected by possession or control may obtain over a security interest perfected merely by the filing of a financing statement. In addition, tax liens and some other liens created outside of the UCC may obtain priority over a UCC perfected security interest. Judgment liens may pose a priority problem for future advances, and tax liens may pose a priority problem for some after-acquired property and future advances. Otherwise, under the UCC, the first secured creditor to "file or perfect" has priority

With respect to real property, the matter is less clear. As a general matter, absent special legislation in the state, future loans may not have same priority as loans advanced when the mortgage or deed of trust is recorded if there is an intervening mortgage, deed of trust or lien recorded before the future loan is made. Accordingly, a close review of state rules and individual state documentary requirements is required in order to ensure priority.

3.13 Are there particular documentary or execution requirements (notarisation, execution under power of attorney, counterparts, deeds)?

With respect to UCC collateral, the documentation requirements are spelled out clearly in the UCC and the requirements generally are straightforward. No notarisation is required. Under prior versions of the UCC, the debtor was required to sign a written security agreement, though as the world moves away from paper and into electronic media, the model UCC, including the UCC as adopted in New York, now requires the debtor to "authenticate a record" that may include an electronic record. Nevertheless, most lenders in corporate loan transactions still generally require a written security agreement. With respect to real property collateral, the documentary and execution requirements tend to be more traditional by looking to a writing, but various law reform efforts are under way to permit electronic mortgages and deeds of trust and electronic recording of mortgages and deeds of trust. The requirements may vary significantly from state to state (for example, real property mortgages often require notarisation under state law, whereas this is generally not the case for UCC collateral).

4 Financial Assistance

4.1 Are there prohibitions or restrictions on the ability of a company to guarantee and/or give security to support borrowings incurred to finance or refinance the direct or indirect acquisition of: (a) shares of the company; (b) shares of any company which directly or indirectly owns shares in the company; or (c) shares in a sister subsidiary?

(a) Shares of the company.

(b) Shares of any company which directly or indirectly owns shares in the company.

(c) Shares in a sister subsidiary.

Generally no. There is no "financial assistance" law *per se* in the United States, but please see the discussion of fraudulent transfer and related principles described in question 2.2.

5 Syndicated Lending/Agency/Trustee/Transfers

5.1 Will your jurisdiction recognise the role of an agent or trustee and allow the agent or trustee (rather than each lender acting separately) to enforce the loan documentation and collateral security and to apply the proceeds from the collateral to the claims of all the lenders?

Yes. In loan documentation, the role is typically that of an "agent", with bond documentation typically using a "trustee".

5.2 If an agent or trustee is not recognised in your jurisdiction, is an alternative mechanism available to achieve the effect referred to above which would allow one party to enforce claims on behalf of all the lenders so that individual lenders do not need to enforce their security separately?

This is not applicable; please see question 5.1.

5.3 Assume a loan is made to a company organised under the laws of your jurisdiction and guaranteed by a guarantor organised under the laws of your jurisdiction. If such loan is transferred by Lender A to Lender B, are there any special requirements necessary to make the loan and guarantee enforceable by Lender B?

In a syndicated lending transaction that includes a lender acting in an agency capacity, a guarantor typically would provide a guaranty to the agent "for the benefit of the lenders under the loan agreement" (or some similar formulation). As such, it should not be necessary for a guarantor to sign the transfer (assignment) documentation in order to be bound, though the contractual language should be carefully reviewed for specific requirements. In the case of a bilateral loan, the contractual terms should also be closely reviewed, though it is advisable to obtain the guarantor's consent to such assignment in any event.

6 Withholding, Stamp and other Taxes; Notarial and other Costs

6.1 Are there any requirements to deduct or withhold tax from (a) interest payable on loans made to domestic or foreign lenders, or (b) the proceeds of a claim under a guarantee or the proceeds of enforcing security?

There is no US federal income tax withholding from payments of interest or principal to US lenders, provided certain documentation requirements are complied with. With respect to the payment of interest to foreign lenders (other than such payments to a US branch of a foreign lender that is engaged in business in the US), the general rule is that a withholding rate of 30% is applied to the gross amount of payments constituting interest and other income (but, subject to the discussion of FATCA below, not to principal). The US has in place bilateral treaties with many jurisdictions, which reduce or entirely eliminate this withholding tax for qualifying foreign lenders. A listing of these treaties is available at http://www.irs.gov/Businesses/International-Businesses/United-States-Income-Tax-Treaties---A-to-Z. Such withholding taxes may also be avoided if the requirements of the so-called "Portfolio Interest Exemption" are satisfied. This exception is generally not available to banks, but could be available to non-bank lenders such as hedge funds. Note that under FATCA (mentioned in question 1.1), foreign lenders generally will be required to identify and report directly to the US Internal Revenue Service information about accounts in such institutions that are held by US taxpayers. The failure to comply with FATCA would result in withholding as discussed in question 1.1 above even for treaty-resident lenders, which would then be required to file a refund claim pursuant to the applicable bilateral tax treaty to recoup any amounts withheld. Generally, the proceeds of a claim under a guarantee or the proceeds of enforcing security are taxed in a manner similar to payments made directly by the borrower.

6.2 What tax incentives or other incentives are provided preferentially to foreign lenders? What taxes apply to foreign lenders with respect to their loans, mortgages or other security documents, either for the purposes of effectiveness or registration?

The US federal government has generally provided few incentives targeted to foreign lenders (as there has not been a policy focus on promoting foreign loans into the United States), though please refer to the bilateral tax treaties and Portfolio Interest Exemption referred to in question 6.1.

6.3 Will any income of a foreign lender become taxable in your jurisdiction solely because of a loan to or guarantee and/or grant of security from a company in your jurisdiction?

In general, a foreign lender, with no presence or activities in the US, does not become subject to US federal income taxation on its net income solely as a result of loaning to, or receiving a guarantee or grant of security from, a borrower or guarantor in the US. However, income derived specifically from a loan made to a US borrower (i.e., interest and other income) would be subject to gross-basis US taxation, typically at a rate of 30%, unless a treaty specified a lower rate, or the Portfolio Interest Exemption applied (please see question 6.1). Moreover, if a foreign lender has a presence or activities in the United States (for instance, employees or agents working out of, or a lending office located in, the US), the foreign lender could be viewed as being engaged in a trade or business in the US, and if so would be subject to net-basis US taxation on any income deemed "effectively connected" with that trade or business.

6.4 Will there be any other significant costs which would be incurred by foreign lenders in the grant of such loan/guarantee/security, such as notarial fees, etc.?

With regard to mortgages and other security documents, there are generally no taxes or other costs applicable to foreign lenders that would not also be applicable to lenders in the US (please see question 3.10 for a general summary of such costs).

6.5 Are there any adverse consequences to a company that is a borrower (such as under thin capitalisation principles) if some or all of the lenders are organised under the laws of a jurisdiction other than your own? Please disregard withholding tax concerns for purposes of this question.

If a corporation is "thinly capitalised" and certain other factors are present, the US tax authorities may assert that instruments described as debt actually constitute equity for US tax purposes. The effect of such re-characterisation would be that payments on the instrument would not be deductible to the borrower for US federal income tax purposes and could be subject to withholding in a manner different than interest payments (for instance, because the Portfolio Interest Exemption would not be available). Moreover, even if treated as debt, US tax rules may deny a deduction (in whole or in part) for payments of interest by a thinly capitalised borrower (i.e., a borrower with a debt-to-equity ratio in excess of 1.5 to 1) to a "related party" that is exempt from US federal income tax on the interest, taking into account any treaty-based reductions in tax rate. If the lenders are organised in a jurisdiction other than that of the borrower, this should not impact the thin capitalisation analysis itself, but, as mentioned above, may impact the withholding rate as well as any relevant "gross-up". Moreover, the 2017 Act enacted sweeping changes to the Code, including a potentially significant limitation on the ability of borrowers to deduct interest for US tax purposes. Many of the provisions contained in the legislation are unclear and/or may be the subject of clarifying guidance from the US Internal Revenue Service.

7 Judicial Enforcement

7.1 Will the courts in your jurisdiction recognise a governing law in a contract that is the law of another jurisdiction (a "foreign governing law")? Will courts in your jurisdiction enforce a contract that has a foreign governing law?

Generally, yes, so long as the choice of law bears a "reasonable relation" to the transaction and application of the foreign governing law would not be contrary to the public policy of the forum state.

On a related note, in connection with a choice of *New York* law as a governing law, a New York statute allows for New York law to be chosen by parties to a contract and, with certain exceptions, such choice of law will be given effect by New York courts if the transaction exceeds $250,000 in value, regardless of whether the choice of New York law bears any reasonable relationship to the transaction. (The choice of New York as a forum is subject to additional requirements under the statute.) California has a similar statute.

7.2 Will the courts in your jurisdiction recognise and enforce a judgment given against a company in New York courts or English courts (a "foreign judgment") without re-examination of the merits of the case?

In most instances, yes. Despite the strong commercial ties between the United States and the United Kingdom, there is no international treaty on reciprocal recognition and enforcement of court judgments (attempts to come to terms on a bilateral treaty in 1981 broke down over the negotiation of the final text). Nevertheless, the Uniform Foreign Country Money Judgments Recognition Act has been adopted by most states (including New York) and sets out basic rules of enforceability in connection with the enforcement of judgments between states in the United States, with "foreign-country" judgments treated in a similar manner as the judgment of a sister state. Generally, if a judgment is obtained in accordance with procedures compatible with United States due process principles, it will be recognised under the Uniform Act. There are many examples of English judgments having been enforced in New York courts.

7.3 Assuming a company is in payment default under a loan agreement or a guarantee agreement and has no legal defence to payment, approximately how long would it take for a foreign lender to (a) assuming the answer to question 7.1 is yes, file a suit against the company in a court in your jurisdiction, obtain a judgment, and enforce the judgment against the assets of the company, and (b) assuming the answer to question 7.2 is yes, enforce a foreign judgment in a court in your jurisdiction against the assets of the company?

In New York, a court could rule almost immediately, perhaps within three to six months or less, with enforcement against assets of the company in New York beginning as soon as the judgment was entered (unless the defendant obtained a stay of enforcement). However, in practice, particularly if an opposing party appears and raises procedural or other issues, matters could take materially longer, up to a year or more.

Enforcement of a foreign judgment is generally pursued in New York by having the foreign judgment "confirmed", with time frames similar to those mentioned above.

7.4 With respect to enforcing collateral security, are there any significant restrictions which may impact the timing and value of enforcement, such as (a) a requirement for a public auction, or (b) regulatory consents?

In a non-bankruptcy context, the timing and restrictions that apply to enforcement of collateral can vary significantly, depending on the type of collateral and relevant state law that applies. The UCC provides a great deal of flexibility in the rules governing disposition of personal property collateral (see question 3.1). The UCC generally permits either "private" or "public" sale, with the only real limitation on the power to sell that the secured party must "act in good faith" and in a "commercially reasonable manner". Under the UCC, after the sale, the secured party generally may pursue the debtor for amounts that remain unpaid (the "deficiency"). The requirements with respect to real property collateral will vary significantly from state to state (and note in particular that in California, there may be limitations with respect the ability of a creditor to collect on a deficiency if the creditor is secured with real property collateral). With respect to regulated entities (including certain energy and communications companies) enforcement may require regulatory approval.

In a bankruptcy context, enforcement would be restricted by the automatic stay (please see question 8.1).

7.5 Do restrictions apply to foreign lenders in the event of (a) filing suit against a company in the USA, or (b) foreclosure on collateral security?

For the most part, distinctions will not be made between foreign and domestic creditors in such proceedings. However, there are certain issues a foreign lender would need to consider in connection with such activities. For example, generally a foreign creditor will need to be authorised to do business in New York before availing itself as a plaintiff of the New York courts. In addition, foreign creditors may be subject to federal or state limitations on or disclosure requirements for the direct or indirect foreign ownership of certain specific types of companies or collateral, including in the energy, communications and natural resources areas.

7.6 Do the bankruptcy, reorganisation or similar laws in your jurisdiction provide for any kind of moratorium on enforcement of lender claims? If so, does the moratorium apply to the enforcement of collateral security?

Yes, please see question 8.1.

7.7 Will the courts in your jurisdiction recognise and enforce an arbitral award given against the company without re-examination of the merits?

The United States is party to the New York Convention. The Convention requires courts of contracting states to give effect to private agreements to arbitrate and to recognise and enforce arbitration awards made in other contracting states, subject to certain limitations and/or potential challenges. Note, however, that loan agreements under New York law generally do not include arbitration clauses.

8 Bankruptcy Proceedings

8.1 How does a bankruptcy proceeding in respect of a company affect the ability of a lender to enforce its rights as a secured party over the collateral security?

In the US, a bankruptcy proceeding may be initiated by either the company (debtor) itself or by its creditors. Once the proceeding is commenced, the relevant statutes in the United States (the "Bankruptcy Code") provide that an "automatic stay" immediately occurs. This automatic stay is effectively a court order that prevents creditors from taking any actions against the debtor or its property, including enforcement actions against collateral. A creditor that violates the automatic stay could face severe penalties, including actual damages caused to the debtor and other creditors, as well as having its enforcement action declared void (punitive damages are typically limited to individual, rather than corporate debtors).

There are, however, a number of protections for a secured creditor who has properly perfected its liens and such liens are not subject to avoidance. First and foremost, upon a liquidation of a debtor, a secured creditor is paid its claim (up to the value of its collateral) prior to the payment of general unsecured creditors or, alternatively, it may receive its collateral back in satisfaction of its secured claim. Also, in the case of a reorganisation of a debtor, cash collateral cannot be used by the debtor without specific authorisation from the bankruptcy court or consent of the secured party, and in other circumstances the Bankruptcy Code mandates that a secured party's interest in its collateral be "adequately protected".

8.2 Are there any preference periods, clawback rights or other preferential creditors' rights (e.g., tax debts, employees' claims) with respect to the security?

In short, yes. A lender's security interest could be voided as a "preferential transfer" if it is provided to the lender within 90 days before a bankruptcy filing (or one year if the lender is an "insider", or related party of the debtor) and as a result of the transfer the lender receives more than it would have otherwise received in the liquidation of the debtor. There are a number of exceptions to this rule, including where there has been a substantially contemporaneous exchange for new value. Please also see the discussion of "fraudulent transfers" in question 2.2.

There are certain claims that may have priority even over a properly perfected security interest, including tax liens, mechanics liens, and certain costs associated with the bankruptcy itself.

8.3 Are there any entities that are excluded from bankruptcy proceedings and, if so, what is the applicable legislation?

There are a number of entities that are either excluded from the Bankruptcy Code or for which special provisions of the Bankruptcy Code or other special legislation apply, including banks, insurance companies, commodity brokers, stockbrokers and government entities and municipalities. Municipalities and government-owned entities (but not states themselves) are eligible for relief under Chapter 9 of the Bankruptcy Code.

8.4 Are there any processes other than court proceedings that are available to a creditor to seize the assets of a company in an enforcement?

Yes. The UCC allows for so-called "self-help" remedies without first commencing a court proceeding. Note that the relevant provisions of a security agreement and governing law should be considered before exercising these types of remedies. These remedies typically can only be used so long as no "breach of the peace" would occur. Subject to the above, the market generally accepts these types of remedies for collateral, such as bank accounts and certificated securities.

9 Jurisdiction and Waiver of Immunity

9.1 Is a party's submission to a foreign jurisdiction legally binding and enforceable under the laws of your jurisdiction?

Generally, yes.

9.2 Is a party's waiver of sovereign immunity legally binding and enforceable under the laws of your jurisdiction?

Yes. The Foreign Sovereign Immunities Act ("FSIA") codifies the law of sovereign immunity in the US. The FSIA allows for such immunity to be waived, and generally upholds waivers, with some limitations (for example, non-commercial property of a sovereign cannot be attached). Certain organisations also receive immunity under authority separate from the FSIA: the International Organizations Immunity Act covers immunity for certain institutions like the IMF, the OECD and the African Union. One issue in connection with the enforcement of such waivers is whether a borrower actually had the immunity to waive when it provided a waiver. Such scenarios arise in the context of the nationalisation of a company. In such a case, a company may not have had any immunity to waive (since it was not previously owned by the state) when it entered into the loan, so any waiver provided prior to being taken over by a state may be considered void. For this reason, New York law-governed loan agreements often include a representation that a loan represents a "commercial act", which excludes the transaction from protection under relevant immunity statutes, whether or not such immunity was in fact effectively waived.

10 Licensing

10.1 What are the licensing and other eligibility requirements in your jurisdiction for lenders to a company in your jurisdiction, if any? Are these licensing and eligibility requirements different for a "foreign" lender (i.e. a lender that is not located in your jurisdiction)? In connection with any such requirements, is a distinction made under the laws of in your jurisdiction between a lender that is a bank versus a lender that is a non-bank? If there are such requirements in your jurisdiction, what are the consequences for a lender that has not satisfied such requirements but has nonetheless made a loan to a company in your jurisdiction? What are the licensing and other eligibility requirements in your jurisdiction for an agent under a syndicated facility for lenders to a company in your jurisdiction?

In the US, a lender is not required to be a bank (indeed, many lenders are non-banks). A lender should be aware of any relevant state lending licensing laws which may require a lender to be licensed. In general, regulated banks do not need to be separately licensed under state law as lenders, but non-bank lenders must be aware of, and comply with, applicable lender licensing laws. These licensing laws are much more stringent in the consumer or "small loan" lending area than in the commercial or corporate lending area (where few states require the licensing of corporate nonbank lenders, California being a notable exception), although in any event non-bank lender licences are typically easier to obtain than a "banking licence".

In general, the applicability of state licensing laws is triggered by the solicitation of loans with, or the making of loans to, residents of that state. Therefore, whether a lender is a U.S. or non-U.S. lender generally has no bearing on whether that lender must be licensed under the laws of a given state. In some cases, one needs to be "in the business of making loans" in order for the licensing statute to be given effect (for example, the New York lender licensing law indicates those lenders who engage in "isolated, incidental or occasional transactions" are not "in the business of making loans" and therefore not covered for purposes of the statute).

Non-compliance with a licence statute could have a material impact on the lender, from not being able to access a state's court system to having a loan be determined to be unenforceable. Whether an agent on a lending transaction would also need to be licensed will depend on the wording of each state's particular statute.

Note there are often contractual restrictions in New York law-governed loan documentation that require a lender be a certain type of organisation that is in the business of making loans. The rationale for this is manifold, from securities law concerns to the preference of the borrower to only deal with sophisticated financial institutions should the loan be sold.

11 Other Matters

11.1 Are there any other material considerations which should be taken into account by lenders when participating in financings in your jurisdiction?

The material considerations to be considered in connection with a financing in the US will vary depending on the type of financing and the parties involved, and a discussion with counsel is encouraged before entering into any financing in the US. However, the above questions address many of the main material issues that arise.

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Venezuela

Rodner, Martínez & Asociados

Jaime Martínez Estévez

1 Overview

1.1 What are the main trends/significant developments in the lending markets in your jurisdiction?

Domestic lending activities are, to a large extent, determined by compulsory lending mandated by the law and regulations for the housing, tourism, agriculture and industrial sectors of the economy. International lending has been substantially diminished given the political circumstances, including the U.S. sanctions, and has been mainly circumscribed to the financing of Government projects and, particularly, further development of the Orinoco heavy oil basin.

1.2 What are some significant lending transactions that have taken place in your jurisdiction in recent years?

Lending transactions are mostly restructurings and supplemental financing in the oil sector, particularly though joint venture companies chartered by PDVSA (a Venezuelan national oil company) and foreign oil companies, in which PDVSA owns the majority of the shares, and trade financing for Venezuelan imports.

2 Guarantees

2.1 Can a company guarantee borrowings of one or more other members of its corporate group (see below for questions relating to fraudulent transfer/financial assistance)?

There are no particular legal restrictions for intercompany loans. However, tax provisions on presumed dividends and transfer pricing may be applicable.

2.2 Are there enforceability or other concerns (such as director liability) if only a disproportionately small (or no) benefit to the guaranteeing/securing company can be shown?

No, absent a conflict with the corporate charter or an insolvency situation.

2.3 Is lack of corporate power an issue?

Definitely. If there is no capacity to issue the consent, the act would not be valid (Article 1141 of the Civil Code and Articles 243 and 270 of the Commercial Code).

2.4 Are any governmental or other consents or filings, or other formalities (such as shareholder approval), required?

No governmental consent or filing is required. Shareholder approval would be necessary if the respective charter and by-laws establish that the power to guarantee third party obligations rests on the shareholders.

2.5 Are net worth, solvency or similar limitations imposed on the amount of a guarantee?

None, except that the enforceability of the guarantee could be set aside if given while insolvent (Article 946 of the Commercial Code).

2.6 Are there any exchange control or similar obstacles to enforcement of a guarantee?

There has been an exchange control in effect since 2003. The foreign exchange system has been modified several times and has proven repeatedly inefficient. The last change occurred on January 26, 2018, when the dual exchange rate system: Dipro (Bs 10/US$) and Dicom (last Bs 3,345/US$) was terminated. Currently foreign exchange is to be done through Dicom, an auction system supervised by the Central Bank of Venezuela, which had been suspended in September 2017. There is no prohibition of Venezuelan companies holding foreign currency assets abroad. If the guarantor has foreign currency funds abroad, it can make the payment in foreign currency without authorisations. Government-controlled entities require Central Bank authorisation to hold foreign currency abroad.

3 Collateral Security

3.1 What types of collateral are available to secure lending obligations?

Security interest can be created over tangible and intangible assets, including real estate, chattel property, inventory, a business establishment, credit rights, intellectual property rights, shares and other securities.

3.2 Is it possible to give asset security by means of a general security agreement or is an agreement required in relation to each type of asset? Briefly, what is the procedure?

Depending on the type of collateral, the security interest document will vary. Some security interest can be created by way of a mortgage (e.g. real estate, chattel property) and others pursuant to a pledge (e.g. shares, account receivables). Some require governmental authorisation and special filings. A single security interest document can cover different types of collateral and forms of encumbrance (mortgage, pledge without transfer of possession). The same security interest document may be registered in registries of various municipal jurisdictions.

3.3 Can collateral security be taken over real property (land), plant, machinery and equipment? Briefly, what is the procedure?

A real estate mortgage may cover the land and the plant (governed by the Civil Code, Article 1877), and the machinery and equipment may be covered by a chattel mortgage (governed by the Chattel Mortgage and Pledge Without Transfer of Possession Act). The mortgage document must be registered in the registry with jurisdiction over the location of the assets.

3.4 Can collateral security be taken over receivables? Briefly, what is the procedure? Are debtors required to be notified of the security?

Security interest may be taken over receivables by way of a pledge. The pledge agreement must be executed before a notary or filed with a notary (to have a certain date). Notice must be given to the debtors (notice of transfer as security interest, Article 1550 of the Civil Code).

3.5 Can collateral security be taken over cash deposited in bank accounts? Briefly, what is the procedure?

A pledge agreement can be entered into in connection with the rights associated with a bank or brokerage account. Notice must be given to the bank or brokerage entity holding the account.

3.6 Can collateral security be taken over shares in companies incorporated in your jurisdiction? Are the shares in certificated form? Can such security validly be granted under a New York or English law governed document? Briefly, what is the procedure?

Shares of a Venezuelan corporation may be pledged. In addition to executing a pledge agreement, a transfer as security interest note should be inscribed in the shareholders' registry book of the corporation. Share certificates are commonly issued (Article 293 of the Commercial Code). However, the transfer of the rights of a shareholder is carried out by a note in the shareholders' registry book (Article 296 of the Commercial Code). The agreement must be governed by Venezuelan law (Articles 20, 27 and 37 of the International Private Law Act).

3.7 Can security be taken over inventory? Briefly, what is the procedure?

Security interest can be taken over inventory by way of a chattel mortgage (Article 30 of the Chattel Mortgage and Pledge Without Transfer of Possession Act) or pursuant to an arrangement with an authorised general warehouse and delivery of warehouse certificates (in accordance with the General Deposit Warehouses Act).

3.8 Can a company grant a security interest in order to secure its obligations (i) as a borrower under a credit facility, and (ii) as a guarantor of the obligations of other borrowers and/or guarantors of obligations under a credit facility (see below for questions relating to the giving of guarantees and financial assistance)?

A security interest can be granted to several creditors and for different transactions. However, if different creditors are receiving a security interest with respect to different transactions, ranking of the security interest and inter-creditor agreements may be necessary.

3.9 What are the notarisation, registration, stamp duty and other fees (whether related to property value or otherwise) in relation to security over different types of assets?

The notarisation charges for documents creating security interest are not calculated based on the type or value of the assets but rather on the particulars of the document (e.g. number of pages). Registrations of security interests, however, generate fees which are calculated based on the value assigned to the security interest. The registration fees will be calculated pursuant to a progressive rate of up to 0.60% (Article 83 of the Public Registry and Notary Act).

3.10 Do the filing, notification or registration requirements in relation to security over different types of assets involve a significant amount of time or expense?

When authorisations are required, the procedure may be a lengthy one. Registration of complex transactions may also require extra time. When the assets are located in different jurisdictions, the security interest document may need to be registered in all of the registries with jurisdiction over the different locations; this may prove to be a long process.

3.11 Are any regulatory or similar consents required with respect to the creation of security?

Chattel mortgages and pledges without transfer of possession can only be created in favour of qualified secured creditors, including foreign banks authorised by the Superintendency of the Banking Sector Institutions (Article 19 of the Chattel Mortgage and Pledge Without Transfer of Possession Act). To request such an authorisation, a draft of the security interest document must be presented.

3.12 If the borrowings to be secured are under a revolving credit facility, are there any special priority or other concerns?

There is no problem in creating a security interest with respect to a revolving credit facility. Priority of mortgages will be set by the date of registration.

3.13 Are there particular documentary or execution requirements (notarisation, execution under power of attorney, counterparts, deeds)?

Mortgage documents must be registered. Registration must be carried out in the registry office with jurisdiction given by the location or the type of asset. Pledges are to be executed before a notary or a counterpart of the pledge agreement must be filed with a notary soon after.

4 Financial Assistance

4.1 Are there prohibitions or restrictions on the ability of a company to guarantee and/or give security to support borrowings incurred to finance or refinance the direct or indirect acquisition of: (a) shares of the company; (b) shares of any company which directly or indirectly owns shares in the company; or (c) shares in a sister subsidiary?

(a) Shares of the company

Guarantees and security interest can be provided to support financing for the acquisition of shares, except that there is a prohibition on making loans or giving security interest for the acquisition of its own shares. The prohibition originates from the provision regarding Treasury shares, which establishes that the company cannot purchase its own shares except with amounts corresponding to retained earnings (Article 263 of the Commercial Code). A more evolved and far-reaching provision is found in the Securities Market Act of 2015 (Article 72).

(b) Shares of any company which directly or indirectly owns shares in the company

Case law has expanded the above-mentioned prohibition to preclude transactions that pretend to bypass the prohibition by using interposed persons.

(c) Shares in a sister subsidiary

The comment for (b) above applies here as well.

5 Syndicated Lending/Agency/Trustee/Transfers

5.1 Will your jurisdiction recognise the role of an agent or trustee and allow the agent or trustee (rather than each lender acting separately) to enforce the loan documentation and collateral security and to apply the proceeds from the collateral to the claims of all the lenders?

A security agent could be created, empowering such agent to act on behalf of all the secured lenders. However, the secured interest must be created in favour of the secured lenders. The security agent may also serve as payment agent and be authorised to receive payments and to make distributions of such payments among the secured lenders.

5.2 If an agent or trustee is not recognised in your jurisdiction, is an alternative mechanism available to achieve the effect referred to above which would allow one party to enforce claims on behalf of all the lenders so that individual lenders do not need to enforce their security separately?

This is not applicable. See the answers above.

5.3 Assume a loan is made to a company organised under the laws of your jurisdiction and guaranteed by a guarantor organised under the laws of your jurisdiction. If such loan is transferred by Lender A to Lender B, are there any special requirements necessary to make the loan and guarantee enforceable by Lender B?

Notice must be given to the debtor and the guarantor if an assignment of a loan takes place (Article 1550 of the Civil Code and 150 of the Commercial Code). The transaction documents may establish additional conditions for the transferability of a loan.

6 Withholding, Stamp and Other Taxes; Notarial and Other Costs

6.1 Are there any requirements to deduct or withhold tax from (a) interest payable on loans made to domestic or foreign lenders, or (b) the proceeds of a claim under a guarantee or the proceeds of enforcing security?

Interest payments are subject to withholding tax when made to foreign lenders (Article 9 (3) of Decree 1808 of 1997). Interest payments to local banks are not subject to withholding (Article 10 of Decree 1808). Guarantees and proceeds of enforcing a security interest are not subject to withholding, unless deemed allocated to the payment of interest.

6.2 What tax incentives or other incentives are provided preferentially to foreign lenders? What taxes apply to foreign lenders with respect to their loans, mortgages or other security documents, either for the purposes of effectiveness or registration?

Currently, there are no tax incentives for foreign lenders. From time to time, exonerations are given to induce the financing of projects in certain economic sectors. Interests on loans made by foreign financial institutions are taxed at the rate of 4.95% (Article 52 of the Income Tax Act). Other rates may apply because of tax treaties. The stamp taxes and fees that are to be paid for the documentation of a loan or a security interest are the same for local and foreign lenders.

6.3 Will any income of a foreign lender become taxable in your jurisdiction solely because of a loan to or guarantee and/or grant of security from a company in your jurisdiction?

Income originating from loans made to Venezuelan borrowers is subject to Venezuelan income tax at a rate of 4.95% (Article 52 of the Income Tax Act). The borrower is to withhold the tax when making the interest payments. If the guarantor or the owner of the security interest is a Venezuelan corporation, no Venezuelan tax will apply to the loan solely because of such circumstance.

6.4 Will there be any other significant costs which would be incurred by foreign lenders in the grant of such loan/guarantee/security, such as notarial fees, etc.?

There are no significant costs associated with the execution of documentation related to a loan, guarantee or security interest, except that the registration of the security interest will entail the payment of registration fees based on a progressive tariff of up to 0.60% of the value of the security interest (Article 83 of the Public Registry and Notary Act).

6.5 Are there any adverse consequences to a company that is a borrower (such as under thin capitalisation principles) if some or all of the lenders are organised under the laws of a jurisdiction other than your own? Please disregard withholding tax concerns for purposes of this question.

No, there are none.

7 Judicial Enforcement

7.1 Will the courts in your jurisdiction recognise a governing law in a contract that is the law of another jurisdiction (a "foreign governing law")? Will courts in your jurisdiction enforce a contract that has a foreign governing law?

Venezuelan courts will recognise a foreign governing law if selected to be the governing law of a contract (Article 29 of the International Private Law Act). Venezuelan courts will enforce such a contract in Venezuela. However, there may be some exceptions for national interest contracts and public policy reasons (Article 151 of the Constitution and Article 5 of the International Private Law Act).

7.2 Will the courts in your jurisdiction recognise and enforce a judgment given against a company in New York courts or English courts (a "foreign judgment") without re-examination of the merits of the case?

Passing of a foreign judgment requires a procedure before the Supreme Court (exequatur), which excludes the examination of the merits (Articles 53 of the International Private Law Act and 850 of the Civil Procedure Code). For arbitral awards, the 1958 New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards will apply.

7.3 Assuming a company is in payment default under a loan agreement or a guarantee agreement and has no legal defence to payment, approximately how long would it take for a foreign lender to (a) assuming the answer to question 7.1 is yes, file a suit against the company in a court in your jurisdiction, obtain a judgment, and enforce the judgment against the assets of the company, and (b) assuming the answer to question 7.2 is yes, enforce a foreign judgment in a court in your jurisdiction against the assets of the company?

A procedure for collection of amounts due may take up to approximately two years, depending on the defences and appeals that the defendant raises during the court procedures. An exequatur procedure, for the passing of a foreign judgment, may take between one and two years and the enforcement against assets of the defendant in Venezuela may take between six months and one year.

7.4 With respect to enforcing collateral security, are there any significant restrictions which may impact the timing and value of enforcement, such as (a) a requirement for a public auction, or (b) regulatory consents?

Venezuelan enforcement procedures will require a public auction (Articles 550 to 584 of the Civil Procedure Code). Notices to the Attorney General's Office will be required if there is a risk of interruption of a public service (Article 99 of the Attorney General Organic Act). The existing exchange control is one of the major obstacles to effectively realising the proceeds of the security interest being enforced.

7.5 Do restrictions apply to foreign lenders in the event of (a) filing suit against a company in your jurisdiction, or (b) foreclosure on collateral security?

This is not applicable. In non-commercial litigations, the foreign plaintiff may be required to post a bond (Articles 36 of the Civil Code and 1102 of the Commercial Code).

7.6 Do the bankruptcy, reorganisation or similar laws in your jurisdiction provide for any kind of moratorium on enforcement of lender claims? If so, does the moratorium apply to the enforcement of collateral security?

If the debtor has a positive network but has liquidity problems, it may apply for a moratorium (Article 898 of the Commercial Code). While in moratorium or in a bankruptcy procedure, the enforcement of rights against the debtor would be suspended, except that the suspension would not apply to the enforcement of security interest (Articles 905, 942 and 964 of the Commercial Code).

7.7 Will the courts in your jurisdiction recognise and enforce an arbitral award given against the company without re-examination of the merits?

Yes. Venezuela is a party to the 1958 New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards.

8 Bankruptcy Proceedings

8.1 How does a bankruptcy proceeding in respect of a company affect the ability of a lender to enforce its rights as a secured party over the collateral security?

The secured lender would be limited in its ability to collect from the bankruptcy assets, other than the collateral, if the collateral is not sufficient to satisfy its claims (Article 1047 of the Commercial Code). If the collateral is not sufficient to satisfy the debt, the bankruptcy effects will apply to the remaining debt, including that interest stop accruing on the bankruptcy declaration date (Articles 943 and 944 of the Commercial Code).

8.2 Are there any preference periods, clawback rights or other preferential creditors' rights (e.g., tax debts, employees' claims) with respect to the security?

There are debts that are preferred by law (privileged creditors, Article 1867 of the Civil Code; labour debts, Article 151 of the Labour and Workers Act), even above the preference corresponding to secured creditors. Security interest granted during the so-called suspicious period may be set aside. A suspicious period may be up to two years and 10 days (Articles 936 and 945 of the Commercial Code). The suspicious period begins 10 days prior to the date on which the court establishes that the insolvency commenced. Payments on unmatured debt or in kind made during the suspicious period may be annulled (Article 945 of the Commercial Code).

8.3 Are there any entities that are excluded from bankruptcy proceedings and, if so, what is the applicable legislation?

Banks, insurance companies and brokerage houses are excluded from bankruptcy and subject to a similar procedure carried by the Superintendency of the Banking Sector Institutions (Articles 240, 247 and 257 of the Banking Sector Institutions Act), the Superintendency of Insurance Activity (Articles 98, 101 and 107 of the Insurance Activity Act) or the National Securities Superintendency (Article 135 of the Securities Market Act), respectively.

8.4 Are there any processes other than court proceedings that are available to a creditor to seize the assets of a company in an enforcement?

No (Articles 1844 of the Civil Code and 542 of the Commercial Code), except for retention rights (Articles 122 and 148 of the Commercial Code) and the collection of credits given as collateral (Article 538 of the Commercial Code).

9 Jurisdiction and Waiver of Immunity

9.1 Is a party's submission to a foreign jurisdiction legally binding and enforceable under the laws of your jurisdiction?

Yes, provided that it is a commercial transaction and the exceptions of national interest contract (Article 151 of the Constitution), Venezuela real estate or public policy (Article 47 of the International Private Law Act) do not apply.

9.2 Is a party's waiver of sovereign immunity legally binding and enforceable under the laws of your jurisdiction?

Yes, subject to the same conditions mentioned in question 9.1.

10 Licensing

10.1 What are the licensing and other eligibility requirements in your jurisdiction for lenders to a company in your jurisdiction, if any? Are these licensing and eligibility requirements different for a "foreign" lender (i.e. a lender that is not located in your jurisdiction)? In connection with any such requirements, is a distinction made under the laws of your jurisdiction between a lender that is a bank versus a lender that is a non-bank? If there are such requirements in your jurisdiction, what are the consequences for a lender that has not satisfied such requirements but has nonetheless made a loan to a company in your jurisdiction? What are the licensing and other eligibility requirements in your jurisdiction for an agent under a syndicated facility for lenders to a company in your jurisdiction?

There are no eligibility requirements for lenders. However, the nature of the lender may be relevant for the purposes of determining the applicable income tax regime (e.g. a 4.95% tax rate applies to interest payments to foreign financial institutions, a 34% tax rate on net income of non-bank lenders (absent a tax treaty provision) and a 40% tax rate applies on net income of local financial institutions). There is no need for the lenders to be licensed or authorised to do business in Venezuela. They do not need to be a licensed bank in the jurisdiction of incorporation.

There are differences between the authorisations required to be a beneficiary of a chattel mortgage and pledge without transfer of possession, depending on the type of lender. No authorisation is required if the lender is a local bank. Authorisation from the Superintendency of the Banking Sector Institutions will be necessary if it is a foreign bank. Authorisation from the Ministry of Agriculture or the Ministry of Communications may be needed for certain security interests in favour of other types of lenders.

For trusts created in Venezuela, the trustee must be a local bank or insurance company, authorised to operate as such and to serve as trustee, by the Superintendency of the Banking Sector Institutions and by the Superintendency of Insurance Activities.

11 Other Matters

11.1 Are there any other material considerations which should be taken into account by lenders when participating in financings in your jurisdiction?

Special consideration must be given to the existing exchange control.

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