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The International Comparative Legal Guide to:

Securitisation 2018

11th Edition

A practical cross-border insight into securitisation work

Published by Global Legal Group, with contributions from:

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URL: www.glgroup.co.uk

GLG Cover Design
F&F Studio Design

GLG Cover Image Source
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Printed by
Ashford Colour Press Ltd
June 2018

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ISBN 978-1-912509-11-9
ISSN 1745-7661

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EDITORIAL

Welcome to the eleventh edition of *The International Comparative Legal Guide to: Securitisation*.

This guide provides the international practitioner and in-house counsel with a comprehensive worldwide legal analysis of the laws and regulations of securitisation.

It is divided into two main sections:

Five general chapters. These chapters are designed to provide readers with an overview of key securitisation issues, particularly from the perspective of a multi-jurisdictional transaction.

Country question and answer chapters. These provide a broad overview of common issues in securitisation laws and regulations in 27 jurisdictions.

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

Special thanks are reserved for the contributing editor Sanjev Warna-kula-suriya of Latham & Watkins 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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Unlocking Value in Private Equity Transactions

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Introduction

It may well be the right time to consider using securitisation to unlock value in private equity transactions. The global economy and financial markets continue their robust growth, and the legal framework for securitisation continues to be stable and even welcoming – witness, for example, the recent publication of the EU's new rules for simple, transparent and standardised securitisations (the "**STS Regulation**", available at http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32017R2402&from=EN).

We discuss in turn below how securitisation can be a valuable tool in support of the private equity sector in the following two principal areas:

- securitisation as a means of financing or refinancing all or part of acquisitions of portfolio companies by private equity houses; and
- securitisation as a means of realising value in private equity investments.

Acquisition Financing

Private equity backed acquisitions customarily involve an equity component and a debt component. Typically, the "true" equity component of an acquisition will be provided by one or more limited partnerships using funds raised and managed by private equity sponsors for that purpose. In some cases, these limited partnerships will incur debt financing against either the investment commitments from limited partners or the limited partnership's investments, or both, using securitisation structures and techniques. In that manner private equity sponsors can leverage their equity funding even before it is invested in acquisitions.

The debt component of a private equity acquisition will typically be provided in the form of leveraged loans (whether senior or subordinated, first or second lien), high yield bonds, or some combination thereof. Of course, funding which acts like equity for purposes of the senior debt financing can also be provided in the form of debt incurred at one or more parent companies and then downstreamed to the acquisition vehicle, creating so-called structural subordination. Financing will be incurred at various stages in an acquisition, from the initial bridge financing, to the more permanent take-out financing, to incremental financing which permits the private equity sponsor to extract some value after a period of initial success with an acquisition, to refinancing all or any of that debt, and, finally, to funding as part of an exit from an acquisition.

Due to its structural integrity, securitisation customarily incurs lower funding costs than leveraged loans or high yield bonds. Securitisations generally result in highly-liquid assets (for example, customer payables that turn into cash within a few months) being ring-fenced from the other credit risks of the target group operating companies. The more homogenous and predictable the cash flows from the receivables, and the more impenetrable the ring-fencing, generally the lower the cost of the financing. As securitisation financing can help lower the average cost of debt in an acquisition, securitisation financing permits private equity sponsors to bid more for target groups or can help private equity sponsors increase returns on equity, or potentially both.

While securitisations can play an important role in each stage of financing, the complexity of structuring and documenting securitisation transactions means that they are more likely to be used at the permanent financing stage or thereafter, and not at the bridge financing phase when speed is essential. That being said, lawyers at this firm have completed so-called "bridge" securitisation financings which later transformed into permanent securitisation financings once certain longer-term conditions were satisfied (and at which time the advance rates in the securitisations increased and funding costs decreased).

Raising financing via the securitisation of trade receivables alongside leveraged loans and high yield bonds in private equity acquisition transactions is now very widely used, and we have written extensively on the issues involved in documenting such transactions (e.g., see our chapter for the 2017 edition of this guide, titled *Documenting Receivables Financings in Leveraged Finance and High Yield Transactions*). Typically, the package of operating covenants for such securitisation transactions will be lighter than the covenants for leveraged loans, and even high yield bonds, and such transactions may or may not have financial covenants given their focus on ring-fenced short-term receivables. It has, for example, become typical for an acquisition to be completed using leveraged loans and/or high yield bonds, and then at a later date to use the proceeds of a trade receivables securitisation to fund a shareholder dividend.

Securitisation financing can also be raised via so-called "whole-business" securitisations in which a special purpose vehicle is established to lend, to the target group, funds raised via rated debt securities secured over the assets of the target group. The cash flows of the target group as a whole are then applied to repay the loans to the issuer and the rated securities to investors. Operating and financial covenants for a whole-business securitisation tend to be largely similar to those for the leveraged loans. Whole-business securitisations generally require target groups having stable cash flows and strong market positions (including high barriers to entry). Liquidity supporting the rated securities will be essential, and there may be some sort of credit enhancement depending on the target group involved.

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Similarly, securitisation financing can be raised via so-called "Opco-Propco" structures, pursuant to which a target group is split into a property-owning part and an operating part. The property-owning part raises funds via rated debt securities secured over the properties. With the proceeds of the securities, the property-owning companies then acquire the properties and lease them to the operating part of the group. Rent on the leases is then applied to repay the securities to investors. Operating and financial covenants tend to be largely similar to those for the leveraged loans. Opco-Propco securitisations generally require target groups to have stable cash flows and strong market positions (including high barriers to entry) in addition to properties that can be sold should cash flows be insufficient to service the securities.

Finally, debt financing for private equity acquisitions is often raised by securitising the leveraged loans originally provided by lenders in the acquisitions. In fact, collateralised loan obligations, or CLOs, are now one of the biggest buyers of leveraged loans. With increasing frequency, leveraged loans are being acquired by specialist funds established by private equity sponsors for the purpose of acquiring and securitising leveraged loans and acquiring equity tranches in CLO transactions.

A traditional CLO transaction begins with a fund manager establishing a warehouse facility, usually with an arranger, pursuant to which leveraged loans are acquired from the secondary market (often, right after the loans have been made at the time of the acquisition). Once a sufficient volume of loans has been acquired, the arranger helps a special purpose vehicle issue rated securities to investors secured by the loan portfolio. The proceeds of the securities are used to repay the warehouse financing and, often, to acquire more loans during a brief ramp-up period which follows. The manager will then reinvest the proceeds of loan repayments and loan sales over a several-year reinvestment period, and thereafter the CLO will be repaid as the loans are repaid.

Specialist private equity sponsor vehicles are a more recent phenomenon. Originally set up to hold retention tranches in CLO transactions in order to meet the requirements of the EU (and, later, the US) risk retention rules, these vehicles gradually became long-term owners of leveraged loans and other non-securitised investments in part due to the EU requirement that "originators" (one type of entity permitted under EU rules to hold 5% retention interests) not be "solely" in the business of securitising assets. A number of private equity sponsors have established such vehicles which not only provide an additional source of financing for their own acquisitions without using their own balance sheet or limited partnership funding, but can also earn several layers of management fees and even access the (leveraged) excess spreads generated by the underlying assets by holding some or all of the equity in the specialist vehicle.

Realising Value

A private equity sponsor can use securitisation to realise the value of its investments in several ways. For example, the sponsor can, when selling a target group, encourage bidders to include one or more of the forms of securitisation financing described above to maximise the sale price. In addition, private equity sponsors can securitise their investments in target groups by selling those investments to special purpose vehicles established for the purpose of acquiring such equity interests. Such vehicles, sometimes known as collateralised fund obligations, or CFOs, acquire such equity interests with funds raised in the capital markets (whether or not publicly rated) or through bank financing.

The benefits of such vehicles to private equity sponsors are manifold, in addition to those described above (e.g., earning management fees). For example, whilst the primary route to realising value in investments will remain an M&A or capital markets transaction in relation to a single portfolio company, sponsors may be able to use such vehicles to monetise all or part of a portfolio investment earlier than the capital or M&A markets might otherwise allow. Such vehicles might permit a sponsor to dispose of part of a portfolio investment without losing control over the remainder. Alternatively, such vehicles might permit a sponsor to dispose of control of such a portfolio investment (and, depending on the facts, achieving off-balance sheet treatment of the target group) while retaining a minority investment and thus participating in future profits. Finally, a sponsor might be able to negotiate a right to repurchase assets from the vehicle and thus enhance the sponsor's flexibility and the potential profitability of an alternative exit in future.

In order for such vehicles to appeal to and successfully perform for investors, however, they will need to apply a variety of securitisation techniques. The cash flows from private equity investments are more unpredictable than from debt investments for several reasons, and their value is more volatile. Thus, as diverse and granular a selection as possible of underlying assets is needed. Moreover, the portfolio should have an expected realisation profile which smooths out the cash flows to be received by the vehicle to the greatest extent possible. Even then, a liquidity facility to pay interest in a timely manner on the most senior tranche of debt securities, as well as perhaps even a funding reserve or other credit or liquidity enhancement, will likely be needed. Over-collateralisation requirements are greater than for normal CLOs.

The structure customarily involves the transfer of limited partnership (LP) interests by the private equity sponsor to a special purpose vehicle. In most cases the general partner (GP) of the limited partnership will be required to consent to such transfer and also to the subsequent creation of security over the LP interests in favour of the security trustee for the securitisation. Additional points for due diligence are the provisions for "clawback" of distributions made to limited partners, and indemnities given by LPs in the partnership agreement – these features, which do not exist in normal CLOs, are factored into the rating analysis for CFOs. The structure will include over-collateralisation (OC) and Interest Cover (IC) tests similar to those used in CLOs and, sometimes, additional leverage ratios which need to be satisfied to permit distributions to the equity holder. Hedging for FX exposure may be avoided because of the significant equity cushion used for over-collateralisation.

Conclusion

Securitisation provides multiple tools for private equity sponsors to achieve higher bid prices, higher levels of acquisition financing, lower costs of funding, earlier monetisation of investments, and higher returns to investors. Securitisation transactions can at times be more difficult to structure and complete than other forms of financing, but it is always an option worth exploring carefully.

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He also has significant expertise in the sale and purchase of financial asset portfolios, distressed investments and restructurings, and the establishment of alternative lending platforms and direct lending.

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"Clients say the 'exceptional' Kem Ihenacho is 'one of the best all-round private equity lawyers we deal with'." *Chambers UK 2018.*

Mr. Ihenacho has also sat on the legal advisory boards of various private equity industry bodies.

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U.S. CLOs: The End of U.S. Risk Retention for Collateral Managers?

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Background on Risk Retention in the United States

In December 2014, the final risk retention requirements for securitisations promulgated by U.S. regulators were published in the U.S. Federal Register ("U.S. Risk Retention Rule").[1] The U.S. Risk Retention Rule requires the sponsor of the securitisation to retain an economic interest in the credit risk of the securitised assets in an amount equal to at least 5 per cent of the ABS interests issued in the transaction ("Required Retention Interest"), subject to certain exceptions. "Sponsor" is defined in the U.S. Risk Retention Rule as "a person who organizes and initiates a securitization transaction by selling or transferring assets, either directly or indirectly, including through an affiliate, to the issuing entity". The Required Retention Interest may be held in the form of an eligible vertical interest, an eligible horizontal residual interest or a combination of both. For a collateralised loan obligation transaction ("CLO"), the regulators determined that the collateral manager of the CLO is the sponsor of the securitisation; however, this determination was challenged by the Loan Syndications and Trading Association ("LSTA") in a suit against the U.S. regulators.[2] The U.S. Risk Retention Rule provides that a CLO manager may satisfy its risk retention obligations under the U.S. Risk Retention Rule by holding the Required Retention Interest either directly or through a "majority-owned affiliate". The U.S. Risk Retention Rule defines a majority-owned affiliate as "an entity (other than the issuing entity) that, directly or indirectly, majority controls, is majority controlled by or is under common majority control with" the CLO manager. For this purpose, majority control means the "ownership of more than 50 per cent of the equity of an entity, or ownership of any other controlling financial interest in the entity, as determined by GAAP".

The U.S. D.C. Circuit Court Ruling

On February 9, 2018, a three-judge panel of the U.S. Court of Appeals for the District of Columbia (the "D.C. Circuit Court") unanimously ruled in favour of the LSTA in its lawsuit against the Securities and Exchange Commission ("SEC") and the Board of Governors of the Federal Reserve System ("FRB") over the application of U.S. credit risk retention requirements to managers of open-market CLOs.[3]

The D.C. Circuit Court concluded that managers of "open-market CLOs"[4] are not subject to the credit risk retention rules mandated by Section 941 of The Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank Act"). The D.C. Circuit Court reasoned that because open-market CLO managers do not sell or transfer assets to the CLO, they are not "securitizers"[5] under Section 941 of the Dodd-Frank Act, and therefore they need not retain any credit risk in the open-market CLOs they manage. In reaching its conclusion, the D.C. Circuit Court agreed with the LSTA's primary contention that "given the nature of the transactions performed by CLO managers, the language of the statute invoked by the agencies does not encompass their activities".

Background on the U.S. Risk Retention Rule's Application to Open-Market CLOs

In the release adopting the U.S. Risk Retention Rule ("Release"), the federal agencies (the SEC, the FRB, the Office of the Comptroller of Currency, the Federal Deposit Insurance Corporation, the Department of Housing and Urban Development and the Federal Housing Finance Agency) that jointly adopted the U.S. Risk Retention Rule ("Agencies") stated that the manager of an open-market CLO "generally acts as the sponsor by selecting the commercial loans to be purchased by the CLO issuing entity and managing the securitised assets once deposited in the CLO structure, which the [A]gencies believe is a transfer or indirect transfer of the assets". The Agencies rejected definitional and policy arguments that the manager of an open-market CLO is not a statutory "securitizer" under Section 941 of the Dodd-Frank Act, asserting that its interpretation of the term "securitizer" was both "reasonable" and "consistent with the context, purposes and legislative history of the statute".

The LSTA filed suit against the SEC and the FRB in November 2014, challenging the application of risk retention under the Final Rules to open-market CLO managers. Specifically, the LSTA argued that, in their promulgation of the U.S. Risk Retention Rule, the Agencies violated the Administrative Procedure Act by arbitrarily and capriciously: (1) construing the term "securitizer" to include open-market CLO managers; (2) requiring "securitizers" to retain a 5 per cent interest based on "fair value" instead of "credit risk", as required by statute; and (3) declining to exempt open-market CLO managers from the retention requirements or to modify those requirements to reflect industry best practices to retain the benchmark level of credit risk without committing excessive capital. The U.S. District Court for the District of Columbia ("District Court") granted judgment in favour of the SEC and FRB in December 2016,[6] after which the LSTA appealed to the D.C. Circuit Court.

The D.C. Circuit Court reversed the District Court decision, agreeing with the LSTA that an open-market CLO manager is not a "securitizer" under Section 941 of the Dodd-Frank Act and,

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consequently, is not subject to the statute's credit risk retention requirements. The D.C. Circuit Court observed that the statute is designed to reach those entities that organise and initiate securitisations "by transferring" assets to issuers. The D.C. Circuit Court acknowledged that the manager of an open-market CLO "organizes and initiates" a CLO transaction, but it dismissed the proposition that a manager's causal role in the acquisition of assets by a CLO issuer from third parties amounts to a "transfer" within the ordinary meaning of that term, or that a manager can be said to "retain" credit risk within the mandate of the statute by purchasing an interest (i.e., the retention interest) in an asset that it has never before held:

> "In their ordinary meaning, words directing that one who "transfers" an asset must "retain" some interest in the associated risk refer 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—that is, the entity is in a position to limit the scope of a transaction so that it transfers away less than all of the asset's credit risk."
>
> "The [A]gencies' interpretation seems to stretch the statute beyond the natural meaning of what Congress wrote; it turns 'retain' a credit risk into 'obtain' a credit risk."

Open-market CLO managers, the D.C. Circuit Court observed, "neither originate the loans nor hold them as assets at any point. Rather, like mutual fund or other asset managers, CLO managers only give directions to an SPV and receive compensation and management fees contingent on the performance of the asset pool over time". To be a "securitizer" within the meaning of the statute, the D.C. Circuit Court concluded, a party "must actually be a transferor, relinquishing ownership or control of assets to an issuer".

The Agencies did not seek review *en banc* of the D.C. Circuit Court ruling, and on April 5, 2018, the District Court granted a summary judgment in favour of the LSTA and vacated the U.S. Risk Retention Rule as it applied to collateral managers of open-market CLOs. The Agencies have the right to request review by the U.S. Supreme Court until May 10, 2018 (or a later date, if granted an extension), but as of the date of this article, the D.C. Circuit Court ruling is fully effective.

Reissuance Transactions

Immediately after the effective date of the U.S. Risk Retention Rule, many CLOs began refinancing, typically at the direction of holders of the CLO subordinated notes ("CLO equity"), CLO notes that were priced prior to December 24, 2014. In the Crescent no-action letter,[7] the SEC concluded that such CLOs could refinance each class of their senior notes once after December 23, 2016 without complying with the U.S. Risk Retention Rule, if the refinancing met the conditions in the letter. One of the conditions in the letter was that each class of notes will be subject to only one refinancing and the supplemental indenture executed in connection with the refinancing of each class will prohibit any further refinancing of the refinanced notes.

In the current market, many CLOs are conducting "resets" in which the holders of the CLO equity direct the refinancing of the senior debt and, in connection therewith, amend certain material terms of the CLO, including extending the maturity date, non-call periods and reinvestment periods. In CLOs that already refinanced based on the Crescent no-action letter, the indenture contains a prohibition against a subsequent refinancing even if the CLO manager complies with the U.S. Risk Retention Rule. In these instances, CLO investors are implementing "reissuances" or "call and roll" transactions, whereby the existing CLO conducts a redemption by liquidation of its notes and a sale of the CLO's assets to a new CLO managed by the same manager. Such sales are conducted on an arm's-length basis.

The market is grappling with the question as to whether or not the new CLO should be viewed as an open-market CLO under the D.C. Circuit Court's ruling in view of the transfer of assets from the existing CLO to the new CLO. We believe that the new CLO should be viewed as an open-market CLO. The D.C. Circuit Court decision is premised on the manner in which the loans are acquired by the CLO. In the new CLO, the manager of the CLO is directing the acquisition of the loans from the existing CLO on an arm's-length basis.

Dual Compliant CLOs

Many managers of U.S. CLOs have complied with the EU risk retention requirements in order to sell to European investors. The EU risk retention rules require the "originator", "sponsor" or "original lender" to retain the 5 per cent net economic interest.[8] A CLO manager may retain the risk of a CLO if it has been authorised as an investment firm subject to CRD IV or if it is the "originator" for the CLO. An "originator" is defined for purposes of Article 405 to include "an entity that purchases a third party's exposures for its own account and then securitizes them". To date, CLO transactions marketed in the EU have typically been structured on the basis that an entity which (i) acquires loans in the secondary market, (ii) holds those loans for a period of time and (iii) subsequently sells those loans to the CLO, may qualify as the originator for that CLO. In many cases, the CLO manager has also acted as the "originator" for the CLO. The D.C. Circuit Court decision did not address whether such "origination" activities would cause the CLO to no longer qualify as an open-market CLO and cause the CLO manager to be the "sponsor" of the CLO which is required to hold the Required Retention Interest. Market participants have begun changing the way a CLO manager "originates" loans for purposes of the EU risk retention requirements. Rather than having the CLO manager purchase the loans in the open market and holding the loans on its balance sheet for a period of time prior to selling the loans to the CLO issuer, the CLO issuer will purchase loans in the open market subject to the obligation of the CLO manager to purchase any loans from the CLO issuer that default prior to the requisite period of time being exhausted. Another more common method for a CLO manager to "originate" loans for a CLO is for the manager to simultaneously make a forward purchase of a loan from a dealer and a forward sale of the same loan to the CLO at the same price, so that if, on the forward settlement date the loan continues to meet the CLO's eligibility criteria, it will be purchased directly by the CLO from the dealer. Although this method of purchasing assets for a CLO was not addressed directly in the D.C. Circuit decision, we think there are compelling arguments that it is consistent with the CLO constituting an open-market CLO.

Middle-Market CLOs

Many lenders in the middle-market loan space are private investment funds managed by investment managers. The D.C. Circuit Court ruling carved out balance sheet and middle-market CLOs from its ruling by stating (in a footnote to the ruling) that their general use of the term "CLO" referred only to open-market CLOs. However, the ruling may have an impact on middle-market CLOs implemented by private investment funds. Currently, the managers of such CLOs have been viewed as the "sponsor" of the CLO. However,

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the D.C. Circuit Court ruling that managers of open-market CLOs do not "transfer" assets within the meaning of the statute opens the possibility that the U.S. Risk Retention Rule should not apply to managers of middle-market CLOs because such managers do not transfer assets to the CLOs which they manage; instead, the assets are transferred to the CLO by other funds under common management. However, in the Release, the Agencies stated that the investment manager of a private investment fund should be considered to be the "sponsor", since the fund itself would not qualify as a "sponsor". "Thus, for example, an entity that … only purchases assets at the direction of an independent asset or investment manager … would not qualify as a 'sponsor'". Therefore, one question is whether this precatory language in the Release has now been superseded (and in effect overruled) by the D.C. Circuit Court ruling, so that an investment fund which transfers loans to a CLO may act as the sponsor and hold any Required Retention Interest.

Applicability to Other Types of Transactions

The holding of the D.C. Circuit Court decision is by its terms limited to open-market CLOs. However, the principles of the decision can be applied to other types of securitisation transactions that are similar to open-market CLOs in that the party which heretofore has been identified as the "sponsor" does not itself transfer any of the securitised assets to the securitisation issuer. For example, collateralised bond obligation transactions ("CBOs") are structurally identical to open-market CLOs, except that they invest in bonds as well as loans. If a CBO issuer buys its bonds only through arm's-length market transactions, and the CBO manager has a similar role to a CLO manager, the U.S. Risk Retention Rule should not apply to the CBO manager under the same rationale that they do not apply to a CLO manager.

There are a range of other securitisation transactions that may no longer be covered by the U.S. Risk Retention Rule, because there may be no "sponsor" of the transaction based on the reasoning of the D.C. Circuit Court decision. The question will be whether or not there is a "transferor" within the meaning of the U.S. Risk Retention Rule. The D.C. Circuit Court rejected arguments advanced by the SEC and the FRB that interpreting Section 941 as not applying to open-market CLO managers "would do violence to the statutory scheme" and "creat[e] a loophole that would allow "securitizers" of other types of transactions to structure around their risk retention obligation", offering several explanations for why the "feared hypothetical loophole is unlikely to materialize".

Potential Legislative Actions

In March 2016, HR 4166 (which is sometimes referred to as the "QCLO Bill") passed the House Financial Services Committee 42-15, with 10 Democrats supporting the bill. The QCLO Bill proposed to reduce the risk retention requirements for "qualified" CLOs (a "QCLO"), which meet six requirements: (i) quality of assets; (ii) portfolio diversification; (iii) minimum capital structure; (iv) alignment of interests; (v) reporting and disclosure; and (vi) manager regulation. The risk retention requirement for a QCLO would be reduced to 5 per cent of the CLO equity, as opposed to equity which has a fair value equal to 5 per cent of the fair value of the securities issued by the CLO. If a CLO did not meet these restrictions, the CLO manager could still retain an eligible vertical interest or eligible horizontal residual interest under the existing rule.

Since 2017, Republicans have controlled the House, the Senate and the Presidency. Because the QCLO bill passed the House Financial Services Committee with bipartisan support, there had been hope that it would pass the full House. If it then was approved by the Senate, most commentators believed that President Trump would sign it. However, the QCLO Bill never passed the full House. On September 14, 2017, the QCLO Bill was re-introduced as H.R. 3772. This 2017 version of the QCLO Bill is almost identical to the 2016 version, with a slight Democratic-led amendment to the retention structure, whereby the retention amount was to remain the same, but was to be comprised of 70 per cent equity and the remaining 30 per cent in a vertical strip. However, President Trump and many Republican Congressmen have supported a broader effort to repeal much of the Dodd-Frank Act (pursuant to which the U.S. Risk Retention Rule was adopted), and the QCLO Bill, in either form, has yet to come up for a vote, and may be superseded or continue to be delayed by this broader legislative effort.

This legislative initiative has been supported by the LSTA, but the D.C. Circuit Court ruling discussed above would seem to obviate the need for any further movement on the current QCLO Bill which is still stalled in Congress.

Treasury Report

In its October 2017 report, the U.S. Department of the Treasury noted that, under Dodd-Frank, a sponsor of an asset-backed security is generally required to retain at least 5 per cent of the credit risk of the assets collateralising the securities. In the U.S. Risk Retention Rule, the Agencies subjected CLO managers to this risk retention requirement by determining that they fell within the statutory definition of a "securitizer". For most securitised products, an originator may originate the loans with the intention of selling them. In contrast, CLO managers do not originate the underlying loans which they choose for the CLO vehicle. CLO managers are typically compensated with management fees which are contingent on the performance on the underlying loans. In this way CLO managers are more like asset managers than "securitizers". Treating them like typical "securitizers", including the burden of credit risk retention, limits their access to capital in the markets. It could also cause smaller CLO managers to exit the market due to this reduced ability to raise capital, possibly creating an undesirable consolidation effect among the larger servicers.

In its report, the Treasury Department noted that credit risk retention is an "imprecise mechanism" for creating alignment between sponsors and investors. But, rather than a broad repeal of the requirement, it states that the regulators should expand exemptions based on the characteristics of eligible asset classes. For CLO managers specifically, the Treasury Department recommends a broad qualified exemption for CLO credit risk retention. Since CLO managers have the ability to discriminate as to the quality of loans they select, the qualified exemption should not be a complete exemption but instead a set of requirements for specific loan types which would be implemented through notice-and-comment rulemaking by the Agencies (where Congress should designate a lead agency from among the six Agencies in order to avoid procedural and interpretive challenges).

Conclusion

The D.C. Circuit Court ruling, if it is not challenged and overturned by the United States Supreme Court, invalidates the application of the U.S. Risk Retention Rule to managers of open-market CLO transactions. The D.C. Circuit Court's ruling is limited to open-market CLO transactions; however, the reasoning of the D.C. Circuit Court ruling extends to other types of CLOs and securitisations

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where the manager does not transfer assets to the CLO issuer. Until the regulators or the courts provide clarity on the applicability of the U.S. Risk Retention Rule to such transactions, it is likely that market practice will develop in a way that will apply the court's reasoning to other CLO structures and securitisations to which it is clearly applicable.

Acknowledgment

The authors would like to acknowledge the assistance, in the preparation of this chapter, of **Paul N. Watterson, Jr.**, a partner in the Structured Finance & Derivatives Group at Schulte Roth & Zabel LLP. Mr. Watterson concentrates on structured product and derivative transactions, the formation and representation of credit funds and capital markets regulation, and is counsel to many participants in the securitisation, credit and derivatives markets. He represents underwriters, issuers and managers in structured financings, including collateralised loan obligations (CLOs) and is involved in many structured finance transactions that use credit derivatives, including regulatory capital transactions and re-packagings. Mr. Watterson earned his A.B., *cum laude*, from Princeton University, and his J.D., *magna cum laude*, from Harvard Law School.

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Endnotes

1. Credit Risk Retention, 79 Fed. Reg. 77602 (December 24, 2014).
2. *In re The Loan Syndications and Trading Association v. United States Securities and Exchange Commission; Board of Governors of the Federal Reserve System*.
3. *Loan Syndications & Trading Ass'n v. SEC*, No. 17-5004 (D.C. Cir. February. 9, 2018).
4. The D.C. Circuit Court described "open-market CLOs" as CLOs in which the loan assets are acquired from "arms-length negotiations and trading on an open market", contrasting them with "balance sheet CLOs" which are "created, directly or indirectly, by the originators or original holders of the underlying loans to transfer the loans off their balance sheets and into a securitization vehicle". *Id*. at 3.
5. "Securitizer" means, with respect to a securitization transaction, either: (1) the depositor of the asset-backed securities (if the depositor is not the sponsor); or (2) the sponsor of the asset-backed securities.
6. *Loan Syndications & Trading Ass'n v. SEC*, 223 F. Supp. 3d 37 (D.D.C. 2016).
7. Crescent Capital LP, SEC No-Action Letter (July 17, 2015).
8. Regulation (EU) No 575/2013 of the European Parliament and of the Council of June 26, 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012, 2013 O.J. L 176/1.

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Schulte Roth & Zabel LLP (www.srz.com) is a market-leading law firm serving the financial services industry from offices in New York, Washington, D.C. and London. Our Structured Finance & Derivatives Group is widely recognised as one of the most sophisticated in the legal profession. We structure and negotiate a variety of complex finance and securitisation transactions – including collateralised loan obligations and asset-backed securitisations, as well as regulatory capital offerings – on behalf of a wide range of market participants including investment managers, issuers, purchasers and sellers of assets, underwriters, placement agents, borrowers and investors. We have extensive expertise structuring, negotiating and drafting all types of structured finance transactions in connection with mortgage-backed and asset-backed securities offerings and structured financing transactions involving the more "exotic" asset types including insurance contracts, structured settlements, litigation claims and cell towers. We have also advised clients on synthetic securitisations involving high-yield loans and bonds, and investment-grade loans and bonds, including regulatory capital transactions and warehouse/portfolio financings structured as total return swap or repurchase facilities. In addition to structuring, drafting and negotiating, we represent clients with regulatory filings, compliance issues and investigations. We also advise clients in complying with the risk retention regulations in the United States and the EU, including assisting clients in the creation of risk retention vehicles. We have acted as deal counsel for many collateralised loan obligations ("CLOs"), as well as collateralised bond obligations ("CBOs"). These transactions have involved the securitisation of high-yield loans and bonds, investment-grade corporate debt, credit default swaps, and interests in hedge funds.

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Regulatory Drivers of Securitisations

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Introduction

Securitisations have a long-established history as funding vehicles for comparatively illiquid assets. The ability to acquire a broad range of financial assets and to create tranches with specified seniority, maturity and return characteristics including credit ratings as high as "AAA" means that securitisations can be used to tailor the duration and credit risk of an investment to the specific needs of various investor classes while addressing idiosyncrasies of a broad range of asset classes. These forces have combined to drive many of the securitisation features we recognise as standard today. Another major driver of securitisations is the regulatory environment facing lenders, banks in particular. With the introduction of the Basel capital standards, securitisations came to be increasingly driven by strategies to optimise the bank's balance sheet within the confines of the Basel capital requirements. As securitisations have adapted to the Basel rules, so too have the Basel rules evolved to address the perceived shortcomings and encourage the perceived benefits of securitisations. Prior editions of this chapter explored the development of the Basel Rules and the manner in which the Basel III capital rules applicable to securitisations have changed to reflect the lessons of the 2008–2009 financial crises. However, the impact of the Basel III rules on securitisations goes well beyond the securitisation capital framework. The generally increased capital requirement imposed by the Basel III framework, combined with additional requirements imposed by various leverage ratios, the liquidity coverage ratio and the net stable funding ratio, further incentivises banks to engage in optimisation strategies that involve the transfer of assets or their associated risk while retaining other aspects of the relevant lending business.

As the impact of the Basel III framework ripples through the financial system and banking institutions adjust and adapt their activities to the evolving capital and regulatory regime, there are significant consequences for the parts of the market where banks can no longer provide sufficient cost-effective financing. Securitisations have the ability to bridge that gap but will also be subject to various requirements and restrictions that will have to be successfully navigated. This article will explore some of the resulting securitisation structures and current developments that are shaped by this continually evolving regulatory environment. Firstly, however, the article will summarise some elements of the Basel III regime in general and the securitisation framework specifically.[i]

The Basel Framework

The Basel Committee on Banking Supervision (the "Basel Committee") has been establishing internationally coordinated capital frameworks for banks dating back to December 1987. The financial crises of 2008 and 2009 resulted in a fundamental review of the Basel capital regime and a revised framework that reflects major changes to the market risk capital rules and additional ratios and requirements was adopted in December 2010 and further revised and refined thereafter for a revised capital regime ("Basel III").

Basel III effectively establishes financial coverage ratios that require banks to maintain certain minimum amounts of capital to total risk-weighted assets ("Capital Ratios"), maintain a certain minimum of capital to total assets ("leverage ratio"), and have high quality investments and access to stable funding to meet their short-term and long-term funding obligations.

The general construct of the Basel III risk-based capital standards is similar to prior Basel standards, but with more stringent limits and a number of other adjustments reflecting the experiences over the intervening years. In the U.S. the minimum common equity Tier 1 capital (primarily common stock) is 4.5% of total risk-weighted assets; the required ratio of all Tier 1 capital instruments to total risk-weighted assets is 6% and the total Tier 1 and Tier 2 capital (primarily common stock and certain preferred and subordinated debt) to risk-weighted assets is 8%. The risk-weighted capital rules, provide detailed provisions for various types of exposures, each being assigned a percentage that will then be multiplied by the capital ratio to determine the amount of capital that will effectively be reserved for that particular exposure. These percentages generally range from 20% to 1,250% (resulting in a deduction against capital ranging from 1.6% to 100% of equity assuming an equity ratio of 8% but which will be higher, and could result in more than 100% deduction against equity, where the required equity ratio exceeds 8%). Certain off-balance sheet or contingent liabilities have an additional multiplier, referred to as a conversion factor, which further reduces the amount of capital that needs to be held against the exposure.

Additional elements of the risk-based capital rules imposed as part of Basel III include: (i) a capital conservation buffer designed to strengthen banks' resilience during economic cycles which, when fully phased in, will be 2.5% and added to the 4.5% generally applicable minimum amount of common equity Tier 1 capital to total risk-weighted assets. U.S. banking organisations that fail to meet the capital conservation buffer are subject to restrictions on their capital distributions, including certain bonus payments to executives; (ii) a countercyclical buffer ranging from 0 to 2.5% (currently at 0%), which is a macroprudential tool that can be used to increase the capital requirements on internationally active banking organisations when there is an elevated risk of above normal losses in the future; (iii) capital requirements for certain investments in the equity of funds held in the banking book, which

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contemplate that such exposures will be deducted from equity or given a risk-weighted capital charge of 1,250% unless the fund can apply a look-through approach to such fund investments; (iv) a revised, standardised, approach for measuring counterparty credit risk exposures; (v) revisions to the securitisation framework issued in December 2014 and July 2016 to strengthen the capital standard for securitisation exposures held in the banking book; and (vi) initial and variation margin requirements for non-centrally cleared derivatives.

The risk-based capital regime is based on the common-sense notion that less capital is required to be reserved against low risk exposures while higher-risk exposures require more capital capable of absorbing losses to be reserved.

The leverage ratio introduced as part of the Basel III regime imposes a minimum ratio of Tier 1 Capital to total on- and off-balance sheet leverage. Generally, the leverage ratio is calculated on the basis of applicable accounting principles for the purposes of determining the on-balance sheet exposure, which is further adjusted by adding back in certain off-balance sheet exposures (by multiplying such exposures by the applicable credit conversion factor), backing out certain collateral and other risk mitigants and making certain additional adjustments for derivatives and assets that have been deducted from capital to arrive at the relevant exposure. The leverage ratio is intended to reduce the overall leverage of a relevant institution, but because that ratio does not adjust for the underlying risk, the leverage ratio creates an incentive to invest in higher-returning, and therefore riskier, assets. In jurisdictions with a high leverage ratio, such as the U.S., banking institutions are likely to be constrained by the leverage ratio rather than the capital ratios, which will drive certain balance sheet optimising activities different from those of banks primarily constrained by the risk-based capital ratios, and which will therefore have an incentive to optimise their risk-weighted return similar to that under prior iterations of the Basel standard.

The Basel Committee has mandated a minimum leverage ratio of 3%. However, some jurisdictions have imposed higher requirements. For example, the U.S. has implemented a 4% Tier 1 Capital to total leverage ratio and, in addition, imposed a 3% supplemental leverage ratio, effective from January 1, 2018, for banking organisations that are subject to the Basel III "advanced approaches" (i.e. using approved internal models to determine the appropriate weighting of various risk-weighted assets). These are banking entities that, together with their subsidiaries, hold consolidated assets of $250 billion or more or consolidated on-balance sheet foreign exposures of $10 billion or more. The U.S. has also imposed enhanced supplemental leverage ratios applicable to global systemically important bank holding companies ("G-SIBs") which, when effective starting 2018, will require an additional 2% to be added to the supplemental leverage ratio (for a supplemental Leverage Ratio of 5% in total) to avoid restrictions on capital distributions and discretionary bonus payments. In addition, in order to be considered "well capitalised" (which brings with it, further regulatory benefits without which banking operations are subject to stricter scrutiny and consent requirements) a U.S. G-SIB bank (as opposed to bank holding company) must add an additional 1% to the Supplemental Leverage Ratio for a total Supplemental Tier 1 Leverage Ratio of 6%.

Basel III also calls for certain liquidity standards to apply to a bank's net short-term funding liabilities and a bank's long-term funding needs. The liquidity coverage ratio addresses a bank's short-term liquidity needs and requires it to hold "High Quality Liquid Assets" sufficient to meet 100% of its net funding needs over a 30-day period. The net stable funding ratio supplements the liquidity coverage ratio, and seeks to determine the extent to which a firm has long-term funding available to satisfy its long-term funding needs and is intended to discourage excessive "maturity transformation" where banks rely on short-term funding to carry long-term investments. The Basel III rules require banks' available stable funding sources over a one-year look-forward period to meet or exceed such bank's stable funding needs over such period.

In the U.S., ratings assigned by credit rating agencies are not permitted to be considered as part of the Basel III capital framework. Instead, the risk-adjusted capital is determined either based on internal models where approved by the relevant banking entities or by application of the standardised approach. However, it is useful to look to the risk weights that would apply under the Basel III ratings approach in order to get a general sense for the general risk-weighted capital requirements and how they differ across different asset classes, maturities and credit risks.

For example, for general corporate exposures, project finance object finance and commodities finance, and certain securitisation exposures, the risk weights under the Basel III general framework would be as follows:[ii]

Rating	**AAA to AA-**	**A+ to A-**	**BBB+ to BBB-**	**BB+ to BB-**	**Below BB-**	**Unrated**
Risk weight where ratings approach permitted	20%	50%	75%	100%	150%	100% (or 85% if small or medium enterprise (SME))
Corporate Exposures – Standardised Credit Risk Assessment Approach (SCRA)	65%			100%		
SME Corporate Exposures – SCRA	85%					
Project finance SCRA	130% pre-operational phase 100% operational phase 80% operational phase (high quality)					
Object finance and commodity finance	100%					
Securitisation ratings based (longer than one year maturity) Senior Tranche	AAA: 20% AA+: 30% AA: 40% AA-: 50%	A+: 50% A: 60% A-: 70%	BBB+: 90% BBB: 105% BBB-: 140%	BB+: 160% BB: 180% BB-: 225%	B+: 280% B: 240% B-: 420% CCC+: 505% Below: 1,250%	
Securitisation Junior Tranche (thin tranche) (longer than one year maturity)	AAA: 70% AA+: 90% AA: 120% AA-: 140%	A+: 160% A: 180% A-: 210%	BBB+: 260% BBB: 310% BBB-: 420%	BB+: 760% BB: 860% BB-: 950%	B+: 950% B: 1,050% B-: 1,150% CCC+: 1,250% Below: 1,250%	

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Utilising Securitisations for Balance Sheet Optimisation

The various Basel III requirements and their interplay are complex and differ somewhat between jurisdictions. Financial institutions will consequently have different sensitivities. For example, a bank outside the U.S. may be subject to improved capital charges if a borrower has a rating, whereas in the U.S., such ratings will not determine the applicable risk weight. An institution that is limited by the leverage ratio may determine that it will look to riskier credits to clear its hurdle rates, whereas a firm that is more constrained by its risk-weighted capital requirements may determine that it is economically more feasible to take a higher rated exposure. The liquidity ratio will impact funding commitments, and effectively increase a bank's cost of making undrawn revolver commitments, delayed draw term loans and letters of credit commitments. Similarly, the way in which banks will value certain collateral and guarantees will differ based on their other exposures and applicable manner in which they calculate their capital requirements.

As noted in the table above, a bank with loan exposures to sub-investment grade corporate borrowers can convert a substantial portion of their exposures into AAA exposures using a securitisation model similar to what is typically found in the CLO space. By further laying off the subordinated risk through an eligible guarantee or credit derivative, the bank will be able to significantly reduce the capital costs, effectively lowering the AAA piece from 100% to 20% and, assuming that the guarantor has a rating in the single A range, reducing the risk weight for the guaranteed portion to around 50%. In fact, this is consistent with the re-emergence of synthetic securitisation transactions where the credit risk related to loan exposures held by banks is transferred in whole or in part through a credit linked note or other credit protection instrument or derivative. Those structures permit banks to continue to be the lender of record for the relevant loans while shifting the credit risk to the capital market through a securitisation. A bank that is primarily constrained by the risk-weighted capital ratios, may determine that synthetic securitisations provide the optimal intersection between capital relief and control over the underlying asset. However, in order for collateral, guarantees, credit derivatives and other credit risk mitigation techniques for hedging the underlying exposure to be recognised for risk-based capital purposes, the operational criteria must be satisfied. Under the Basel III securitisation framework, these include compliance with generally applicable Basel III requirements relating to counterparty exposures including those relating to what constitutes eligible collateral, provided that securitisation SPEs are not recognised as eligible guarantors for purposes of that framework such that the exposure will have to look to collateral or other guarantors. Banks must transfer significant credit risk associated with the underlying exposures to third parties and the instruments used to transfer credit risk may not contain terms or conditions that limit the amount of credit risk transferred. The CRR gives two examples of when significant risk is deemed to have been transferred: (a) where the originator holds a mezzanine position (within the meaning of the CRR) for which the risk-weighted exposure does not exceed 50% of the risk-weighted exposure of all mezzanine transactions; and (b) in a securitisation without a mezzanine tranche, the originator does not hold more than 20% of the 1,250% securitisation exposures and such exposures exceed expected loss by a substantial margin.[iii] In other circumstances, a substantial risk may be viewed as transferred if the originator can demonstrate in every case that the reduction of own funds is justified by the transfer of credit risk to third parties.[iv]

In order for a synthetic securitisation to provide relief under the risk-weighted capital rules, the synthetic securitisation must provide a credit mitigant that is in the form of either (a) financial collateral, (b) an eligible guarantee, or (c) an eligible credit derivative. The terms of the relevant credit mitigant cannot contain any of the prohibited provisions (i.e. any provision that (i) allows for the termination of the credit protection due to a deterioration in the credit quality of underlying assets, (ii) requires the relevant bank to alter or replace underlying exposures to improve the credit quality of the underlying exposures, (iii) increases the cost of credit protection in response to a deterioration of the credit quality of the underlying exposures, (iv) increases the yield payable to parties other than the bank as a result of deterioration of the credit quality of the underlying exposures, or (v) provides for increases in retained first loss positions or credit enhancement provided by the bank after inception of the securitisation). Furthermore, the bank must obtain a well-reasoned opinion from legal counsel that confirms the enforceability of the credit risk mitigant in all relevant jurisdictions and any clean-up calls must be exercisable solely at the discretion of the bank or the servicer, must not be structured to avoid allocating losses to securitisation exposures held by investors or otherwise structured to provide credit enhancement to the securitisation and, in case of a synthetic securitisation, can only be exercisable when 10% or less of the of the principal amount of the underlying exposures or the securitisation exposures compared to the exposures at inception remain outstanding.

A fully-paid credit linked note ("CLN") will result in a full transfer of the risk without any further capital charges. On the other hand, a credit default swap that is not fully collateralised or collateralised with assets that are subject to a risk weighting factor greater than zero will introduce risk either to the counterparty or to the underlying collateral. The single counterparty exposure limits imposed under the Dodd Frank Act and the large exposure regime in the EU also provides limitations on banks' abilities to use synthetic instruments to transfer their risk exposures.

However, as hinted at above, even if a synthetic securitisation is effective in transferring risk for capital ratio purposes, the underlying exposures will still come into play as part of the leverage ratio calculations and, as such, may not provide the desired relief in those circumstances. The market for synthetic securitisations is also much smaller and investors are still sceptical to certain synthetic exposures of the type that have given rise to certain conflicts of interest legislation, though not yet any implementing rules, under the Dodd Frank Act. Such securitisations are also viewed as more complex and thus less desirable in the current market, which puts a premium on simplicity. For these reasons, it is likely that traditional securitisations will take on a greater role in balance sheet optimisations, even where the goal is to optimise for risk-weighted capital ratio purposes. The inherent risk-reducing effects of pooling and the credit enhancements afforded senior investors through tranching, combined with the capital costs faced by banks, have driven a robust pipeline of open-market CLOs where third-party managers are investing in loans acquired from originators and secondary-market sellers. A bank that wishes to retain the lending relationship with the borrowers and that is aiming for optimisation of capital requirements dictated by the risk-weighted asset requirements, may find synthetic securitisation structures to be more attractive than an outright sale to a secondary-market CLO where the lender risks losing the direct relationship with the borrower. However, because synthetic securitisations do not transfer the underlying exposures off-balance sheet, such structures do not

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address any capital requirements resulting from application of the leverage ratio. As such, a bank that is currently constrained by the leverage ratio rather than the risk-weighted capital requirements would be better off using a "true sale" securitisation structure whereby the assets are transferred off the bank's balance sheet. It is possible to structure the true sale transfer of the asset such that the bank remains the holder of record, and therefore also remains in the lender-borrower relationship as if the loans had not been sold to a securitisation, by using a structure, such as a New York law-governed participation agreement, whereby the transferor bank retains title, but the economic, and therefore "true", ownership is transferred to a third-party purchaser. Such a transfer structure may represent a "best of both worlds" type of securitisation transaction by combining the benefit of a true sale securitisation with that of a synthetic securitisation. In fact, there are structures emerging whereby lenders are transferring to CLOs revolving exposures through participation agreements that provide the borrower with the credit risk of the original lender, while the original lender in turn has transferred the credit risk to the securitisation. Such a securitisation, when appropriately structured, would also permit a bank to determine that the liquidity risk and funding risk for purposes of the liquidity coverage ratio and net stable funding ratio have both been transferred to the securitisation entity thereby providing further capital relief for the bank. The bank's continued involvement with the underlying participated asset will require careful attention to accounting requirements to obtain off-balance sheet treatment of the securitisation vehicle in order to satisfy the operational criteria for risk transfer through a traditional securitisation. This exercise has become more involved post-crises as a result of accounting changes that, amongst other things, eliminated the concept of "qualifying special purpose entities" which essentially afforded off-balance sheet treatment to most, if not all, securitisation special purpose entities. However, off-balance sheet treatment is routinely achieved using standard, generally accepted techniques and does not present an insurmountable hurdle.

A bank that is primarily constrained by the leverage ratio will likely look primarily to traditional securitisations for relief. In doing so, the bank must ensure that it complies with the operational criteria for such securitisations. The Basel III operational requirements for traditional securitisations are as follows: (a) the transfer of significant credit risk associated with the underlying exposures to third parties; (b) the transferor does not maintain effective or indirect control (defined as a right to repurchase to realise their benefits or an obligation to retain the risk) of the transferred exposures; (c) the exposures are legally isolated from the transferor, through true sale or sub-participation, such that they are beyond the reach of the transferor's creditors, even in bankruptcy or receivership; (d) the transferee is a special purpose entity (SPE) where the holders of the beneficial interests in that entity have the right to pledge or exchange such interests without restriction; (e) any clean-up calls must meet the following criteria ((x) exercise must be at the bank's discretion (cannot be mandatory); (y) cannot be structured to provide credit enhancement or for investors to avoid losses; and (z) can only be exercisable when 10% or less of original underlying portfolio or issued securities remains); (f) the securitisation does not contain provisions that (x) require the originating bank to alter the underlying exposures to enhance credit quality (other than through sale at market prices to third parties); (y) allow the originating bank to increase its retained first-loss position or any credit enhancement provided by it; or (z) increase the yield payable to any party other than the bank in response to a deterioration in the credit quality of the underlying pool; and (g) no termination options or triggers except eligible clean-up calls, termination for specific changes in tax and regulation or permitted early amortisation provisions.

The disincentive provided by the Basel III rules on infrastructure financing coupled with the significant needs to unlock a more rapid financing structure for infrastructure projects is currently driving a number of projects at the G-20 level and also at the World Bank and other multi-national entities to further determine how infrastructure financing can be provided more rapidly and cost-efficiently including through securitisations. There are examples of infrastructure CLOs having been done, and securitisations have become common for certain types of infrastructure projects such as solar financing and toll roads. Although there are a number of hurdles in different countries that need to be addressed for infrastructure loans (especially for projects in emerging markets) to become a significant viable securitisation asset class, there is a growing recognition that bank lenders will become increasingly less able to continue in their traditional financing role absent a securitisation or other take-out structure, given the Basel III considerations. At the same time, there is a recognition that simply transferring the relevant risk to a securitisation entity and ultimately the investors, also does not always work efficiently. While there are certain risks that effectively can be held by a securitisation entity, there are other risks, such as political risks, that may be more efficiently held by entities other than securitisation SPVs. This focus on risk allocation and potential "conforming" loan standards may, in turn, drive a standardisation process of "conforming" infrastructure loans which, in turn, may cause a significant increase in infrastructure financing in general and a surge in infrastructure securitisations in particular.

Risk Retention Financing

Aside from the Basel III capital requirements, the regulatory developments that have arguably had the greatest impact on securitisation structures are the risk retention requirements and structuring transactions so as to adequately comply with the risk retention rules' limitations on financing, hedging and transferring such risk retention risks.

The actual impact of the risk retention rules differs based on asset class. In the U.S., certain asset classes are potentially exempt from the risk retention requirement so long as certain underwriting standards are satisfied. Other asset classes or non-conforming structures may be subject to risk retention but with limited impact because the relevant securitisation sponsor would in any event retain a significant exposure to the securitisation. This would be the case, for example, where the required over-collateralisation for a particular securitisation for commercial reasons is greater than, or equal to, the 5% required to be retained by the sponsor under the risk retention requirements.

The risk retention rules have spawned an entire "industry" focus on risk retention financing arrangements that has attracted an entirely new class of investors to such financing structures. This was welcome news to the securitisation industry, which had feared a lack of adequate risk retention financing and instead was presented with an enhanced investor pool. The industry has demonstrated a remarkable range of innovative risk retention financing structures. The market for risk retention financing has contracted recently, however, since the D.C. Court of Appeals ruled on February 9, 2018 that the current U.S. risk retention rules do not apply to open-market CLOs and similar structures. The court reasoned that requiring the collateral manager to purchase *additional* assets for the purpose of complying with the risk retention requirements, runs contrary to the plain words of the enabling statute, i.e. Section 941 of the Dodd-Frank Act. The court further noted that the basis for alignment of interests between investors and securitisation sponsors that lies at the heart of the risk retention rules is different for open-market

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CLOs because the managers of such CLOs are similarly situated to the CLO investors and not saddled with the same conflicts as would be the case for a sponsor that also was involved in arranging the laws. Furthermore, the European risk retention rules continue to differ from the U.S. rules in a number of ways that make risk retention structuring more complicated. For example, while U.S. risk retention rules permit a majority-owned affiliate of the CLO manger to be the risk retaining entity, the European risk retention rules focus more on the sponsor and originator to ensure that risks are either held by such originator or held by an entity in the originator chain that satisfies the requirement for risk retention.

The European and U.S. risk retention rules also impose important limitations, especially when viewed in conjunction with the relevant accounting standards. For example, risk retention generally has to be: in the form of a retention of the most junior security in a securitisation transaction with a fair value equal to at least 5% of the fair value of all securities issued by such entity; in the form of a retention of 5% of each security issued (a vertical slice); or a combination of the two. Given the 1,250% risk weight assigned to securitisation equity exposures and the ability to treat a vertical slice as a direct exposure to the underlying asset (which avoids the otherwise punitive risk weight that would apply to a straight summation of the securitisation exposures), vertical risk retention will likely be the viable alternative when securitisations are used for balance sheet optimisation purposes.

Other Important Rules and Developments

Both the House and the Senate have passed versions of a bill to revise a number of bank regulations including certain adjustments to the capital required for smaller banks in general or for certain lines of business, in terms of the larger banks. However, these rules are still subject to reconciliation and do not impact that generality of the foregoing. The changes are structured to roll back or adjust a number of the provisions that were introduced as part of the Dodd Frank Act and also otherwise adjust some of the bank capital requirements. Most of these changes will benefit institutions with less than $10 billion in assets. However, other portions of the bill will reach across the board to also capture larger financial institutions. For example, the senate bill adjusts how the supplemental leverage ratio is calculated and also expands the definition of "high quality liquid assets" to include certain municipal securities. Significantly, the bill also raises the floor for when a financial institution would be considered systemically important from $50 billion to $250 billion. However, the political pressures that are emerging as the two bills are being reconciled are likely to drive significant additional changes to these amendments.

Conclusion

As the Basel III rules continue to be phased in and the balance sheet pressures of higher risk weights and the leverage ratio become more significant, we would expect securitisations to receive increased attention to satisfy the growing need for balance sheet optimisation. Securitisations provide capital efficiencies by allowing banks to originate various underlying exposures, transfer the bulk of its exposures to non- (or less-) regulated parties wishing to take the credit risk on the underlying exposures and thereby allow banks to continue to service the demand for originating new financing. The consultation issued by the Basel Committee and the International Organisation of Securities Commissioners ("IOSCO") to identify criteria for "simple, transparent and comparable securitisations"[v] highlights the need for building sustainable securitisation markets by increasing investor demand. With the added risk-weighted benefits afforded to STC-compliant structures under Basel III, it is likely that the supply for such high quality securitisations will increase which, in turn, would likely contribute significantly toward investor comfort with, and demand for, the asset class, thereby creating a strong force for rebuilding a robust securitisation market. Similarly, as the G-20 and the World Bank and other multinational entities are focusing on finding solutions to the infrastructure financing needs that cannot efficiently be serviced by bank lenders and seek to establish a more time- and cost-efficient infrastructure financing market, it is likely that securitisations will continue to strengthen their positions as a major part of that solution. In light of the significant infrastructure financing needs across both developed and emerging markets, there is real potential for quickly achieving an infrastructure securitisation market that is able to attract investors that traditionally allocate far less to individual infrastructure bonds and that can achieve the types of secondary liquidity that we see in the CLO market, both of which would drive a robust securitisation solution.

Endnotes

i. See also "Securitisation in Light of the New Regulatory Landscape", *International Comparative Legal Guide to Securitisation 2017*.

ii. See, e.g. "High-level summary of Basel III reforms" issued December 2017.

iii. European Union Capital Requirements Regulations at 243(2).

iv. *Id*. at Article 243(4).

v. Joint Report by the Basel Committee on Banking Supervision and the Board of the International Organization of Securities Commissions: "*Criteria for identifying simple, transparent and comparable securitisations*" (July 2015) available at https://www.iosco.org/library/pubdocs/pdf/IOSCOPD494.pdf. See also Joint Report by the Basel Committee on Banking Supervision and the Board of the International Organization of Securities Commissions: "*Criteria for identifying simple, transparent and comparable short term securitisations*" (July 2017) available at https://www.bis.org/bcbs/publ/d414.pdf.

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Reviving Securitisation in Europe: From Regulation to Implementation

Association for Financial Markets in Europe

Anna Bak

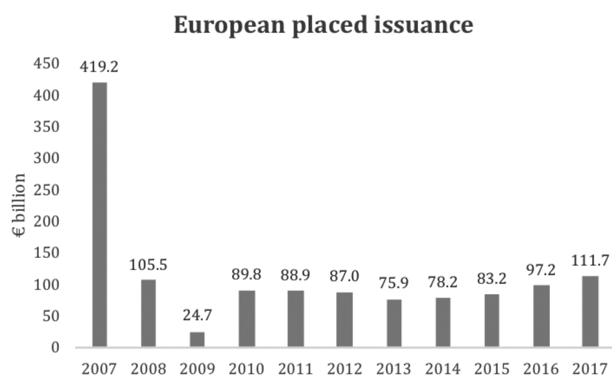
The Year in Review

Since we last contributed to this publication, AFME's key focus has continued to be on the STS Regulation, establishing the "Simple Transparent and Standardised" ("STS") securitisation framework as well as common rules for all securitisations, and the related Capital Requirements Regulation ("CRR") Amendment, which together form the new STS "Securitisation Package". However, since publication in the Official Journal of the European Union (the "OJ") in December 2017, attention has now turned to the implementation and development of the secondary legislation, including the variety of technical standards and guidelines.

Before reviewing where we currently stand in more detail, let us first recap briefly on the state of the market and the final outcomes under the new Securitisation Package.

European securitisation market

1.1 European placed issuance (EUR billion)



Source: *AFME/SIFMA Members, AFME, Bloomberg, Dealogic, Thomson Reuters, SIFMA*

The volumes of new issuance in Europe continue to disappoint. In 2017, EUR 235 billion of securitised product was issued in Europe, which is a decrease of 2% from the EUR 239.6 billion issued in 2016. Of this, only EUR 111.7 billion was placed on the market, representing less than half (48%) of the total European issuance. The number of investors active in the securitisation market needs to grow, otherwise there is a risk that the market will no longer be able to support the staff, infrastructure and other fixed costs necessary for it to thrive. Therefore, if the securitisation market is ever to recover, the implementation of the Securitisation Package, and the recognition of the STS framework within that, has to happen fast.

There are more positives than negatives in the final STS rules

On 28 December 2017, the final texts of both the STS Regulation and CRR Amendment were published in the OJ. Both texts entered into force on 17 January 2018 (20 days later). The date of application of both the STS Regulation and CRR Amendment is 1 January 2019, giving market participants around a year to adjust to the new rules. These have now been finalised and, helpfully, most of the more controversial proposals made earlier in the legislative process have not been adopted.

Specifically, restrictions on permitted market participants, public disclosure of information listing the names of investors ("investor name give up") and an increase in the risk retention rate, do not appear in the final legislation. The problems relating to self-certified residential loan securitisations and acquired portfolios have been partially addressed as well, broadly leaving market participants with a workable outcome.

Nevertheless, certain issues remain unaddressed. Perhaps the biggest stumbling blocks are the lack of provisions for third-country-originated transactions, for an adjusted standard for existing and legacy transactions, and sub-optimal "grandfathering" provisions for legacy transactions.

Those, and several other key issues, were discussed in more detail in this publication last year, and therefore this chapter does not propose to repeat that discussion. We will focus instead on the implementing measures which are now underway.

From Regulation to Implementation

As noted above, the publication of the two regulations does not end the legislative process of the securitisation reform. What comes now is the "Level 2" stage, which includes development of the secondary legislation that will allow the new framework to be implemented.

A brief summary of the European Level 2 legislative process

Once the European Commission, the European Council and the European Parliament have agreed on the final legislative text of the regulation, the text known as "Level 1" text is published in the OJ and it then enters into force. Level 1 text sets out rules and general principles; however, it does not include detailed provisions which are necessary for the laws to be fully operative and implemented. For this to happen, implementing measures, drafted and adopted by the Commission, following advice from the European Supervisory

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Authorities (the "ESAs"),[1] are required. Those implementing acts (the "Level 2" acts) may themselves take the form of a Directive or a Regulation (when drafted by the EC) or the form of Binding Technical Standards[2] or Guidelines (when drafted by the ESAs). The Level 2 measures are often referred to as "secondary legislation"; however, there is nothing "secondary" to their importance – quite the contrary.

For instance, the STS Regulation requires that "the [STS] securitisation shall be backed by a pool of underlying exposures that are homogeneous in terms of asset type …" (Art. 20, the homogeneity criterion). Yet, it does not specify what "homogeneity" exactly means. What the regulation does, however, is provide a mandate for the EBA to draft the regulatory technical standards (the "RTS"), which will specify the conditions under which securitisation transactions will be considered homogeneous.

The Level 1 text also sets up a new transparency regime for originators, sponsors and SSPEs, requiring certain information about all securitisation transactions (not just STS securitisations) to be made available to investors, potential investors and to national competent authorities (Art. 7). The required information will be disclosed via new (and to be established) securitisation "depositories". However, it is ESMA who will develop the technical standards to specify the information that the originator, sponsor and SSPE must provide in order to comply with this obligation. Similarly, the details of the format of the information (templates) and the rules governing the reporting of data will be decided via the Level 2 legislation.

The CRR Amendment broadens access to the Securitisation Internal Ratings-Based Approach ("SEC-IRBA"), a methodology of calculating capital charges based on internal modelling. The calculations and access conditions of the SEC-IRBA are highly complex and technical; for example, the CRR Amendment includes provisions mandating the EBA to issue regulatory technical standards on how institutions can use this method, including the conditions for use of the "proxy" (or "external") data.

These are just few examples indicating the importance of the Level 2 legislation, without which the STS framework will not work in practice. Therefore, over the course of 2018 and 2019, market participants should expect to see many items of secondary legislation and guidance, dealing with a wide variety of matters including risk retention, the meaning of homogeneity, transparency requirements and data templates, the STS notification template, the use of the "top-down" approach for IRBA capital calculations, and the authorisation of third-party verifiers for STS securitisation.

Furthermore, the date of publication of the Level 1 texts sets out the deadlines for the EBA and ESMA to draft the Level 2 texts. These deadlines are now defined with precise dates, which are based on the entry into force of the STS Regulation and CRR Amendment. Consequently, the ESAs are due to submit all RTS by either 18 July 2018 (six months after entry into force) or 18 January 2019 (12 months after entry into force). The technical standards will then be approved by the European Commission, and will undergo scrutiny by the European Parliament and European Council, before finalisation. The next few months or so will therefore be crucial for determining the important details of the framework. Discussions will be technical as the ESAs are bound by the principles agreed in the Level 1 texts.

The key technical standards and guidelines

The EBA and ESMA received together over 30 different mandates to develop various technical standards, guidelines or reports. Below we will focus on just a few, which are considered key parts of the Securitisation Package.

In December 2017, the EBA and ESMA published five consultations including the following.

EBA draft RTS on risk retention for all securitisation transactions

These draft regulatory technical standards set the requirements for originators, sponsors and original lenders related to risk retention, in particular with regard to: (a) the modalities for retaining risk, including fulfilment through a synthetic or contingent form of retention; (b) the measurement of the level of retention; (c) the prohibition of hedging or selling the retained interest; (d) the conditions for retention on a consolidated basis; and (e) the conditions for exempting transactions based on a clear, transparent and accessible index.[3]

The RTS, when finalised, will replace the current Commission Delegated Regulation on risk retention. Helpfully, the EBA has proposed a general approach for ensuring that the current risk retention technical standards are carried over to the new standards. Continuity is appropriate given the significant overlap in the key aspects of the requirements between the two regimes; a different approach involving a broader reworking of the technical standards would risk creating significant compliance confusion. However, certain issues such as jurisdictional scope, consolidated application and grandfathering have not been properly addressed in the draft RTS.

EBA draft RTS on the homogeneity of underlying exposures in STS securitisation

As mentioned above, the homogeneity criterion requires further specification; thus the draft RTS outline these. The EBA's proposals are based on a set of four criteria: underwriting; servicing; asset categories; and risk factors. In general, the principles underlying the draft RTS seem manageable. That said, it is extremely important that the final RTS make clear that the criteria (and in particular the risk factors) can be applied and analysed flexibly and in a manner appropriate to the particular transaction. The final RTS will be applicable to both STS asset-backed commercial paper ("ABCP") and to STS term securitisations.

Separately, the EBA is also now consulting on draft guidelines and recommendations on interpretation of all STS criteria (not just homogeneity), as well as guidelines on adapted interpretation for STS ABCP securitisations.[4]

ESMA draft RTS and ITS on disclosure requirements, operational standards, and access conditions for all securitisations

The RTS will cover the securitisation disclosure requirements, operational standards for handling disclosures, and the terms and conditions of access for users of securitisation disclosures. Therefore, the RTS will deal with details of what data must be provided, and the reporting templates.

In the draft RTS, ESMA took a general approach of starting from existing templates (the ECB and Article 8b templates) in developing the templates to be appended to the draft RTS. Leveraging-off of the work already done is of course very helpful, as a great deal of effort on the part of regulators, the ECB and market participants went into the development of those templates some years ago and into adjusting to the disclosure obligations embodied therein.

Similarly, the industry welcomes ESMA's approach with respect to private transactions,[5] which essentially exempts private transactions from the scope of the reporting templates. This is a sensible approach that takes due account of commercial realities and remains consistent with both the letter and the spirit of the treatment of private securitisations set out in the Securitisation Regulation.[6] However, the status of ABCP securitisations remains uncertain, as the draft RTS say that both ABCP transactions and ABCP programmes (both

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of which are usually private securitisations) are outside the scope of the draft RTS, yet also specifically contemplate them.

However, one of the key points of concern in respect of technical standards on disclosures is the timing. Beyond simply providing certainty as to the future requirements as early as possible, it is essential to avoid the interim application of the RTS made under Article 8b of the Credit Rating Agencies Regulation pursuant to Article 43(8) of the Securitisation Regulation. Therefore, very helpfully, ESMA has published a letter in which it states that it has reorganised its resources and priorities and will aim to deliver its final report on the RTS and ITS on disclosures to the Commission in mid-July 2018, i.e. six months in advance of the deadline under the Securitisation Regulation. This should allow the EC to prepare for speedy adoption of these technical standards and thus address concerns about the risk of duplicative implementation of the disclosure obligation.

Two other pieces of Level 2 legislation are associated with the transparency regimes under the Securitisation Regulation: the first covering technical advice on fees for securitisation repositories; and the second on RTS and ITS on application for registration as a securitisation repository.

ESMA draft RTS and ITS on content and format of the STS notification

These draft technical standards specify the information that the originator, sponsor and SSPE are required to provide in order to comply with their STS notification requirements.

ESMA's proposals to provide a certain amount of general information in the STS notification to facilitate the identification of the notification seem broadly reasonable, with two exceptions. First, disclosing information relating to the originators of ABCP transactions in the STS notification is not appropriate and is inconsistent with the disclosure regime as it applies to ABCP securitisations. Second, with respect to the anonymised notifications for private securitisations, the only information made publicly available should be the unique reference number assigned by ESMA to the STS notification document. That document could then be made available to investors and potential investors who would derive comfort from the fact that the corresponding number appeared on ESMA's public website.

ESMA draft RTS on third-party firms providing STS verification services

The originator, sponsor or SSPE may use the service of an authorised third party to check whether a securitisation complies with STS criteria. The STS framework allows for third parties to verify STS compliance, but leaves it to ESMA to specify the conditions under which a firm may become an authorised STS verifier. Therefore, among the five consultations published in December 2017 were also draft RTS which specify the information to be provided to the competent authorities by companies applying for such authorisation.

EBA work on capital

One of the EBA's key priorities in 2018 are the technical standards and guidelines mandated under the CRR Amendment, which will be essential in determining the details of the new capital regime for securitisations, both STS and non-STS. The EBA is expected[7] to consult on the RTS for conditions for the use of K_{IRB} (a capital requirement calculation), which will be necessary for banks in applying the SEC-IRBA methodology. Connected with these RTS is the EBA's set of guidelines, including the guidelines (and a report) on practices on hierarchy of approaches,[8] on the computation of K_{IRB} for dilution risk,[9] on the determination of tranche maturity and weighted average life ("WAL")[10] and on estimates of probability of default and loss given default using incremental risk capital.[11]

Next to the technical standards and guidelines described above, there are number of other mandates, which are perhaps less urgent but nevertheless important. These include the EBA Guidelines on implicit support,[12] the EBA Report on the STS eligibility of synthetic securitisation[13] (which is due in July 2019) and two reports on Significant Risk Transfer ("SRT").[14]

LCR and Solvency II Remain Problematic

The Securitisation Package requires certain adjustments to the existing laws, including the rules for liquidity coverage ratio ("LCR") and Solvency II (governing capital treatment of insurance investors).

In January 2018, the Commission consulted on proposals for revisions to the LCR which, disappointingly, fall short of improving the treatment of STS securitisation. The proposals align the LCR eligibility criteria with the STS requirements; however, they do not promote STS securitisation to Level 2A. STS securitisations remain as Level 2B assets.

AFME argues that there is little point to the new framework if the prudential strength of STS securitisations will not be given improved treatment under the LCR. We say that senior tranches of all STS securitisations, whether term or ABCP, should be classified as Level 2A assets with maximum allocations and minimum haircuts equivalent to the current treatment of covered bonds of Credit Quality Step ("CQS") 2. The European Commission is expected to publish the final text of the LCR revision at the end of Q2 or in Q3 2018.

Similar concerns apply with regard to the Commission proposals for Solvency II review which ought to incorporate changes necessary to accommodate the new STS regime. Unfortunately, while the proposals provide a more balanced approach to the capital calibrations for STS senior positions, the risk factors for mezzanine and junior tranches remain very high. Further, no relief at all is provided for non-STS securitisations.

This is problematic because securitisation needs to be able to deliver risk transfer to build the capital markets union ("CMU") and reduce reliance on banks. Insurance company investors have, therefore, a particularly important role to play at the mezzanine and junior level. These levels of investment match their risk-return investment needs and are the levels where they can perform the function of facilitating risk management and diversification in the financial system. The capital relief (or transfer of risk) banks could achieve from selling mezzanine bonds to insurers would help to significantly free up bank capital that would flow back into the real economy. The absolute levels of the current proposed calibrations for mezzanine and subordinated tranches, and their cliff effects, do not incentivise investment – so those benefits are unlikely to be achieved. Therefore, it is crucial that revised calibrations under Solvency II encourage insurers to buy mezzanine and junior tranches.

We Must Not Miss the Opportunity

The STS label has always been a means to an end: restarting and building "a sustainable EU market for securitisation";[15] distinguishing the strong performance of securitisation in Europe post-crisis from the poor performance of US sub-prime mortgages; and ensuring lessons of the past have been learned.

This has now largely been achieved and 10 years on from the global financial crisis we can see how well most European securitisation

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has performed: both STS and non-STS. However, for the markets in Europe to recover, we need STS to be recognised properly in key secondary legislation, as well as appropriate treatment of non-STS securitisation.

Therefore, the success of the framework now largely depends on the detailed provisions to be determined in the technical standards and guidelines – which need to be adopted soon. The LCR and Solvency II frameworks should encourage banks to participate in the senior tranches and insurers to bring back their investments in non-senior securitisation positions.

If this important work is not completed, then this crucial opportunity for securitisation to contribute to Capital Markets Union will be missed, over-reliance on bank funding will continue and the European financial system will be less strong.

Endnotes

1. ESAs include the European Banking Authority ("EBA"), the European Securities Markets Authority ("ESMA") and the European Insurance and Occupational Pensions Authority ("EIOPA").
2. The Binding Technical Standards include the Regulatory Technical Standards ("RTS") and Implementing Technical Standards ("ITS").
3. As per Art. 6 (6) of the STS Securitization Regulation.
4. At the time of writing, the draft guidelines on interpretation of the STS criteria have been published and open for consultation until 20 July 2018.
5. "The reporting templates do not apply securitisations where no prospectus has to be drawn up in compliance with Directive 2003/71/EC (often referred to as 'private securitisations')"; recital 3 of the draft RTS.
6. Art. 7(2).
7. At the time of the writing, the draft RTS are expected to be published in the second half of 2018.
8. (CRR Art. 254(8).)
9. (CRR Art. 255(8).)
10. (CRR Art. 257(4).)
11. (CRR Art. 377(3).)
12. (CRR Art. 250(4).)
13. (STS Art. 45(1).)
14. (CRR Art. 244(6)/CRR Art. 245(6).)
15. http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:52015PC0472 (explanatory memorandum).

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Credit Fund Warehouse Origination Facilities

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Introduction

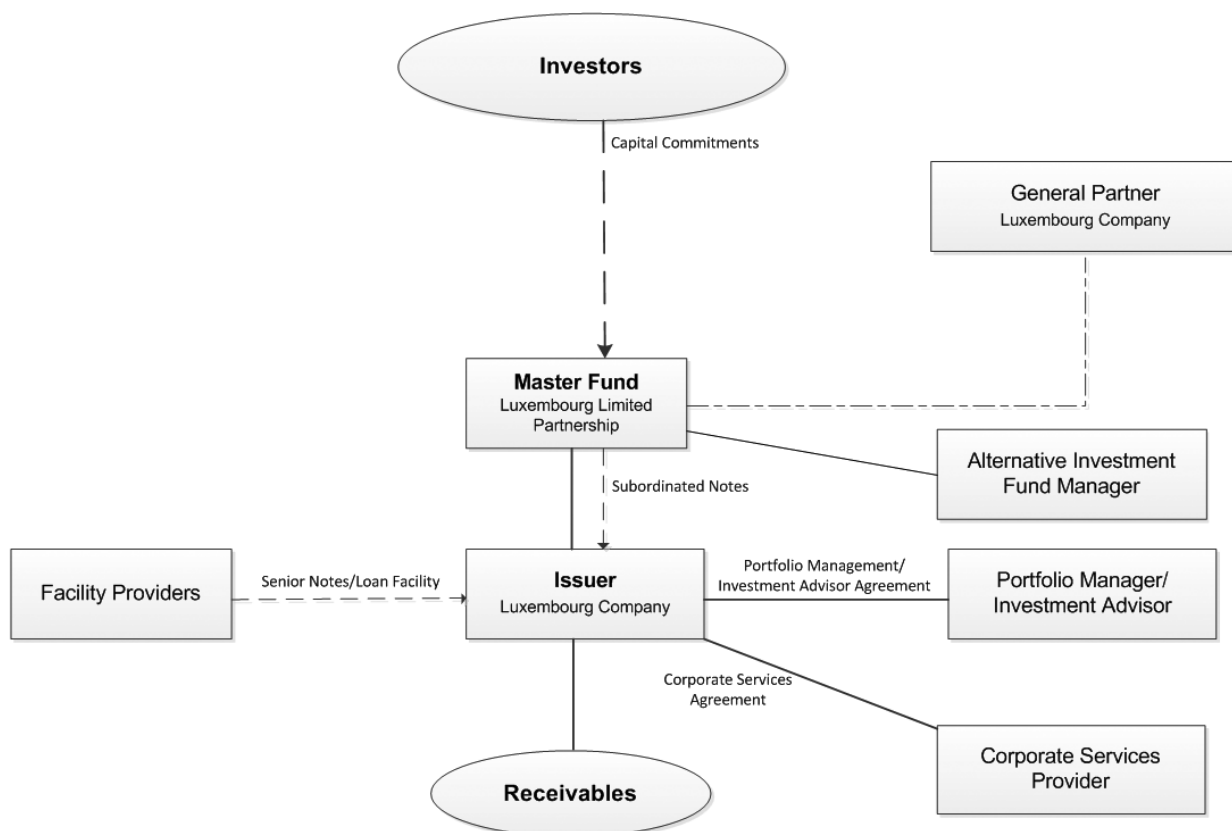
In recent years, there has been a dramatic increase in investor appetite for credit funds. The increase in interest is largely attributed to the general macroeconomic issues of poor returns offered by banks on deposits, as well as other traditional forms of financing and investors seeking higher yields on fixed income instruments. Credit funds in Europe have been traditionally limited to money market funds which invested in commercial paper and other high-grade instruments, but the recent surge of interest in credit funds has resulted in fund managers investing across a diverse range of asset classes including leveraged loans, SME loans, consumer credit and commercial real estate loans. There is also a developing trend of credit funds using permanent leverage to enhance returns, and it is now commonplace for lenders to provide credit funds with asset-backed warehouse origination facilities which they will use to originate or acquire portfolios of leveraged loans, consumer loans and mortgage loans.

The composition of the borrowing base (the receivables against which the lenders will advance funds) is integral to the operation of warehouse origination facilities. There are well-established eligibility criteria, largely taken, or adapted, from CLO or RMBS warehouse transactions, which are heavily negotiated to ensure that they are aligned with the fund's investment strategy and the evolution of the market in which the fund invests.

This chapter discusses the basic structure of credit fund warehouse origination facilities and considers some of the main negotiating points.

Structure

The structure of a typical credit fund is as follows:



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The entities involved in the structure are:

- an asset-holding company which advances the loans to be made by the fund. This is ordinarily a newly established special purpose vehicle. This vehicle (the "**Issuer**") issues notes to the senior finance provider and to its parent (discussed below) and usually qualifies as a Luxembourg securitisation vehicle. The Issuer might instead enter into a loan facility rather than a note issuance for its senior funding, but if it is a Luxembourg securitisation vehicle it will need to issue notes to its parent (see below);
- the parent of the asset-holding company, which is usually (but not always) a limited partnership based in a jurisdiction that is favourable to its investors – this will normally be Luxembourg for a European-focused fund. This entity is the main investment vehicle for all entities comprising the credit fund (the "**Master Fund**"). Investors can be limited partners in this entity or can access the fund via feeder funds and/or parallel partnerships;
- the general partner of the Master Fund which is, usually, also the general partner of any other partnerships forming the fund and, in a European-focused fund (as above), a Luxembourg limited liability company;
- an alternative investment fund manager which will provide regulated services to the Master Fund and which will usually delegate to a portfolio manager or investment advisor (as described below); and
- the manager of the fund (the "**Portfolio Manager**"), ordinarily based in another jurisdiction, charged with providing the Issuer and the other entities comprising the fund with investment advisory and/or portfolio management services such as acquisition, monitoring, disposal and replacement of investments (or recommending the same) under a portfolio management/investment advisory agreement.

As noted above, the Issuer is an SPV and so will require various services in order to perform its role under the transaction. A warehouse origination transaction will normally involve roles common to most securitisation structures, such as a corporate services provider, cash manager and servicer providing the requisite corporate, administration, collection and cash management services for the Issuer. However, unlike ABS transactions, it might be the case that certain functions are provided by the fund's administrator (such as corporate services and cash management) rather than entities typically providing those services in the public securitisation markets. In addition, servicing is potentially split between that fund administrator and, to a lesser extent, the Portfolio Manager.

Financing

Traditionally, fund-level leverage has involved a loan from institutions regularly engaged in fund finance. Whilst that would be a secured loan and would ordinarily be fairly restrictive in relation to the fund's operations, it will not, for example, be structured to the standard of a rated ABS deal. In contrast, credit fund warehouse origination facilities generally adopt a structure that is based on ABS technology and frequently have regard to rating agency methodology.

In a warehouse origination facility, the Issuer will either issue senior notes to one or more banks under a note purchase agreement (the "**Noteholders**") or borrow loans from one or more banks under a senior loan facility (the "**Lender**" and, together with the Noteholders, the "**Facility Providers**"). The note purchase, or senior facility, agreement is likely to be based on similar terms and adopt a similar structure to warehouse facilities used preparatory to asset-backed securitisations. Increasingly, credit fund managers in the direct lending market are pushing for these agreements to follow Loan Market Association provisions in order to ensure consistency across their funds but also to reflect the terms of the loans the fund will itself be making.

The Issuer will also issue subordinated loan notes to the Master Fund under a loan note issuance programme established by the Issuer. The subordinated funding is usually governed by Luxembourg law and based on similar terms to many other Luxembourg securitisation vehicle note issuances representing, in essence, shareholder funding. If a Luxembourg securitisation vehicle isn't being used, the subordinated funding can be a more straightforward intra-group loan but will normally be governed by the law of the jurisdiction of establishment of the Issuer or Master Fund (rather than, for example, English law).

Perhaps the biggest distinction between a credit fund warehouse origination facility and a typical warehouse facility is the origination aspect and the tenor of the facility. A typical warehouse would ordinarily be established to finance loans that have already been made and are being sold to the Issuer by an originating entity preparatory to a term and/or public securitisation refinancing. For a warehouse origination facility, the emphasis is predominately on the Issuer originating assets itself (subject to the discussion below on risk retention) rather than acquiring funded loans. Accordingly, the speed at which a fund can draw on its facility is likely to be of prime concern to the Portfolio Manager so that they can ensure speed of execution in the deployment of the fund's capital. That being said, it is also common for credit funds to combine a warehouse origination facility with an equity bridge (or subscription line) facility. Where these two facilities are used in tandem, the Issuer will effectively draw on the warehouse origination facility in order to refinance debt borrowed under that bridge facility. In addition, the warehouse origination facility is frequently a medium-term financing solution for the fund (or indeed a permanent solution for shorter tenor assets) with no prospect of an ABS take out.

Security

As one would expect, the Facility Providers are granted security over all of the assets of the Issuer (principally being the leveraged, SME consumer or commercial real estate loans originated, or acquired, by the Issuer together with any cash in the bank account(s) of the Issuer). In addition, reflecting the structure of the transaction as a fund, the Facility Providers receive security over the subordinated funding from the Master Fund. The intention behind this is that the Facility Providers have indirect access to the uncalled capital commitments of the investors in the Master Fund by calling on that subordinated funding and having the Master Fund, in turn, call on its investors. Over time, as the uncalled capital commitments of the investors are reduced, the underlying assets of the Issuer will form the main recourse for the Facility Providers.

Borrowing Base

The borrowing base, i.e. the portfolio of receivables in respect of which the Facility Providers are prepared to advance amounts under the warehouse origination facility is, as one would expect, fundamental to any form of financing whose recourse is ultimately to the assets originated by the fund. The make-up of the borrowing base forms the substance of the Facility Providers' credit decision. The characteristics of the borrowing base are even more important to the functioning of a revolving warehouse origination facility because a new decision to lend needs to be taken at the end of each interest period.

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The Issuer's (and Portfolio Manager's) primary concern is, of course, to ensure that the receivables that form the borrowing base are as extensive as possible in order to be able to borrow the maximum amount of money allowed under the facility documents. In addition, it is vitally important to a fund's competitive advantage in its target market that it can offer as broad a range of lending products as possible. The Facility Providers, in comparison, are motivated to restrict the type of receivables which can form the borrowing base to those of the highest credit quality and, ideally, to ensure homogeneity given that their recourse is ultimately to those receivables. The eligibility criteria and concentration limits (discussed below), which determine the composition of the borrowing base, are therefore the main source of negotiation in putting together this form of facility. The eligibility criteria which generally receive the most attention in the negotiation are:

- The types of receivable which could be originated or acquired by the Issuer. This goes to the heart of the lending strategy of the fund and encompasses the type of instrument (e.g. loan, lease etc.) to which the Issuer is permitted to be party, the leverage multiple that the Issuer can offer to its borrowers and the type of financing structure that the Issuer can be party to with its borrowers and the borrowers' other creditors.

  Given the continuing evolution of funds' investment strategies and their search for a competitive edge, this criterion is usually significantly negotiated. In the leveraged loan context, significant time might be spent agreeing what each party intends by the terms **senior secured**, **subordinated** and **second lien**. The structural changes to the unitranche product, which are the mainstay of the direct lending fund's arsenal, directly impact this criterion because those changes have, in the main, been focused on the ranking of the loan and the capital structure of the underlying borrowers. In the residential mortgage context, time might equally be taken up by, among other things, restricting the type of borrowers to which mortgages can be advanced and how their credit is assessed and the ranking of the mortgage loans/whether any other debt can be secured on the mortgage property.
- In relation to direct lending funds and commercial real estate funds, transferability (i.e. that the receivable may be owned by and freely transferred by the Issuer). This criterion needs to be considered carefully in light of financial sponsors' focus on the identity of the potential transferees of the loans made by the Issuer (to portfolio companies of those sponsors). The Facility Providers require certainty that the receivables in the borrowing base can be freely transferred should there be a need to enforce the Facility Providers' security over those receivables and realise value by selling the receivables in the secondary loan market. In contrast, a sponsor will usually seek to restrict potential transferees by reference to "white" or "black" lists of permitted or restricted transferees. There is usually a resulting compromise of providing for a certain minimum number of transferees on a "white list" or allowing for a "black list".
- Restriction on further advances, revolving loans or multi-draw term loans being included in the borrowing base. The Facility Providers are likely to be concerned that the Issuer would be unable to generate an ongoing commitment to advance amounts to borrowers. The concern stems from the Issuer being an SPV which does not have the ability to provide further advances or to operate a revolving or multi-draw facility in the same manner as a bank would, both from the perspective of having the available funds to satisfy the lending obligation and the staff to manage requests for further drawings. Whilst the exclusion of further advances and revolving loans is a common one in these types of facilities, there is sometimes an argument, in the context of direct lending fund facilities, that a multi-draw facility should be permitted on the basis that there are likely to be a limited number of future drawdowns and the lending vehicle would simply need to demonstrate that it has sufficient resources to support the entire commitment under that multi-draw facility.
- Categorisation of a receivable as "defaulted" and the extent to which it is eligible. Receivables with respect to which non-payment and certain other events of default have occurred will not form part of the borrowing base. The circumstances in which non-payment results in ineligibility and the categories of events of default that render a receivable "defaulted" are therefore a key area for negotiation. In the context of consumer credit, there will be significant discussion of the level of payment arrears and when they should trigger ineligibility. This will be tied to the specific asset class and whether, for example, it is first charge or second charge, prime or non-confirming.

  For a direct-lending fund and a commercial real estate fund, the events of default are usually defined by reference to the LMA form of leveraged facilities agreement. Specifically, the events of default include: (i) non-payment; (ii) unlawfulness and invalidity; (iii) insolvency; and (iv) repudiation together with cross acceleration in relation to senior or *pari passu* indebtedness. It is customary to reference these events to their occurrence under the underlying loan instrument but lenders can insist on including the events of default in the warehouse origination facility such that if an event of that type occurs, regardless of its existence in the underlying loan instrument, it would render the receivable defaulted and ineligible.
- Additional criteria, which will be negotiated on a case-by-case basis to reflect the fund's/Manager's investment strategy, including:
  - for direct lending funds: the required enterprise value of the borrowers, the minimum EBITDA of the borrowers and the minimum equity in the underlying transactions; and
  - for consumer credit funds: the types of borrower, the types of underlying collateral and the creditworthiness of the borrowers.

Excess Concentrations

Tied to the borrowing base composition is the question of diversification of the receivables. Whilst the eligibility criteria will govern the type of receivable that can form part of the borrowing base, lenders are also concerned about the potential for concentration of assets to develop. This concentration could lead, through the aggregation in the borrowing base, to an amplification of the effects of any risks to the underlying obligors. Consequently, certain concentration limits are included in these types of transaction to prevent the borrowing base being too exposed to certain types of receivable. Examples of concentration limits which receive a significant amount of negotiation include:

- In the case of direct lending funds: receivables in any single type of industry. The negotiation in this area stems from the investment strategy of the fund/Manager. It is customary for concentration limits by industry to be referenced to the Moody's Industry Classification (which forms one of the bases of Moody's credit rating of public CLO transactions). Therefore, it is necessary to agree revised limits for any specific sectors which a fund invests in disproportionately to other sectors, based ultimately (as above) on the investment strategy of the fund and its manager.
- Receivables, collateral security or obligors, governed by the law or located in a particular country or group of countries. As with the first bullet point above, if a fund/Manager has a focus on a specific country or set of countries there will need to be a greater concentration limit for those countries. Separately, in the context of consumer credit, Facility

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Providers might be concerned to ensure that the relevant collateral security is not overly concentrated in particular regions. Similarly, that obligors are predominately located in the same country as the governing law of the receivable or that they are not resident in certain jurisdictions.

- For direct lending funds, receivables where the underlying borrower did not have an EBITDA that exceeded a certain agreed level. As with the equivalent eligibility criterion (mentioned above) this concentration limit goes to the heart of the fund's/manager's investment strategy (i.e. the sector of the market in which the Issuer will lend) and so this is a straight commercial negotiation as to what the Facility Providers would accept as the greater part of the borrowing base.
- To some extent tied to the last point but more related to consumer credit funds: creditworthiness of the obligors. Particularly in the context of non-prime consumer credit, there will be a degree of focus on the credit scores (in a general sense) of the obligors both defining what low creditworthiness comprises and also placing limits on certain sub-sections of those lower creditworthy obligors.

Advance Rate

Whilst the combination of the borrowing base and the concentration limits determine what assets the Facility Providers will lend against, the amount that the Facility Providers will advance against those assets is determined by the advance rate. As one would expect, it is customary for different advance rates for different types of receivables to be included. Receivables that are perceived as having a lower credit risk from a legal perspective, such as receivables of a higher ranking, have a higher advance rate than receivables that are perceived as having a higher credit risk such as subordinated receivables. The level of each advance rate is solely a commercial negotiation point albeit that there can be some discussion as to a sub-set of receivables having a greater or lower advance rate to reflect leverage levels or ranking of those receivables.

Risk Retention

The commitment under any structure similar to that described above is likely to be classified as a securitisation for regulatory purposes, being (at present) the requirements of the Capital Requirements Regulation ("**CRR**"), the Alternative Investment Fund Managers Directive ("**AIFMD**") and Solvency II. As a result, the Portfolio Manager will need to ensure that a qualifying retaining entity will hold the requisite minimum 5 per cent "material net economic interest" in the securitisation. Whilst the new Securitisation Regulation will impose the compliance burden on both the Facility Providers and the originator (among others), other than AIFMD (to a limited extent) the existing regulatory framework imposes direct obligations for compliance on the Facility Providers with the associated regulatory capital charge penalty for failure to demonstrate compliance.

It is therefore necessary to agree, in a risk retention letter, that a relevant entity (or entities) will retain the risk/exposure described above. More frequently than not, the retained interest for an ABS transaction is held by a corporate entity. In a fund structure, the consideration needs to be given to the appropriate entity to hold the retained interest. In this context, thought will need to be given to the correct entity which will provide the relevant undertakings and representations on behalf of a fund, such as the fund's general partner or its manager (although the latter is likely to be commercially unacceptable for most managers). In addition, the ownership structure of a partnership will need to be borne in mind and consideration of whether multiple entities should hold the retained interest, particularly in light of the CRR's definitions of, and requirements for, the "originator", "sponsor" and "original lender". Similarly, restrictions might need to be placed around the ability of a partnership to replace its general partner.

Current Issues

The use of leverage by managers of credit funds, particularly those operating in the middle-market, is on the rise. This increase is driven both by the need to diversify fund terms and activity levels in this market but also by the extent to which the underlying assets, leverage loans, consumer loans and mortgage loans, are readily capable of gearing by forming a borrowing base for warehouse origination facilities, in loan or note format.

Whilst warehouse and/or warehouse origination facilities preparatory to CLO and RMBS have been the greater share of the market to date, increasingly managers of real estate, consumer finance and potentially private equity are looking to lever their fund strategies. There is therefore scope for significant growth in the number and range of fund managers using this form of financing.

Conclusion

The architecture of the warehouse origination facility described above has a significant amount in common with traditional ABS warehouse facilities and more straightforward lending on borrowing base terms. However, care needs to be taken in relation to the interaction between the fund structure and the typical requirements of a securitisation. As can be seen from the above, this is particularly the case in the context of the risk retention requirements imposed both on the financial institutions providing leverage and the manager as well as, in the future, any other entity involved in establishing the facility.

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Australia

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1 Receivables Contracts

1.1 Formalities. In order to create an enforceable debt obligation of the obligor to the seller: (a) is it necessary that the sales of goods or services are evidenced by a formal receivables contract; (b) are invoices alone sufficient; and (c) can a binding contract arise as a result of the behaviour of the parties?

(a) There is no general requirement that an agreement for a sale of goods or a provision of services be evidenced by a formal written contract between the parties. However, certain contracts do require the formality of writing, such as contracts for the sale of land (or interests in land) and credit contracts regulated under the *National Consumer Credit Protection Act 2009* (Cth) ("**NCCPA**") (which also mandates detailed form and content requirements). In some cases, electronic transactions legislation may allow a contract that is required to be "in writing" to be entered into other than using a physical paper agreement. The *Personal Property Securities Act 2009* (Cth) ("**PPSA**") requires a security agreement to be evidenced in writing and either signed by the seller or adopted by the seller by conduct.

(b) Where no special rules such as those noted in (a) apply, an invoice may be sufficient evidence of contractual relations provided that the basic requirements of contract formation are met (namely offer, acceptance, consideration, certainty, completeness, capacity and intention to create legal relations).

(c) Where no special rules such as those noted in (a) apply and the basic requirements of contract formation highlighted in (b) are met (including an intention to create legal relations), the conduct of the parties may be sufficient for a contract to be deemed to exist.

1.2 Consumer Protections. Do your jurisdiction's laws: (a) limit rates of interest on consumer credit, loans or other kinds of receivables; (b) provide a statutory right to interest on late payments; (c) permit consumers to cancel receivables for a specified period of time; or (d) provide other noteworthy rights to consumers with respect to receivables owing by them?

The NCCPA regulates loans and leases (and, e.g., associated guarantees and mortgages) entered into with consumers, and regulates matters such as the contract form, disclosures and conduct. Where the receivables are margin loans, these will be regulated by relevant provisions of the *Corporations Act 2001* (Cth) ("**CA**") rather than the NCCPA and will be subject to their own disclosure, licensing and responsible lending regime.

(a) Under the NCCPA:

- restrictive charging provisions apply to small amount credit contracts; and
- a general cap of 48% applies to credit contracts, calculated as provided in the NCCPA.

(b) There is no express statutory right to demand payment of default interest under statute in Australia. However, this is a commonly accepted contractual term and, subject to meeting certain requirements, is not prohibited.

Default interest is permitted under the NCCPA if it is only imposed on an event of default, only in respect of the amount in default and only while that default continues.

The right to default interest should also be clearly set out in the contract and the amount should not be so high as to constitute a penalty or be considered unconscionable or unfair.

(c) Unless the contract prohibits its early repayment, a credit provider must accept early payments under NCCPA regulated contracts. The NCCPA also restricts early termination charges and obliges credit providers and lessors to consider applications for contract variation due to hardship (e.g., illness or unemployment).

(d) Consumer protection legislation (including the NCCPA) provides consumers with extensive rights and protections. Other key protections include:

- obligations relating to responsible lending, disclosure and contractual form; and
- consumer rights of contractual review, to have unfair terms declared void, to access external dispute resolution schemes (which may have regard to "fairness" generally rather than strict legal obligations, and cannot be appealed) or to have a court reopen an unjust transaction.

1.3 Government Receivables. Where the receivables contract has been entered into with the government or a government agency, are there different requirements and laws that apply to the sale or collection of those receivables?

The application of relevant rules to contracting with government will depend on which "arm" of the "government" a party is contracting with (e.g., whether it is the Commonwealth or a state, and whether it is the Crown in the right of the Commonwealth or a state, or a separate statutory corporation formed under federal or state law). Government contracts for receivables are generally subject to the

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same requirements and laws as contracts between other persons, but there can be some modifications in their application (for example, the powers of the Commonwealth are limited by the Constitution of Australia and a statutory corporation will only have the powers enumerated in its constituting statute). Other important points to note include:

- the parliament of the Commonwealth or a state or territory can pass laws that affect a contract it has previously entered into;
- enforcement against the Crown is subject to special procedures under Crown proceedings legislation;
- the payment of a debt owed by the Crown from government revenue must be authorised by legislation; and
- in very limited cases, executive necessity may allow the Crown to breach a contract without penalty on the basis of its public responsibility.

2 Choice of Law – Receivables Contracts

2.1 No Law Specified. If the seller and the obligor do not specify a choice of law in their receivables contract, what are the main principles in your jurisdiction that will determine the governing law of the contract?

In these circumstances, an Australian court will generally determine the governing law by:

- firstly, assessing whether an implied choice of law can be inferred as a matter of contractual construction; and
- secondly, if no such implied choice of law can be inferred, by identifying the law with the closest and most real connection to the contract (having regard to factors such as the place of residence and business of the parties).

2.2 Base Case. If the seller and the obligor are both resident in your jurisdiction, and the transactions giving rise to the receivables and the payment of the receivables take place in your jurisdiction, and the seller and the obligor choose the law of your jurisdiction to govern the receivables contract, is there any reason why a court in your jurisdiction would not give effect to their choice of law?

Australian courts will generally give effect to an express choice of law, subject to that choice being *bona fide*, there not being any public policy reason for not giving effect to the choice of law, and the choice of law not infringing any statute of the forum. On the facts of the base case, it is unlikely that any of those vitiating factors would apply.

2.3 Freedom to Choose Foreign Law of Non-Resident Seller or Obligor. If the seller is resident in your jurisdiction but the obligor is not, or if the obligor is resident in your jurisdiction but the seller is not, and the seller and the obligor choose the foreign law of the obligor/seller to govern their receivables contract, will a court in your jurisdiction give effect to the choice of foreign law? Are there any limitations to the recognition of foreign law (such as public policy or mandatory principles of law) that would typically apply in commercial relationships such as that between the seller and the obligor under the receivables contract?

Please see question 2.2. Australian courts will generally give effect to an express choice of foreign law, subject to the exceptions noted.

If questions of foreign law arise in Australian courts, the party asserting a particular effect of foreign law must prove that effect by providing expert evidence, and the Australian courts treat the effect as a question of fact to be established by evidence.

3 Choice of Law – Receivables Purchase Agreement

3.1 Base Case. Does your jurisdiction's law generally require the sale of receivables to be governed by the same law as the law governing the receivables themselves? If so, does that general rule apply irrespective of which law governs the receivables (i.e., your jurisdiction's laws or foreign laws)?

There is no general rule in Australia that the sale of receivables needs to be governed by the same law as the receivables themselves and, as noted in question 2.2, Australian courts will generally respect a choice of law (subject to certain exceptions). However, the law of the receivable is still relevant (for example, in construing the rights and obligations of the parties to the receivable contract).

The PPSA has separate conflict of law rules which are complex. They do not affect the choice of law of the sale of receivables, but are raised here for completeness. Generally speaking, the PPSA applies to a transfer of receivables if the seller is located in Australia or if the receivable is an Account or Chattel Paper payable in Australia. One or both of these are satisfied in most Australian securitisations. If the PPSA applies:

- perfection as against the debtor is governed by the PPSA rules (see question 4.2); and
- perfection as against third parties asserting a competing interest in the receivable is generally determined by the laws of the jurisdiction in which the seller is located. However, because of the complexity in this area, we expect that in practice purchasers will often register even if the seller is located outside Australia.

3.2 Example 1: If (a) the seller and the obligor are located in your jurisdiction, (b) the receivable is governed by the law of your jurisdiction, (c) the seller sells the receivable to a purchaser located in a third country, (d) the seller and the purchaser choose the law of your jurisdiction to govern the receivables purchase agreement, and (e) the sale complies with the requirements of your jurisdiction, will a court in your jurisdiction recognise that sale as being effective against the seller, the obligor and other third parties (such as creditors or insolvency administrators of the seller and the obligor)?

If the seller is located in Australia, Australian requirements would apply as discussed in question 3.1.

3.3 Example 2: Assuming that the facts are the same as Example 1, but either the obligor or the purchaser or both are located outside your jurisdiction, will a court in your jurisdiction recognise that sale as being effective against the seller and other third parties (such as creditors or insolvency administrators of the seller), or must the foreign law requirements of the obligor's country or the purchaser's country (or both) be taken into account?

If the seller is located in Australia, Australian requirements would

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apply as discussed in question 3.1. However, the law of the obligor's country may also be relevant, particularly if it has rules on how the obligation can be transferred.

3.4 Example 3: If (a) the seller is located in your jurisdiction but the obligor is located in another country, (b) the receivable is governed by the law of the obligor's country, (c) the seller sells the receivable to a purchaser located in a third country, (d) the seller and the purchaser choose the law of the obligor's country to govern the receivables purchase agreement, and (e) the sale complies with the requirements of the obligor's country, will a court in your jurisdiction recognise that sale as being effective against the seller and other third parties (such as creditors or insolvency administrators of the seller) without the need to comply with your jurisdiction's own sale requirements?

The same answer applies as for question 3.3.

3.5 Example 4: If (a) the obligor is located in your jurisdiction but the seller is located in another country, (b) the receivable is governed by the law of the seller's country, (c) the seller and the purchaser choose the law of the seller's country to govern the receivables purchase agreement, and (d) the sale complies with the requirements of the seller's country, will a court in your jurisdiction recognise that sale as being effective against the obligor and other third parties (such as creditors or insolvency administrators of the obligor) without the need to comply with your jurisdiction's own sale requirements?

If the obligor's debt is payable in Australia, Australian requirements will apply as discussed in question 3.1 in addition to the requirements of the seller's country.

3.6 Example 5: If (a) the seller is located in your jurisdiction (irrespective of the obligor's location), (b) the receivable is governed by the law of your jurisdiction, (c) the seller sells the receivable to a purchaser located in a third country, (d) the seller and the purchaser choose the law of the purchaser's country to govern the receivables purchase agreement, and (e) the sale complies with the requirements of the purchaser's country, will a court in your jurisdiction recognise that sale as being effective against the seller and other third parties (such as creditors or insolvency administrators of the seller, any obligor located in your jurisdiction and any third party creditor or insolvency administrator of any such obligor)?

If the seller is located in Australia, Australian requirements would apply as discussed in question 3.1 in addition to the other applicable requirements.

4 Asset Sales

4.1 Sale Methods Generally. In your jurisdiction what are the customary methods for a seller to sell receivables to a purchaser? What is the customary terminology – is it called a sale, transfer, assignment or something else?

In Australia, a sale of receivables is generally by way of legal or equitable assignment.

Under a legal assignment, legal and equitable title is passed to the purchaser, who becomes sole owner of the receivable. A legal assignment must be an absolute assignment in writing of the whole of a present debt, with written notice to the debtor.

Equitable assignments are more common in securitisation transactions, under which the purchaser obtains beneficial ownership of the receivable, but legal title remains with the seller. An equitable assignment requires valuable consideration and a clear intention to assign identifiable receivables and may have additional risks including that:

- the debtor may be fully discharged by paying the seller, and may exercise set-offs against the seller (see question 4.13);
- the seller may sell the same receivable to another purchaser (PPSA registration (see question 4.2) and otherwise notice to the debtor can overcome this); and
- the purchaser may need to join the seller in actions against the debtor.

4.2 Perfection Generally. What formalities are required generally for perfecting a sale of receivables? Are there any additional or other formalities required for the sale of receivables to be perfected against any subsequent good faith purchasers for value of the same receivables from the seller?

Perfection is governed by property law statutes in the various Australian states and territories and by the rules of equity. The PPSA also imposes separate but overlapping perfection rules where the receivables are "Accounts" or "Chattel Paper" under the PPSA, which will be the case in most Australian securitisations.

"Perfection" in this context has two elements:

(a) obtaining the best interest against the debtor:
  - a legal assignment is fully perfected against the debtor and an equitable assignment can be perfected by notice to the debtor; and
  - under the PPSA, despite notice to the debtor, the debtor and the seller may modify the contract as it relates to payments that have not been fully earned by performance, but only if, amongst other things, this does not materially adversely affect a purchaser's rights; and

(b) obtaining best interest against third parties:
  - the interest of an assignee of Accounts or Chattel Paper is a deemed security interest under the PPSA, which can be registered under the PPSA giving a priority based on registration time against other interest holders (including other purchasers);
  - failure to register under the PPSA does not invalidate the assignment as against the debtor or any insolvency official appointed to the debtor;
  - where the receivable is Chattel Paper, a promissory note or certain other negotiable instruments, a holder of the original instrument may have PPSA priority over other registered assignees; and

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- where the PPSA does not apply, notice of assignment to the debtor will generally give priority over other interested parties who have not yet given notice.

4.3 Perfection for Promissory Notes, etc. What additional or different requirements for sale and perfection apply to sales of promissory notes, mortgage loans, consumer loans or marketable debt securities?

The general rules are set out in questions 4.1 and 4.2. However, each of these debt classes raises specific issues. For example:

- an assignment of promissory notes does not require PPSA perfection;
- an assignment of mortgage loans may require registration of land mortgage transfers on land titles registers;
- assignment clauses in consumer and small business loans can, in some cases, give rise to unfair contract terms issues; and
- marketable debt securities sold through clearing systems are subject to the rules of the clearing system.

4.4 Obligor Notification or Consent. Must the seller or the purchaser notify obligors of the sale of receivables in order for the sale to be effective against the obligors and/or creditors of the seller? Must the seller or the purchaser obtain the obligors' consent to the sale of receivables in order for the sale to be an effective sale against the obligors? Whether or not notice is required to perfect a sale, are there any benefits to giving notice – such as cutting off obligor set-off rights and other obligor defences?

Notice of the assignment will allow the purchaser to enjoy the benefits described in questions 4.1 and 4.2. Notice is not always given at the time of assignment, however, and many market participants rely on an ability to perfect assignment at a later date if required.

If the receivables contract permits, or does not prohibit, an assignment, then obligor consent is not required.

If the contract prohibits assignment, but the receivable is an Account or Chattel Paper under the PPSA, then an assignment is valid regardless of lack of consent. However, the debtor may have contractual and tortious remedies arising out of contract breach.

4.5 Notice Mechanics. If notice is to be delivered to obligors, whether at the time of sale or later, are there any requirements regarding the form the notice must take or how it must be delivered? Is there any time limit beyond which notice is ineffective – for example, can a notice of sale be delivered after the sale, and can notice be delivered after insolvency proceedings have commenced against the obligor or the seller? Does the notice apply only to specific receivables or can it apply to any and all (including future) receivables? Are there any other limitations or considerations?

The notice can be delivered at any time. However, payments occurring and competing interests arising before the notice is given are not affected by such notice.

For a legal assignment, the notice must be in writing and comply with certain state-based requirements under applicable legislation.

If the PPSA applies, the notice must comply with the content requirements set out in the PPSA.

4.6 Restrictions on Assignment – General Interpretation. Will a restriction in a receivables contract to the effect that "None of the [seller's] rights or obligations under this Agreement may be transferred or assigned without the consent of the [obligor]" be interpreted as prohibiting a transfer of receivables by the seller to the purchaser? Is the result the same if the restriction says "This Agreement may not be transferred or assigned by the [seller] without the consent of the [obligor]" (i.e., the restriction does not refer to rights or obligations)? Is the result the same if the restriction says "The obligations of the [seller] under this Agreement may not be transferred or assigned by the [seller] without the consent of the [obligor]" (i.e., the restriction does not refer to rights)?

Australian courts would generally interpret each of these contractual restrictions as prohibiting a transfer or assignment of receivables by the seller to the purchaser without consent. However, where a contract requires consent and such consent is forthcoming, the assignment of contractual rights would be permissible.

It is likely that Australian courts would find no difference between the first two formulations above. The third formulation does not specifically prohibit the transfer of rights (with or without consent). Therefore, under the third formulation, it may be possible to assign certain rights without consent.

4.7 Restrictions on Assignment; Liability to Obligor. If any of the restrictions in question 4.6 are binding, or if the receivables contract explicitly prohibits an assignment of receivables or "seller's rights" under the receivables contract, are such restrictions generally enforceable in your jurisdiction? Are there exceptions to this rule (e.g., for contracts between commercial entities)? If your jurisdiction recognises restrictions on sale or assignment of receivables and the seller nevertheless sells receivables to the purchaser, will either the seller or the purchaser be liable to the obligor for breach of contract or tort, or on any other basis?

If the contract prohibits assignment but the receivable is an Account or Chattel Paper under the PPSA, an assignment is generally valid regardless of lack of consent. However, the debtor may have contractual and tortious remedies arising out of contract breach.

If the PPSA does not apply, a contractual restriction prohibiting assignment may mean that any assignment without consent is invalid between the obligor and the purchaser.

4.8 Identification. Must the sale document specifically identify each of the receivables to be sold? If so, what specific information is required (e.g., obligor name, invoice number, invoice date, payment date, etc.)? Do the receivables being sold have to share objective characteristics? Alternatively, if the seller sells *all* of its receivables to the purchaser, is this sufficient identification of receivables? Finally, if the seller sells *all* of its receivables *other than* receivables owing by one or more specifically identified obligors, is this sufficient identification of receivables?

The sale document must adequately identify the receivables to be sold such that at any point in time those receivables that are subject to the assignment can be distinguished from those that are not by reference to the wording of the sale document. However, provided that the class of receivables being transferred can be, and

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is, identified with adequate certainty to distinguish it from other receivables, this need not be achieved through listing each specific receivable.

The receivables being sold do not need to share the same objective characteristics but it is quite common for receivables being sold to share specified "eligibility criteria".

A sale can generally be drafted to attach to all of the receivables of the seller, provided that "receivables" are sufficiently defined for these purposes, and a sale of all receivables other than specifically identified receivables (or adequately identified classes of receivables) can also generally be structured.

If receivables are secured by security over cars, ships, aircraft or certain intellectual property rights, then there may be benefits in registering that underlying security with respect to the serial number for those items.

4.9 Recharacterisation Risk. If the parties describe their transaction in the relevant documents as an outright sale and explicitly state their intention that it be treated as an outright sale, will this description and statement of intent automatically be respected or is there a risk that the transaction could be characterised by a court as a loan with (or without) security? If recharacterisation risk exists, what characteristics of the transaction might prevent the transfer from being treated as an outright sale? Among other things, to what extent may the seller retain any of the following without jeopardising treatment as an outright sale: (a) credit risk; (b) interest rate risk; (c) control of collections of receivables; (d) a right of repurchase/redemption; (e) a right to the residual profits within the purchaser; or (f) any other term?

The language of the contract should clearly and expressly be that of a sale and the legal character of the rights and obligations created by the terms of the contract should be consistent with that language. Australian courts are likely to look to the legal substance of the transaction rather than its economic substance. In particular, a court is likely to adopt a two-step analytical process:

- firstly, a determination of the rights and obligations the parties gave each other under the terms of the sale contract; and
- secondly, the characterisation of such rights and obligations as a matter of law (without regard to the intention of the parties).

The transaction must not be a "sham". The parties must not disguise the transaction as a sale, if the true nature of the rights and obligations intended by the parties are not those of a sale.

Not all "retention" factors will undermine the characterisation as a sale. For example:

- it is common for the seller to act as servicer of the receivables;
- there are accepted ways to structure purchase price mechanics to provide for variable or deferred elements; and
- the seller may provide indemnity protection for representations and warranties relating to the receivables.

In addition, a sale should not be recharacterised simply because the seller has a right to repurchase the transferred receivables. However, a right of repurchase may increase the risk of recharacterisation if it exists in conjunction with other features which, taken together, suggest the creation of legal rights and obligations inconsistent with those of a sale.

Under the PPSA, a transfer of Accounts or Chattel Paper is generally treated as a security interest regardless of economic effect. However, if a transfer of Accounts or Chattel Paper does "secure payment or performance of an obligation", then the proceeds are subject to a mandatory waterfall which requires residual proceeds to be returned to the seller after the secured obligation has been satisfied. It seems unlikely that this will apply unless the whole transaction is recharacterised as a secured loan.

4.10 Continuous Sales of Receivables. Can the seller agree in an enforceable manner to continuous sales of receivables (i.e., sales of receivables as and when they arise)? Would such an agreement survive and continue to transfer receivables to the purchaser following the seller's insolvency?

Yes, a present assignment of adequately identified future property for valuable consideration can be recognised in equity (but not at common law).

Please see question 4.11 further in relation to a subsequent insolvency.

4.11 Future Receivables. Can the seller commit in an enforceable manner to sell receivables to the purchaser that come into existence after the date of the receivables purchase agreement (e.g., "future flow" securitisation)? If so, how must the sale of future receivables be structured to be valid and enforceable? Is there a distinction between future receivables that arise prior to versus after the seller's insolvency?

Yes, as per question 4.10. The sale should be for valuable consideration with the sale documentation including clear and unambiguous identification of the receivables to be assigned. The assignment of the future receivables should occur automatically by the terms of the sale contract without any further act being required. If properly drafted, the receivable should vest in the purchaser immediately upon coming into existence and there is some legal authority to support the validity of the assignment after the commencement of a winding up of the seller. However, arrangements under which payments continue – at least for some period – to be made to the seller, can potentially have an impact on the purchaser. Although the purchaser may be able to trace receipts into the assets of the seller, the purchaser will not be in an effective position to control receipts. Please also see question 6.5 and, in relation to the PPSA, above.

4.12 Related Security. Must any additional formalities be fulfilled in order for the related security to be transferred concurrently with the sale of receivables? If not all related security can be enforceably transferred, what methods are customarily adopted to provide the purchaser the benefits of such related security?

The formalities required for a legal assignment of related securities will depend on the type of related security involved. For example, a legal assignment of a real property mortgage will require the registration of a transfer of the mortgage on the relevant land titles register. Transfers of related securities regulated by the PPSA will need to be perfected by PPSA registration.

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4.13 Set-Off; Liability to Obligor. Assuming that a receivables contract does not contain a provision whereby the obligor waives its right to set-off against amounts it owes to the seller, do the obligor's set-off rights terminate upon its receipt of notice of a sale? At any other time? If a receivables contract does not waive set-off but the obligor's set-off rights are terminated due to notice or some other action, will either the seller or the purchaser be liable to the obligor for damages caused by such termination?

Australia recognises a number of different types of set-off. The effect of notice on these rights will depend on the type of set-off in question. Generally, notice will terminate the accrual of rights of contractual or statutory set-off, but will not terminate any accrued rights in respect of pre-notice cross-debts. An assignee will generally take subject to any such accrued rights of set-off and any other equities. In the case of equitable set-off, the assignee may in some circumstances take subject to equitable set-off in respect of both pre- and post-notice cross-claims. Insolvency set-off is mandatory and self-executing, but the mutuality requirement for insolvency set-off will generally be destroyed by the assignment.

The mere operation of these principles to fix the rights of the parties is unlikely to give rise to liability for damages. However, if, for example, the termination of set-off rights arose from an assignment in breach of the underlying agreement, the obligor may in some circumstances have a claim for contractual or tortious remedies such as damages in respect of the relevant breach.

4.14 Profit Extraction. What methods are typically used in your jurisdiction to extract residual profits from the purchaser?

In Australia, the securitisation vehicle is most commonly a trust, from which residual profit can be extracted by distributions to the beneficiaries of that trust. The originator may also act as subscriber for one or more classes of notes issued by the trust and returns can be extracted on these notes. Fees can also be extracted by the originator acting as, for example, servicer or manager of the trust.

5 Security Issues

5.1 Back-up Security. Is it customary in your jurisdiction to take a "back-up" security interest over the seller's ownership interest in the receivables and the related security, in the event that an outright sale is deemed by a court (for whatever reason) not to have occurred and have been perfected (see question 4.9 above)?

It is not customary to take "back-up" security to address the risk that the sale is deemed by a court not to have been perfected.

5.2 Seller Security. If it is customary to take back-up security, what are the formalities for the seller granting a security interest in receivables and related security under the laws of your jurisdiction, and for such security interest to be perfected?

The security interest will need to be perfected by PPSA registration. Please see question 5.3.

5.3 Purchaser Security. If the purchaser grants security over all of its assets (including purchased receivables) in favour of the providers of its funding, what formalities must the purchaser comply with in your jurisdiction to grant and perfect a security interest in purchased receivables governed by the laws of your jurisdiction and the related security?

The most common form of security is a general security interest over all assets of the purchaser.

The security interest must be perfected by PPSA registration within prescribed time limits. It is possible to perfect security interests in some assets by possession or control only, with no registration, but this is unusual in the securitisation context.

5.4 Recognition. If the purchaser grants a security interest in receivables governed by the laws of your jurisdiction, and that security interest is valid and perfected under the laws of the purchaser's jurisdiction, will the security be treated as valid and perfected in your jurisdiction or must additional steps be taken in your jurisdiction?

If the purchaser is an Australian company or an Australian registered foreign company, then the security interest must comply with Australian validity and perfection rules.

Where the purchaser is not Australian or Australian registered, the Australian conflict of laws rules for intangible property are complex. In practice, most security interests over receivables governed by Australian law are taken so as to comply with validity and perfection requirements in Australia. Please see section 3 for further details.

5.5 Additional Formalities. What additional or different requirements apply to security interests in or connected to insurance policies, promissory notes, mortgage loans, consumer loans or marketable debt securities?

As a general matter, there are no additional or different requirements except as noted in section 4.

5.6 Trusts. Does your jurisdiction recognise trusts? If not, is there a mechanism whereby collections received by the seller in respect of sold receivables can be held or be deemed to be held separate and apart from the seller's own assets (so that they are not part of the seller's insolvency estate) until turned over to the purchaser?

Yes, Australia recognises trusts.

Collection trusts are commonly used in Australian securitisation transactions. Collection trusts and turnover trusts may be security interests under the PPSA, and it is common to register them.

5.7 Bank Accounts. Does your jurisdiction recognise escrow accounts? Can security be taken over a bank account located in your jurisdiction? If so, what is the typical method? Would courts in your jurisdiction recognise a foreign law grant of security (for example, an English law debenture) taken over a bank account located in your jurisdiction?

Escrow accounts are recognised in Australia, but are uncommon.

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It is more common for the purchaser to take security over the payment bank account.

Security is commonly taken over bank accounts under a security agreement by way of charge or mortgage and perfected by PPSA registration. Tripartite arrangements with the account bank are recommended.

Where the security holder is an Australian authorised deposit-taking institution ("**ADI**") and it is taking security over an account for which it is the account bank, it has absolute priority and registration is not required.

As a general rule, Australian courts will recognise and enforce foreign-law security over bank accounts in Australia. However, Australian rules for validity and perfection apply in most cases.

5.8 Enforcement over Bank Accounts. If security over a bank account is possible and the secured party enforces that security, does the secured party control all cash flowing into the bank account from enforcement forward until the secured party is repaid in full, or are there limitations? If there are limitations, what are they?

The secured party, or any receiver appointed by it, controls all cash from enforcement forward. However, if the secured party does not control the bank account for the purposes of the PPSA, then certain statutory preferred creditors may have priority rights to the bank account, which can disrupt the secured party's control of the cash.

5.9 Use of Cash Bank Accounts. If security over a bank account is possible, can the owner of the account have access to the funds in the account prior to enforcement without affecting the security?

Yes, generally, as long as that is provided for in the terms of the security document.

6 Insolvency Laws

6.1 Stay of Action. If, after a sale of receivables that is otherwise perfected, the seller becomes subject to an insolvency proceeding, will your jurisdiction's insolvency laws automatically prohibit the purchaser from collecting, transferring or otherwise exercising ownership rights over the purchased receivables (a "stay of action")? If so, what generally is the length of that stay of action? Does the insolvency official have the ability to stay collection and enforcement actions until he determines that the sale is perfected? Would the answer be different if the purchaser is deemed to only be a secured party rather than the owner of the receivables?

If the sale of receivables is a true sale by way of legal assignment and has been perfected, a seller's insolvency should not interfere with a purchaser's rights in respect of the purchased receivables (subject to those matters discussed at question 6.3). If there has been a true sale, but it is only by way of equitable assignment, the position may be more complex and practical issues may arise. If there is any doubt as to whether the assignment has been perfected, an administrator or liquidator of the seller may obtain an interim injunction from a court staying the enforcement by the purchaser of its rights, pending judgment from the court as to whether the assignment has been perfected.

If the purchaser is deemed to be only a secured party (in the sense of holding a security interest such as a charge over the receivables) rather than the owner of the receivables, then, broadly, if the security interest:

- is a "circulating security interest", it may in certain circumstances be void against the company's liquidator;
- is not perfected, it will vest in the seller upon its going into administration or liquidation;
- is perfected by registration and by no other means and registration occurred within certain prescribed time periods, the interest will vest in the seller upon its going into administration or liquidation; and
- is perfected:
  - the purchaser will be bound by the statutory stay on enforcement during the administration of the seller; and
  - an administrator of the seller may be able to dispose of the receivables which are the subject of the security interest in the ordinary course of the seller's business in certain circumstances.

The period of the stay on enforcement of security interests during administration referred to above is typically between 15 and 30 business days, but this period may be extended as a result of a resolution of creditors or orders of the court (and can be extended by up to a year or possibly longer).

To the extent that the purchaser is exercising a contractual right against the seller in collecting, transferring or otherwise exercising ownership rights over the purchased receivables, it may also be subject to a stay during the administration period (refer to the first bullet point in the answer to question 8.7 below).

6.2 Insolvency Official's Powers. If there is no stay of action, under what circumstances, if any, does the insolvency official have the power to prohibit the purchaser's exercise of its ownership rights over the receivables (by means of injunction, stay order or other action)?

An insolvency official does not generally have the power to prohibit the purchaser's exercise of rights in connection with an effective sale of receivables, other than in the circumstances discussed in questions 6.1 and 6.3. However, the insolvency official is not required to assist the purchaser where such assistance is necessary for the purchaser to exercise their rights.

6.3 Suspect Period (Clawback). Under what facts or circumstances could the insolvency official rescind or reverse transactions that took place during a "suspect" or "preference" period before the commencement of the seller's insolvency proceedings? What are the lengths of the "suspect" or "preference" periods in your jurisdiction for (a) transactions between unrelated parties, and (b) transactions between related parties? If the purchaser is majority-owned or controlled by the seller or an affiliate of the seller, does that render sales by the seller to the purchaser "related party transactions" for purposes of determining the length of the suspect period? If a parent company of the seller guarantee's the performance by the seller of its obligations under contracts with the purchaser, does that render sales by the seller to the purchaser "related party transactions" for purposes of determining the length of the suspect period?

If a transaction takes place within a specified "suspect" or "preference" period, a liquidator may be able to have the transaction set aside if it is a "voidable transaction". In general terms,

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voidable transactions include unfair preferences and uncommercial transactions while the company was insolvent, unfair loans and unreasonable director-related transactions. The suspect period depends on the type of voidable transaction (for example, it is generally six months from the commencement of administration or liquidation for unfair preferences and two years for uncommercial transactions, but this may be extended to either four or 10 years in certain circumstances).

The suspect period for insolvent transactions involving related entities is four years, which may apply where the purchaser is majority owned or controlled by the seller or the purchaser and the seller are otherwise part of the same corporate group. The existence of a guarantee by a parent company of the seller does not on its own render sales "related party transactions".

6.4 Substantive Consolidation. Under what facts or circumstances, if any, could the insolvency official consolidate the assets and liabilities of the purchaser with those of the seller or its affiliates in the insolvency proceeding? If the purchaser is owned by the seller or by an affiliate of the seller, does that affect the consolidation analysis?

Assuming that the purchaser and the seller are separate and independent bodies, there is no statutory right or established Australian line of authority that would allow an insolvency official to consolidate their assets in insolvency proceedings. However, if the purchaser and the seller are related entities and/or their affairs are intermingled in a prescribed manner, it may be possible for a liquidator to obtain a pooling order or to make a pooling determination to permit the purchaser and the seller to be wound up on a pooled basis. Further, the assets and liabilities of corporate groups with complex cross-guarantees may be aggregated in certain circumstances.

6.5 Effect of Insolvency on Receivables Sales. If insolvency proceedings are commenced against the seller in your jurisdiction, what effect do those proceedings have on (a) sales of receivables that would otherwise occur after the commencement of such proceedings, or (b) on sales of receivables that only come into existence after the commencement of such proceedings?

Once certain insolvency proceedings have been commenced:

- no sale of receivables can occur unless the relevant insolvency official or the relevant Australian court consents;
- if the contract has been entered into but the purchase price has not been paid (or the purchaser has not otherwise acquired a proprietary interest in the receivables), the purchaser will have an unsecured claim against the seller with regards to any loss the purchaser suffers; and
- if there has been a true sale of future receivables, and the purchaser has paid the purchase price in full prior to the initiation of administration or liquidation, then (subject to the discussion in questions 6.1 and 6.3) the seller's insolvency alone will not affect the purchaser's rights in relation to the receivables.

6.6 Effect of Limited Recourse Provisions. If a debtor's contract contains a limited recourse provision (see question 7.3 below), can the debtor nevertheless be declared insolvent on the grounds that it cannot pay its debts as they become due?

In Australia, a company is insolvent if it cannot pay its debts as and when they fall due and payable. The equivalent position for vehicles established as trusts is more complicated, as a trust is not a separate legal entity from its trustee.

To our knowledge, Australian courts have not specifically looked at the effect of limited recourse clauses on a company's solvency. It is unlikely that Australian courts would consider that a limited recourse debt is "payable" to the extent that it exceeds the value of the assets to which a properly drafted limited recourse clause is directed, such that the failure by a debtor to pay that portion of the debt which exceeded the value of the assets could render the debtor insolvent. However, we are aware of an English judgment to the contrary which, whilst not binding on Australian courts and made in unusual circumstances, may still be persuasive in some circumstances.

7 Special Rules

7.1 Securitisation Law. Is there a special securitisation law (and/or special provisions in other laws) in your jurisdiction establishing a legal framework for securitisation transactions? If so, what are the basics? Is there a regulatory authority responsible for regulating securitisation transactions in your jurisdiction?

Although Australia does have a legislative framework for covered bonds, it does not have a specific legislative framework for securitisation. However, in the case of securitisations involving ADIs, APS 120 (a prudential standard specific to securitisation established by the Australian Prudential Regulation Authority ("**APRA**")) applies, and APRA has primary responsibility for regulating the prudential aspects of securitisation. In addition, some Australian laws (such as stamp duty laws) make specific provision for securitisation in certain circumstances (for example, in the form of exemptions), and many laws of general application will impact a securitisation transaction.

7.2 Securitisation Entities. Does your jurisdiction have laws specifically providing for establishment of special purpose entities for securitisation? If so, what does the law provide as to: (a) requirements for establishment and management of such an entity; (b) legal attributes and benefits of the entity; and (c) any specific requirements as to the status of directors or shareholders?

Australia does not have a specific legislative framework for the establishment of special purpose entities for securitisation.

7.3 Location and form of Securitisation Entities. Is it typical to establish the special purpose entity in your jurisdiction or offshore? If in your jurisdiction, what are the advantages to locating the special purpose entity in your jurisdiction? If offshore, where are special purpose entities typically located for securitisations in your jurisdiction? What are the forms that the special purpose entity would normally take in your jurisdiction and how would such entity usually be owned?

Securitisation vehicles are most commonly established in Australia as special purpose trusts, but can also be established as special purpose companies.

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Advantages to using an Australian trust include that (a) the Australian market is familiar with trust structures, and (b) governance of the trust is relatively easy to implement (for example, a manager can be appointed and allocated special duties and control rights).

Where structured as a special purpose trust, it is common for all or a majority of the trust units to be owned by the seller or a related entity of the seller.

The securitisation vehicle may be established offshore where, for example, debtors or receivables are located offshore.

7.4 Limited-Recourse Clause. Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) limiting the recourse of parties to that agreement to the available assets of the relevant debtor, and providing that to the extent of any shortfall the debt of the relevant debtor is extinguished?

Australian courts should generally give effect to a clause limiting the recourse of parties to specified assets provided that the contract itself is enforceable (and, in the case of a contract governed by the foreign law, that contract and the limited recourse clause are enforceable as a matter of the foreign law). However, please see question 1.2 and section 8 in relation to consumer contracts.

7.5 Non-Petition Clause. Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) prohibiting the parties from: (a) taking legal action against the purchaser or another person; or (b) commencing an insolvency proceeding against the purchaser or another person?

Australian courts should generally give effect to a clause prohibiting a creditor from taking legal action or commencing an insolvency proceeding (subject to the corresponding provisos in question 7.4). However, please see question 1.2 and section 8 in relation to consumer contracts.

7.6 Priority of Payments "Waterfall". Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) distributing payments to parties in a certain order specified in the contract?

Yes, an Australian court should generally give effect to properly drafted contractual provisions which provide for the application of proceeds from the enforcement of security over the securitisation vehicle's assets, to the creditors bound by such provisions and entitled to such proceeds in a prescribed order (and, in the case of a foreign law-governed waterfall, on the assumption that the waterfall is enforceable under the relevant foreign laws). However, certain creditors have priority entitlements under Australian law which cannot be contracted out of in a priority waterfall. For example, liquidators are entitled to be paid their remuneration and expenses in realising assets in priority to secured creditors. Employees also have certain priority entitlements.

7.7 Independent Director. Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) or a provision in a party's organisational documents prohibiting the directors from taking specified actions (including commencing an insolvency proceeding) without the affirmative vote of an independent director?

As directors are under a duty to act in the best interests of a company and to prevent a company from insolvent trading, any contractual provision or provision in a company's organisational documents prohibiting a director from taking specified actions could be contrary to those duties. As a general principle, Australian courts will not allow directors to act in accordance with such a provision where those actions would otherwise be inconsistent with their duties as directors. In exceptional circumstances, Australian courts have given effect to such provisions where they are subject to a "fiduciary out", allowing a director to act contrary to the contractual provision if the actions of the director would be in breach of any duty owed to the company or unlawful.

7.8 Location of Purchaser. Is it typical to establish the purchaser in your jurisdiction or offshore? If in your jurisdiction, what are the advantages to locating the purchaser in your jurisdiction? If offshore, where are purchasers typically located for securitisations in your jurisdiction?

The same answer applies as for question 7.3.

8 Regulatory Issues

8.1 Required Authorisations, etc. Assuming that the purchaser does no other business in your jurisdiction, will its purchase and ownership or its collection and enforcement of receivables result in its being required to qualify to do business or to obtain any licence or its being subject to regulation as a financial institution in your jurisdiction? Does the answer to the preceding question change if the purchaser does business with more than one seller in your jurisdiction?

The NCCPA (see question 1.2) applies if credit is provided to consumers in the course of a business of providing credit carried on in Australia or as part of, or incidentally to, any other business of the credit provider carried on in Australia (including where a person engages in conduct that is intended to induce people in Australia to use the goods or services of the person or is likely to have that effect, whether or not the conduct would have that effect in other places as well).

Where credit is provided to consumers, certain persons (e.g., credit providers and lessors and persons exercising their rights or obligations), will require an Australian Credit Licence ("**ACL**") unless an exemption applies. In the first instance this includes the purchaser where the legal title is perfected, as the collection and enforcement of the receivables will be carrying on a business of being credit provider in Australia. An exemption is available to securitisation entities in certain circumstances if specified requirements are met, and other exemptions may be available in particular circumstances.

As noted above, different requirements under the CA will apply if the receivables are margin loans.

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In addition to the ACL requirements, an Australian financial services licence ("**AFSL**") may be required by certain securitisation participants (e.g., trustees and trust managers) under the CA unless an exemption applies. The jurisdictional test in relation to AFSLs is similar to the NCCPA requirements and would unlikely be avoided on the basis that the only business carried on in Australia was in relation to receivables.

Further, the CA also requires a foreign company to be registered with the Australian Securities and Investments Commission if it will "carry on business in Australia", which will depend on a number of factors including whether there is some repetition of commercial activities in Australia.

Where a foreign company has as its sole or principal business in Australia the borrowing or lending of money, or has certain assets in Australia, it may also have to register under data collection and reporting legislation.

8.2 Servicing. Does the seller require any licences, etc., in order to continue to enforce and collect receivables following their sale to the purchaser, including to appear before a court? Does a third-party replacement servicer require any licences, etc., in order to enforce and collect sold receivables?

A servicer will be exercising the rights and obligations of a credit provider and will therefore require an ACL. This applies whether the servicer is an original or replacement servicer.

Certain Australian states and territories also have separate debt collection legislation which requires debt collectors to be registered or licensed in those jurisdictions.

The servicer may also require an AFSL if the receivables involve financial services regulated under the CA, including insurance or margin loans.

8.3 Data Protection. Does your jurisdiction have laws restricting the use or dissemination of data about or provided by obligors? If so, do these laws apply only to consumer obligors or also to enterprises?

The *Privacy Act 1988* (Cth) ("**PA**") regulates how personal information can be collected, used and disclosed. It imposes ongoing standards in relation to personal information, including security and access obligations.

The PA only applies to information about individuals, but applies regardless of the consumer's purpose in entering into the receivable. It extends to personal information about individuals collected in relation to a corporate customer (e.g., directors or employees).

The PA also contains specific requirements that apply to credit information. This information is subject to tighter restrictions on how the information can be collected, used and disclosed.

Bankers also have a duty of secrecy to their customers which arises out of the relationship between banker and customer. This duty applies to both individuals and corporates.

In addition, an equitable duty of confidentiality applies to information of a confidential nature, and unauthorised use or disclosure may constitute a breach of this duty. Contracts may also impose confidentiality obligations and a breach may result in a breach of contract.

8.4 Consumer Protection. If the obligors are consumers, will the purchaser (including a bank acting as purchaser) be required to comply with any consumer protection law of your jurisdiction? Briefly, what is required?

The NCCPA will apply where a debtor or lessee is a relevant consumer. See further questions 1.2 and 8.1.

If the receivables are sold, the debtor will generally have the same rights against the purchaser as against the original credit provider for failures to comply with the contract disclosure, and certain conduct and fee restrictions under the NCCPA.

Other relevant legislation includes various consumer protections such as:

- provisions making certain unfair contract terms void; and
- prohibitions against unconscionable conduct and misleading and deceptive conduct.

Relevant legislation also contains "linked credit provider" provisions, under which credit providers and lessors can be responsible for the conduct of third parties (e.g., retailers) where the contract or lease has been entered into to finance goods or services offered by those third parties.

8.5 Currency Restrictions. Does your jurisdiction have laws restricting the exchange of your jurisdiction's currency for other currencies or the making of payments in your jurisdiction's currency to persons outside the country?

Regulations can be made to control the buying, borrowing, selling, lending or exchanging of foreign currency in Australia, but there are no such regulations currently in place.

The approval or authorisation of the Minister for Foreign Affairs is required for certain transactions involving dealings with assets in connection with persons or entities linked to terrorist activities or certain proscribed countries.

Other regulations generally prohibit dealing with certain "designated persons or entities" by directly or indirectly making assets (including shares and securities) available to or for their benefit without a permit, and our anti-money laundering legislation may prohibit the entering into of transactions with residents of prescribed foreign countries (although no countries are currently prescribed).

There are no operative exchange controls on the transfer of money out of Australia but reporting obligations may apply to certain transfers.

8.6 Risk Retention. Does your jurisdiction have laws or regulations relating to "risk retention"? How are securitisation transactions in your jurisdiction usually structured to satisfy those risk retention requirements?

There is currently no separate explicit risk retention requirement in Australia for securitisation transactions.

8.7 Regulatory Developments. Have there been any regulatory developments in your jurisdiction which are likely to have a material impact on securitisation transactions in your jurisdiction?

The Australian financial sector has been subject to significant regulatory reform over recent years. Some of the key recent changes are described below:

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- The insolvency laws in Australia have recently been amended to introduce a stay on the enforcement of certain rights during an administration, receivership or a creditors' scheme of arrangement to avoid an insolvent liquidation. Broad anti-avoidance provisions will apply. It has not yet been confirmed what exclusions will apply; however, it is currently anticipated that exclusions will be made for certain financial contracts.
- In February 2018, all organisations who have personal information security obligations under the PA will be required to notify individuals if their personal information has been subject to a data breach. Data breaches will only have reported to individuals if the breach is "notifiable" (i.e., is likely to result in "serious harm" to the individual).
- Small amount credit contracts and consumer leases may also be subject to stricter regulatory requirements. There is currently legislation before parliament which will require all small amount credit contract providers to document in writing that the contract is not unsuitable and ensure the contracts have equal repayment instalments. All small amount credit contracts will also be subject to statutory earnings protections such that repayments cannot exceed 10% of the consumer's net income. Consumer leases will be subject to increased responsible lending obligations, protected earnings requirements, new disclosure requirements, caps on fees and charges, and other requirements. Anti-avoidance rules will apply to both small amount credit contracts and consumer leases.
- Credit card providers may also have increased responsible lending obligations under the NCCPA. Under proposed new legislation, providers must conduct an enhanced unsuitability assessment before a credit card contract is entered into or any increase in credit limit is approved. Retrospective interest rate charges on interest free periods will be prohibited. The current draft of the legislation also increases regulation around credit limits. Providers will be unable to offer unsolicited credit limit increases and must make it easier for consumers to reduce their credit limit or terminate their credit card contract.
- APRA's powers have been broadened to allow it to make rules and issue directions relating to the lending activities of non-ADI lenders where it has identified material risks of instability in the Australian financial system. Directions powers and penalties will also be introduced for non-ADI lenders who contravene a direction from APRA. This will give APRA further control over entities who provide finance in Australia but are not considered to be conducting "banking business" under the Banking Act 1959 as they do not take deposits, and have therefore not previously been subject to direct regulation by APRA.

9 Taxation

9.1 Withholding Taxes. Will any part of payments on receivables by the obligors to the seller or the purchaser be subject to withholding taxes in your jurisdiction? Does the answer depend on the nature of the receivables, whether they bear interest, their term to maturity, or where the seller or the purchaser is located? In the case of a sale of trade receivables at a discount, is there a risk that the discount will be recharacterised in whole or in part as interest? In the case of a sale of trade receivables where a portion of the purchase price is payable upon collection of the receivable, is there a risk that the deferred purchase price will be recharacterised in whole or in part as interest? If withholding taxes might apply, what are the typical methods for eliminating or reducing withholding taxes?

Australia imposes withholding tax on, among other things, payments of interest or royalties from Australian residents to foreign resident recipients.

Whether Australian withholding tax will apply to payments, and the rate of withholding, will depend on:

- in the case of interest, whether the payments are interest, or in the nature of or in substitution for interest;
- in the case of royalties, whether the payment is regarded as a royalty for Australian tax purposes (which may include payments for the use of intellectual property and commercial or scientific equipment or information); and
- the country where the recipient is located.

The default rate of interest withholding tax in Australia is 10% and the default rate of royalty withholding tax in Australia is 30%. The rate may be reduced if the recipient is resident in a country with which Australia has a double tax treaty and the treaty limits the rate of withholding tax. Some treaties reduce the rate to nil in the case of interest withholding tax, and 5% in the case of royalty withholding tax.

For certain underlying receivables (e.g., certain notes), an exemption from interest withholding tax may be available if the underlying issue satisfies the public offer test. A company may satisfy the public offer test in a variety of ways, including offering the notes to 10 or more unrelated financiers or entities that carry on the business of investing in securities, or listing the notes on a stock exchange. There is no equivalent exemption for royalty withholding tax.

For the purposes of Australian interest withholding tax, there is a risk that any discount on a sale of trade receivables may be recharacterised as interest. The tax consequences of deferred payments will depend on the terms of the deferral (e.g., whether any contingencies are involved) and whether any part of the deferred payment is referable to or in substitution for interest.

After 31 December 2018, the U.S. Foreign Account Tax Compliance Act may require certain Australian obligors to withhold 30% tax from payments to certain non-compliant sellers or purchasers. Whether such withholding will apply will depend in part on the approach to "foreign passthru payments" to be developed by the U.S. Government, and any relevant treaties entered into or legislation implemented in other jurisdictions.

9.2 Seller Tax Accounting. Does your jurisdiction require that a specific accounting policy is adopted for tax purposes by the seller or purchaser in the context of a securitisation?

Australian taxation laws do not require a specific accounting standard to be adopted for securitisation. However, Australian accounting policies adopted by an entity can impact on the Australian tax treatment of the entity's income and outgoings in some situations. Specific provisions may apply to securitisation vehicles and in respect of financial transactions.

9.3 Stamp Duty, etc. Does your jurisdiction impose stamp duty or other transfer or documentary taxes on sales of receivables?

In Australia, stamp duty is imposed at the state and territory level on certain kinds of transactions or instruments. These stamp duty laws are not uniform in terms of which transactions or instruments are subject to duty, the rates of duty or the available exemptions. Up to eight separate sets of stamp duty laws can apply to a transaction. Generally, the location of the receivables and, in some cases, the related securities will determine which stamp duty laws need to be considered.

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Stamp duty issues that can arise in relation to a securitisation include on the transfer of receivables and on the granting of security, although exemptions can apply (for which the exact structure and drafting can be important).

9.4 Value Added Taxes. Does your jurisdiction impose value added tax, sales tax or other similar taxes on sales of goods or services, on sales of receivables or on fees for collection agent services?

Goods and services tax ("**GST**") in Australia is imposed at the rate of 10% of the GST-exclusive consideration for a taxable supply. The sale of receivables and related securities is not generally a taxable supply. However, the supply of collection agent services will generally be a taxable supply on which GST is payable by the supplier. In some circumstances, a securitisation vehicle may be entitled to claim back 75% of the GST payable by the service provider if the securitisation vehicle is registered for GST.

9.5 Purchaser Liability. If the seller is required to pay value-added tax, stamp duty or other taxes upon the sale of receivables (or on the sale of goods or services that give rise to the receivables) and the seller does not pay, then will the taxing authority be able to make claims for the unpaid tax against the purchaser or against the sold receivables or collections?

Australian tax law empowers relevant taxing authorities to collect tax debts (whether or not related to the relevant transaction) and other amounts owing to a recalcitrant taxpayer from third parties. This power generally applies where the third party owes or may later owe money to the taxpayer. In these circumstances, the relevant taxing authority is generally empowered to require the third party to pay the money directly to the taxing authority instead of to the taxpayer.

9.6 Doing Business. Assuming that the purchaser conducts no other business in your jurisdiction, would the purchaser's purchase of the receivables, its appointment of the seller as its servicer and collection agent, or its enforcement of the receivables against the obligors, make it liable to tax in your jurisdiction?

The purchaser's potential liability for Australian tax depends on its country of residence for tax purposes.

If the purchaser is resident in a country with which Australia has a double tax treaty, the purchaser should not be liable to Australian tax provided the purchaser does not have a permanent establishment in Australia. This may depend, amongst other things, on the terms of appointment of the seller as its agent in Australia. The terms of the treaty may also provide that particular income is taxable in Australia to a certain extent (e.g., withholding tax on interest).

If the purchaser is resident in a country with which Australia does not have a double tax treaty, the purchaser should only be liable for Australian tax on Australian sourced income. This is determined by reference to the nature of the income and relevant circumstances. In this respect, income that is subject to Australian withholding tax (e.g., interest) is not otherwise assessable in Australia.

9.7 Taxable Income. If a purchaser located in your jurisdiction receives debt relief as the result of a limited recourse clause (see question 7.3 above), is that debt relief liable to tax in your jurisdiction?

Australian commercial debt forgiveness ("**CDF**") provisions operate to claw back the tax benefit a debtor receives when a commercial debt owed by the debtor is forgiven.

In broad terms, a debt is a "commercial debt" if interest paid on the debt is *prima facie* allowable as a deduction to the debtor. A debt is "forgiven" where the obligation to pay is extinguished.

The debtor's deductible revenue losses, or other tax benefits and attributes, are reduced by the forgiven amount (taking into account certain adjustments). However, the provisions do not result in tax necessarily being payable by the debtor.

Acknowledgment

The authors acknowledge the significant contribution of Hal Bolitho in relation to all aspects of the PPSA analysis, and the valuable contributions of other members of our Banking & Finance team (including our regulatory team), our Taxation team, our Dispute Resolution team and our Mergers & Acquisitions team, who contributed to this chapter.

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- Banking Law Firm of the Year, *ALB China* Law Awards 2016 and 2017.
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- Banking and Finance Firm of the Year, *China Law and Practice* Awards 2017.
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Canada

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1 Receivables Contracts

1.1 Formalities. In order to create an enforceable debt obligation of the obligor to the seller: (a) is it necessary that the sales of goods or services are evidenced by a formal receivables contract; (b) are invoices alone sufficient; and (c) can a binding contract arise as a result of the behaviour of the parties?

(a) No, whether there is an enforceable debt will be determined by evidence of the intention of the parties. Nevertheless, receivables are typically not eligible for purchase unless evidenced by written documentation.

(b) Yes, if they are sufficient to identify and describe the transactions.

(c) Yes, but purchasers typically require written documentation.

1.2 Consumer Protections. Do your jurisdiction's laws: (a) limit rates of interest on consumer credit, loans or other kinds of receivables; (b) provide a statutory right to interest on late payments; (c) permit consumers to cancel receivables for a specified period of time; or (d) provide other noteworthy rights to consumers with respect to receivables owing by them?

(a) Under the Interest Act (Canada), any agreement which stipulates an interest rate must contain an annual interest rate or, where the rate is for a period of less than one year, an express statement of the annual equivalent interest rate. Failure to do so will result in the imposition of an interest rate not to exceed five per cent per year. In addition, where agreements are secured by real property, a higher rate of interest cannot be recovered on amounts in arrears. Even where no real property security is involved, a stepped-up interest rate after default may be unenforceable as a penalty.

The Criminal Code (Canada) makes it a criminal offence to receive an effective annual rate of interest that exceeds 60 per cent. Interest under the Criminal Code is broadly defined to include interest, fees, fines, penalties, commissions and similar charges and expenses that a borrower pays in connection with the credit advanced.

(b) Generally, no.

(c) Each province has consumer protection legislation which provides cooling-off periods with respect to sales made outside the seller's place of business (e.g. door-to-door sales) as well as certain types of consumer contracts. In addition, certain provinces provide consumers with rights of cancellation if the seller fails to meet certain mandatory disclosure requirements. Such information requirements may include cost of borrowing disclosure and other product and pricing information.

(d) Under the Interest Act, natural persons have a right in certain circumstances to prepay a mortgage in full (together with payment of an additional three months' interest) at any time after five years from the date of the loan if principal or interest under the mortgage are payable more than five years after the date of the loan. Under federal and provincial consumer protection legislation, providers of consumer financing are required to disclose the "cost of credit" or "cost of borrowing" associated with the financing, which includes not only interest but any other amounts that the borrower is required to pay as a condition of entering into the agreement, such as administration fees and registration fees, and disclosure of an "annual percentage rate" that annualises these costs.

1.3 Government Receivables. Where the receivables contract has been entered into with the government or a government agency, are there different requirements and laws that apply to the sale or collection of those receivables?

Yes, assignments of certain debts owed by the government of Canada and many federal Crown corporations are invalid unless the assignment is absolute and not by way of security only and notice in the prescribed form has been given to and acknowledged by the appropriate government official. Some provinces have similar restrictions. Complying with these restrictions may be onerous and time-consuming. Therefore, government receivables are often excluded as ineligible unless they comprise a large portion of the pool, in which case the statutory requirements must be complied with.

2 Choice of Law – Receivables Contracts

2.1 No Law Specified. If the seller and the obligor do not specify a choice of law in their receivables contract, what are the main principles in your jurisdiction that will determine the governing law of the contract?

If the parties do not specify a choice of law, the court will apply the law of the jurisdiction with the most real and substantial connection with the contract. The court will consider such factors as the place where the contract was entered into and is to be performed, the form and language of the contract, residence of the parties, and any

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arbitration or submission to jurisdiction clauses. Contract law is a matter of provincial jurisdiction, so the applicable jurisdiction in each case will be a particular province.

2.2 Base Case. If the seller and the obligor are both resident in your jurisdiction, and the transactions giving rise to the receivables and the payment of the receivables take place in your jurisdiction, and the seller and the obligor choose the law of your jurisdiction to govern the receivables contract, is there any reason why a court in your jurisdiction would not give effect to their choice of law?

Subject to certain exceptions and conditions discussed in question 2.3 below, courts will generally recognise and apply the parties' choice of governing law.

2.3 Freedom to Choose Foreign Law of Non-Resident Seller or Obligor. If the seller is resident in your jurisdiction but the obligor is not, or if the obligor is resident in your jurisdiction but the seller is not, and the seller and the obligor choose the foreign law of the obligor/seller to govern their receivables contract, will a court in your jurisdiction give effect to the choice of foreign law? Are there any limitations to the recognition of foreign law (such as public policy or mandatory principles of law) that would typically apply in commercial relationships such as that between the seller and the obligor under the receivables contract?

Courts generally recognise and apply contractual choice of law clauses if expert evidence of the foreign law is adduced, the choice is *bona fide* and legal and there is no reason for avoiding it on public policy grounds.

However, the court:

- will apply Canadian laws relating to procedural matters or laws having overriding effect (such as bankruptcy and insolvency, tax, securities or criminal law);
- will not give effect to foreign revenue, expropriatory or penal laws (except in Quebec, where there is reciprocity); and
- will not enforce any obligation whose performance would be illegal under the laws of any jurisdiction in which the obligation is to be performed.

3 Choice of Law – Receivables Purchase Agreement

3.1 Base Case. Does your jurisdiction's law generally require the sale of receivables to be governed by the same law as the law governing the receivables themselves? If so, does that general rule apply irrespective of which law governs the receivables (i.e., your jurisdiction's laws or foreign laws)?

Generally, no; however, perfection of the security interest deemed to be created by the absolute assignment of the receivables will be governed by the applicable domestic or foreign personal property security regime irrespective of which law governs the sale agreement or the receivables. The governing law for perfection purposes will be determined by conflict of law rules that cannot be varied by contract. For the purposes of this question and each example below, we have assumed that the reference to the domestic jurisdiction is a reference to a particular Canadian province.

3.2 Example 1: If (a) the seller and the obligor are located in your jurisdiction, (b) the receivable is governed by the law of your jurisdiction, (c) the seller sells the receivable to a purchaser located in a third country, (d) the seller and the purchaser choose the law of your jurisdiction to govern the receivables purchase agreement, and (e) the sale complies with the requirements of your jurisdiction, will a court in your jurisdiction recognise that sale as being effective against the seller, the obligor and other third parties (such as creditors or insolvency administrators of the seller and the obligor)?

Yes; however, the purchaser will also need to perfect the security interest deemed to be created as described in question 3.1. In addition, for the sale to be effective against the obligor, the obligor must be notified of the assignment as further described in question 4.4.

3.3 Example 2: Assuming that the facts are the same as Example 1, but either the obligor or the purchaser or both are located outside your jurisdiction, will a court in your jurisdiction recognise that sale as being effective against the seller and other third parties (such as creditors or insolvency administrators of the seller), or must the foreign law requirements of the obligor's country or the purchaser's country (or both) be taken into account?

Yes, subject to the considerations regarding choice of law, perfection and notice to obligors referred to in questions 2.3, 3.1, 3.2 and 4.4; provided that if the obligor is located in another jurisdiction, the effectiveness of such sale against the obligor will be subject to the laws of the jurisdiction of the obligor.

3.4 Example 3: If (a) the seller is located in your jurisdiction but the obligor is located in another country, (b) the receivable is governed by the law of the obligor's country, (c) the seller sells the receivable to a purchaser located in a third country, (d) the seller and the purchaser choose the law of the obligor's country to govern the receivables purchase agreement, and (e) the sale complies with the requirements of the obligor's country, will a court in your jurisdiction recognise that sale as being effective against the seller and other third parties (such as creditors or insolvency administrators of the seller) without the need to comply with your jurisdiction's own sale requirements?

Yes, subject to the considerations referred to in questions 2.3, 3.1, and 3.2. In particular, while a court may recognise the choice of law of the receivables purchase agreement, as discussed in question 2.3, a court will apply Canadian laws having overriding effect such as insolvency law. Accordingly, in an insolvency of the seller, in order for the sale to be recognised as effective against creditors or insolvency administrators of the seller, the sale may need to satisfy Canadian true sale requirements. In addition, the effectiveness of such sale against the obligor will be subject to the laws of the jurisdiction of the obligor.

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3.5 Example 4: If (a) the obligor is located in your jurisdiction but the seller is located in another country, (b) the receivable is governed by the law of the seller's country, (c) the seller and the purchaser choose the law of the seller's country to govern the receivables purchase agreement, and (d) the sale complies with the requirements of the seller's country, will a court in your jurisdiction recognise that sale as being effective against the obligor and other third parties (such as creditors or insolvency administrators of the obligor) without the need to comply with your jurisdiction's own sale requirements?

Yes, subject to the considerations referred to in questions 2.3, 3.1, 3.2 and 4.4.

3.6 Example 5: If (a) the seller is located in your jurisdiction (irrespective of the obligor's location), (b) the receivable is governed by the law of your jurisdiction, (c) the seller sells the receivable to a purchaser located in a third country, (d) the seller and the purchaser choose the law of the purchaser's country to govern the receivables purchase agreement, and (e) the sale complies with the requirements of the purchaser's country, will a court in your jurisdiction recognise that sale as being effective against the seller and other third parties (such as creditors or insolvency administrators of the seller, any obligor located in your jurisdiction and any third party creditor or insolvency administrator of any such obligor)?

Yes, subject to the same considerations referred to in question 3.4.

4 Asset Sales

4.1 Sale Methods Generally. In your jurisdiction what are the customary methods for a seller to sell receivables to a purchaser? What is the customary terminology – is it called a sale, transfer, assignment or something else?

The sale of receivables (other than lease receivables) is typically documented as an absolute assignment of the receivables and related security and is generally referred as a sale, transfer and/or absolute assignment. The receivables sold may consist of revolving or amortising pools of whole receivables or undivided interests in such receivables.

For "pay through" debt securities, the seller typically assigns the receivables as a single step transaction to a special purpose vehicle (SPV) under a purchase agreement. For "pass through" securities, the seller assigns the receivables to a custodian or an intermediary SPV which then issues securities in the form of certificates representing sales of undivided ownership interests in the pools of assets. This intermediate assignment is required chiefly to comply with securities legislation that requires a distinct issuer.

Lease receivables are generally transferred pursuant to a concurrent lease or sale-sale leaseback transaction because a sale of unaccrued lease receivables may create undesirable tax consequences. Lease securitisation transactions are also generally structured as two-step transactions in order to limit the risk that the original lessor may disclaim the lease in any insolvency proceeding. The first step of such transaction is the conveyance of the leased assets to a SPV which then concurrently leases the asset to the "purchaser".

4.2 Perfection Generally. What formalities are required generally for perfecting a sale of receivables? Are there any additional or other formalities required for the sale of receivables to be perfected against any subsequent good faith purchasers for value of the same receivables from the seller?

An absolute transfer of receivables is deemed to create a security interest, whether or not it secures an obligation. This must be perfected to be enforceable against third parties, usually by registering a financing statement under the applicable Personal Property Security Act (PPSA) in the common-law jurisdiction where the seller is deemed to be located for the purposes of the relevant PPSA (in all provinces except Ontario, the seller's chief executive office; in Ontario, the seller's location depends on its type – e.g., a corporation incorporated under provincial law is located in the relevant province). Failure to do so does not invalidate the sale, but the SPV's ownership interest both may become subject to competing claims of the seller's secured creditors and would be ineffective against an insolvency official.

An assignment of receivables payable in Quebec or subject to Quebec law must be perfected under Quebec law. Perfection by registration in the Quebec central registry is only possible if the receivables transferred constitute a "universality of claims" (that is, all of the receivables in a specified category). Otherwise notice must be given to each obligor, which is usually not practicable or desirable.

Where the receivables are evidenced by chattel paper (a document that evidences both a monetary obligation and the security interest that secures it), unless the purchaser takes possession of the chattel paper, another purchaser who does take possession of the chattel paper in the ordinary course of business without knowledge of the purchaser's interest could acquire the chattel paper free of the purchaser's interest.

4.3 Perfection for Promissory Notes, etc. What additional or different requirements for sale and perfection apply to sales of promissory notes, mortgage loans, consumer loans or marketable debt securities?

Promissory notes that constitute bills of exchange under the Bills of Exchange Act (Canada) are assigned by endorsement and physical delivery. Promissory notes that do not meet the requirements of the Bills of Exchange Act are regarded simply as evidence of the debt, assignments of which may be effected and perfected like any other receivable.

The PPSAs do not apply to transfers of interests in real property (such as mortgages), (although they do apply to assignments of mortgage receivables that do not transfer the real property interest). Transfers of mortgages must be registered on title to the land to be effective against third parties. Registrations are typically not made until enforcement (sale or foreclosure), under registrable powers of attorney delivered on closing. Unregistered beneficial assignments of mortgages can still be recognised as effective sales as between the parties.

Transfers of marketable debt securities are governed in most provinces by Securities Transfer Acts (STAs). Under the STAs directly held certificated securities are transferred by delivery of the certificate to the transferee together with an endorsement (on the certificate or on a separate stock transfer/power of attorney). Registration on the books of the issuer of the security is necessary for the security to be enforceable against the issuer. Securities held indirectly with securities intermediaries through the tiered holding

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system and immobilised in clearing agencies are acquired when the securities intermediary credits the transferee's account with the security, giving rise to a "security entitlement" to the security.

No additional requirements are required in connection with sales of consumer loans.

The PPSAs do not apply to a transfer of an interest or claim in or under any policy of insurance or annuity. Security over an insurance policy may require compliance with provincial insurance legislation, which for some types of insurance requires the policy owner to execute a collateral assignment and give notice to the insurer, which must be acknowledged. However, under the Civil Code of Québec ("Civil Code"), insurance policies can be charged by a hypothec. Priority over the insurance policy is established by notice to the insurer and priority is established by the date of registration of the hypothec. Furthermore, the insurer can be required to pay the proceeds of insurance directly to the secured party by notice to the insurer.

4.4 Obligor Notification or Consent. Must the seller or the purchaser notify obligors of the sale of receivables in order for the sale to be effective against the obligors and/or creditors of the seller? Must the seller or the purchaser obtain the obligors' consent to the sale of receivables in order for the sale to be an effective sale against the obligors? Whether or not notice is required to perfect a sale, are there any benefits to giving notice – such as cutting off obligor set-off rights and other obligor defences?

To effect a full legal assignment entitling the transferee to enforce the receivable against the obligor without joining the assignor, the transferor must give notice of the assignment to the obligor.

Under the PPSAs, notice to the obligor is not required for the security interest constituted by the assignment of a receivable to be effective against creditors of the seller provided the security interest is perfected by registration of a financing statement. However, the obligor for an assigned receivable is obligated to pay the receivable directly to the assignee/secured party only after receiving notice, reasonably identifying the relevant rights, that the receivable has been assigned. Except for certain consumer receivables, an agreement by the obligor cutting off defences as against an assignee is generally enforceable by a good faith assignee for value without notice. Absent such an agreement, the obligor under an assigned receivable may assert against the assignee any defences against the assignor arising under the underlying contract or a related contract and may set off any debts owing to the obligor payable before the obligor received notice of the assignment. Consent of the obligor is generally not required for the sale to be effective against the obligor, but see discussion under questions 3.3 and 4.6.

Under the Civil Code, as described in question 4.2, if the assignment of receivables does not constitute a universality of claims, the assignment may only be opposable against creditors of the seller if notice is given to the respective obligors.

4.5 Notice Mechanics. If notice is to be delivered to obligors, whether at the time of sale or later, are there any requirements regarding the form the notice must take or how it must be delivered? Is there any time limit beyond which notice is ineffective – for example, can a notice of sale be delivered after the sale, and can notice be delivered after insolvency proceedings have commenced against the obligor or the seller? Does the notice apply only to specific receivables or can it apply to any and all (including future) receivables? Are there any other limitations or considerations?

There are no specific requirements regarding the form of notice given to obligors or how it must be delivered. The notice must be sufficient to reasonably identify the rights being assigned and, if requested by the obligor, further proof must be provided within a reasonable time that the assignment has been made. There is no specific time limit.

4.6 Restrictions on Assignment – General Interpretation. Will a restriction in a receivables contract to the effect that "None of the [seller's] rights or obligations under this Agreement may be transferred or assigned without the consent of the [obligor]" be interpreted as prohibiting a transfer of receivables by the seller to the purchaser? Is the result the same if the restriction says "This Agreement may not be transferred or assigned by the [seller] without the consent of the [obligor]" (i.e., the restriction does not refer to rights or obligations)? Is the result the same if the restriction says "The obligations of the [seller] under this Agreement may not be transferred or assigned by the [seller] without the consent of the [obligor]" (i.e., the restriction does not refer to rights)?

A restriction on the assignment of the seller's rights under an agreement giving rise to receivables without the consent of the obligor will generally be interpreted as prohibiting a transfer of the underlying receivables without such consent. A restriction on the transfer or assignment of the underlying agreement without such consent will generally be interpreted the same way, since an assignment of an agreement is usually understood to include an assignment of rights. However, a restriction on assignment that refers only to the seller's obligations would not be interpreted as prohibiting a transfer of receivables, which are rights to receive payment under the agreement.

4.7 Restrictions on Assignment; Liability to Obligor. If any of the restrictions in question 4.6 are binding, or if the receivables contract explicitly prohibits an assignment of receivables or "seller's rights" under the receivables contract, are such restrictions generally enforceable in your jurisdiction? Are there exceptions to this rule (e.g., for contracts between commercial entities)? If your jurisdiction recognises restrictions on sale or assignment of receivables and the seller nevertheless sells receivables to the purchaser, will either the seller or the purchaser be liable to the obligor for breach of contract or tort, or on any other basis?

Under most PPSAs, terms in a contract that prohibit or restrict the assignment of or granting of a security interest in receivables arising thereunder are unenforceable against third parties. However, these saving provisions only apply to assignments of whole receivables, not to undivided or partial interests. There are no similar saving

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provisions under the Civil Code. In addition, the seller may still be subject to a claim for breach of its contract with the obligor.

The effect on a purported assignment of a contract in breach of a negative covenant prohibiting assignment without the consent of the obligor (either subject to the Civil Code or not covered by the PPSA saving provision) is unclear. However, one view is that such an assignment would be invalid and unenforceable. As a result, such an assignment might not constitute a true sale that would be effective against an insolvency official. Therefore, receivables subject to restrictions on assignment are often excluded as ineligible.

4.8 Identification. Must the sale document specifically identify each of the receivables to be sold? If so, what specific information is required (e.g., obligor name, invoice number, invoice date, payment date, etc.)? Do the receivables being sold have to share objective characteristics? Alternatively, if the seller sells *all* of its receivables to the purchaser, is this sufficient identification of receivables? Finally, if the seller sells *all* of its receivables *other than* receivables owing by one or more specifically identified obligors, is this sufficient identification of receivables?

In order to constitute a true sale, among other criteria, the receivables being sold must be sufficiently described so that they can be accurately identified as having been sold. However, the sale document does not need to specifically identify each receivable so long as there is some mechanism for identifying which receivables or interests therein have been sold. In addition, although not a sale requirement, for the sale to constitute a "universality" under the Civil Code, the receivables must be identified by category or type (including "all" receivables) to be opposable to third parties. While a transfer of all receivables other than certain specified receivables may be sufficient for sale purposes, it may not constitute a "universality" unless the excluded receivables are identified by objective criteria sufficient to be accurately identified by a third party without additional information.

4.9 Recharacterisation Risk. If the parties describe their transaction in the relevant documents as an outright sale and explicitly state their intention that it be treated as an outright sale, will this description and statement of intent automatically be respected or is there a risk that the transaction could be characterised by a court as a loan with (or without) security? If recharacterisation risk exists, what characteristics of the transaction might prevent the transfer from being treated as an outright sale? Among other things, to what extent may the seller retain any of the following without jeopardising treatment as an outright sale: (a) credit risk; (b) interest rate risk; (c) control of collections of receivables; (d) a right of repurchase/redemption; (e) a right to the residual profits within the purchaser; or (f) any other term?

Courts generally respect the intention of the parties to effect a legal sale as evidenced by the language used in the relevant documents and other communications, even where the economic substance of the transaction may resemble a secured loan. However, a statement of such an intention is not necessarily dispositive; the following additional factors will also be taken into account in determining whether a transaction constitutes a true sale:

- Whether the ownership/collection risk passes to the purchaser and recourse to the seller is limited: full recourse to the seller for "collectability" of the receivables is permitted, but not "economic recourse" whereby the seller agrees to pay the purchaser a specified rate of return regardless of whether the receivables are collected.
- Whether the transferred assets can be identified and the purchase price calculated at any time.
- Whether the right to retain surplus collections passes to the purchaser.
- Seller's rights to repurchase the receivables: the seller cannot retain an unlimited right to redeem or repurchase the receivables.
- Whether responsibility for collection of the receivables passes to the purchaser: although servicing and collection of the receivables by the purchaser would support a true sale, it is not determinative, and sellers commonly retain servicing rights.

4.10 Continuous Sales of Receivables. Can the seller agree in an enforceable manner to continuous sales of receivables (i.e., sales of receivables as and when they arise)? Would such an agreement survive and continue to transfer receivables to the purchaser following the seller's insolvency?

A seller can agree to continuous sales of receivables. However, with respect to sales arising following the seller's insolvency, see questions 6.1, 6.2, 6.3 and 6.5 below.

4.11 Future Receivables. Can the seller commit in an enforceable manner to sell receivables to the purchaser that come into existence after the date of the receivables purchase agreement (e.g., "future flow" securitisation)? If so, how must the sale of future receivables be structured to be valid and enforceable? Is there a distinction between future receivables that arise prior to *versus* after the seller's insolvency?

Yes, generally a seller may sell all present and future receivables. The sale should be structured as a present sale of all present and future receivables (or an undivided interest in them) as opposed to a future sale of new receivables. The terms of the sale related to the future receivables must also be sufficiently certain to satisfy requirements for enforceability and true sale. With respect to receivables that arise after the seller's insolvency, see questions 6.1, 6.2, 6.3 and 6.5 below.

4.12 Related Security. Must any additional formalities be fulfilled in order for the related security to be transferred concurrently with the sale of receivables? If not all related security can be enforceably transferred, what methods are customarily adopted to provide the purchaser the benefits of such related security?

Security interests securing transferred receivables (i.e. liens against vehicles) may be assigned to the purchaser along with the related receivables, provided that such security is expressly included in the transferred assets. Perfection of the security interest constituted by an assignment of receivables does not apply to assignments of the related intangible security as such (unless incorporated in chattel paper). A financing change statement may be registered to record the assignment of the underlying security interest to the purchaser. However, such registrations are not mandatory and are usually not done where large numbers of liens are involved.

As noted in question 4.3, the PPSAs do not apply to transfers of real property interests.

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Under the Civil Code, the transfer of most leases and conditional sale agreements must be registered:

- If the lien is a lease or conditional sale, reference to the underlying lien can be made in the registration of the assignment of the receivables.
- If the lien is a hypothec, registration is required and a copy of the certified statement of registration must be provided to the account debtors.

If these formalities are not satisfied, the assignment is not perfected against a subsequent assignee who has complied with them. However, the insolvency official is not a subsequent assignee for these purposes.

4.13 Set-Off; Liability to Obligor. Assuming that a receivables contract does not contain a provision whereby the obligor waives its right to set-off against amounts it owes to the seller, do the obligor's set-off rights terminate upon its receipt of notice of a sale? At any other time? If a receivables contract does not waive set-off but the obligor's set-off rights are terminated due to notice or some other action, will either the seller or the purchaser be liable to the obligor for damages caused by such termination?

As noted in question 4.4, an obligor's set-off rights with respect to obligations owing to it by the assignor of a receivable generally terminate when the obligor receives notice of the assignment, unless these rights are terms of the underlying contract. The assigned receivable will continue to be subject to the terms of the underlying contract (including contractual set-off) and any defences or claims arising therefrom or a closely connected contract and any other defences or claims, unless the obligor has made an enforceable agreement not to assert such defences. The seller may be liable for damages caused by the termination if the contract prohibited such assignment.

4.14 Profit Extraction. What methods are typically used in your jurisdiction to extract residual profits from the purchaser?

In Canada, profit extraction typically is structured as (i) payment of deferred compensation from excess spread by way of a deferred purchase price or release of cash reserves, and (ii) subordinated tranches or co-ownership interests. It is generally uncommon to charge servicing fees for profit extraction due as such fees generally attract GST/HST.

5 Security Issues

5.1 Back-up Security. Is it customary in your jurisdiction to take a "back-up" security interest over the seller's ownership interest in the receivables and the related security, in the event that an outright sale is deemed by a court (for whatever reason) not to have occurred and have been perfected (see question 4.9 above)?

No. If the sale is recharacterised as a security interest, the sale document should constitute the security agreement and perfection of the assignment under the PPSA will suffice.

5.2 Seller Security. If it is customary to take back-up security, what are the formalities for the seller granting a security interest in receivables and related security under the laws of your jurisdiction, and for such security interest to be perfected?

This is not applicable in Canada.

5.3 Purchaser Security. If the purchaser grants security over all of its assets (including purchased receivables) in favour of the providers of its funding, what formalities must the purchaser comply with in your jurisdiction to grant and perfect a security interest in purchased receivables governed by the laws of your jurisdiction and the related security?

In the common law provinces, a purchaser would typically grant security over all its present and after-acquired personal property in a general security agreement, which would include receivables. The provider of funding would perfect its security interest by registering a financing statement under the applicable PPSA filing regime, as determined by the PPSA conflict of laws rules.

In Quebec, a hypothec may be granted by a purchaser to secure any obligation, and may create a charge on movable (personal) or immovable (real) property. Registration of the hypothec in the public registry provided for under the Civil Code is required to render the hypothec opposable (enforceable) against third parties.

5.4 Recognition. If the purchaser grants a security interest in receivables governed by the laws of your jurisdiction, and that security interest is valid and perfected under the laws of the purchaser's jurisdiction, will the security be treated as valid and perfected in your jurisdiction or must additional steps be taken in your jurisdiction?

Under the conflict of law provisions of the PPSAs, the validity, perfection and priority of a security interest in receivables is generally governed by law of the jurisdiction where the debtor granting the security interest (in this case, the purchaser) is deemed to be located (see question 4.2 above). Accordingly, if under the laws of the jurisdiction in which the purchaser is located the security interest is valid and perfected, it will be likewise regarded in Canada.

Under the conflicts of laws provisions of the Civil Code, the validity of a hypothec charging receivables is governed by the law of the domicile of the grantor (in this case, the purchaser) at the time of the grant of such hypothec, while perfection is governed by the grantor's current domicile. For a legal person, the domicile corresponds to the head office.

5.5 Additional Formalities. What additional or different requirements apply to security interests in or connected to insurance policies, promissory notes, mortgage loans, consumer loans or marketable debt securities?

Subject to the requirements discussed in question 4.3, there are no additional requirements in connection with taking security over promissory notes, consumer loans or marketable debt securities.

For insurance policies, see question 4.3 above.

As noted in question 4.3 the PPSAs do not apply to transfers of interests in real property. Separate technical provisions in each province apply to taking security over real property.

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5.6 Trusts. Does your jurisdiction recognise trusts? If not, is there a mechanism whereby collections received by the seller in respect of sold receivables can be held or be deemed to be held separate and apart from the seller's own assets (so that they are not part of the seller's insolvency estate) until turned over to the purchaser?

Trusts validly constituted under their jurisdiction of establishment are generally recognised.

5.7 Bank Accounts. Does your jurisdiction recognise escrow accounts? Can security be taken over a bank account located in your jurisdiction? If so, what is the typical method? Would courts in your jurisdiction recognise a foreign law grant of security (for example, an English law debenture) taken over a bank account located in your jurisdiction?

Yes, provincial law recognises escrow accounts, subject to the terms of the applicable escrow account agreement.

The PPSAs and the Civil Code permit a lender to take security over deposit accounts. Deposits in bank accounts are treated as receivables owed by or claims against the depository bank. Security over bank accounts is typically granted by a security agreement under the PPSAs and by way of a hypothec under the Civil Code. Security over deposit accounts can be perfected by registering a PPSA financing statement (or its equivalent under the Civil Code) in the province in which the debtor is deemed to be located.

In addition, the Civil Code permits a secured party to perfect a hypothec in deposit accounts by control. Where the creditor is also the account bank, the creditor obtains control by the account holder consenting to the 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.

Courts would recognise a foreign law grant of security provided that it satisfies the requirements for creation of a security under the PPSA or Civil Code, as applicable.

5.8 Enforcement over Bank Accounts. If security over a bank account is possible and the secured party enforces that security, does the secured party control all cash flowing into the bank account from enforcement forward until the secured party is repaid in full, or are there limitations? If there are limitations, what are they?

Subject to the terms of the applicable security documents or blocked account agreement, on default by the debtor, the secured party has the right to direct the depository bank to transfer or sweep funds from the bank account to the secured party to satisfy the obligations secured.

5.9 Use of Cash Bank Accounts. If security over a bank account is possible, can the owner of the account have access to the funds in the account prior to enforcement without affecting the security?

Yes; however, if the account is subject to a blocked account agreement, rights of access may be limited even prior to enforcement.

6 Insolvency Laws

6.1 Stay of Action. If, after a sale of receivables that is otherwise perfected, the seller becomes subject to an insolvency proceeding, will your jurisdiction's insolvency laws automatically prohibit the purchaser from collecting, transferring or otherwise exercising ownership rights over the purchased receivables (a "stay of action")? If so, what generally is the length of that stay of action? Does the insolvency official have the ability to stay collection and enforcement actions until he determines that the sale is perfected? Would the answer be different if the purchaser is deemed to only be a secured party rather than the owner of the receivables?

Provided that the receivables were validly and effectively sold to the purchaser, an insolvency stay of proceedings against the seller will not prohibit the purchaser from exercising transfer and ownership rights over collected receivables. To the extent that the receivables have not been collected at the time the stay comes into effect: (i) the enforcement of the purchaser's rights to such payment may be stayed until the insolvency official or the court confirms that the sale is a valid transfer of the receivables; (ii) costs associated with collection of the receivables may be charged against the amounts collected; (iii) the terms of the stay may preclude the purchaser from notifying the relevant obligors of the sale until validity of the sale has been determined; and (iv) where the seller and/or creditors of the seller contest the validity of the sale (or otherwise asserting a claim to those receivables), the purchaser may be required to commence proceedings against the seller or third parties. In addition, if collected receivables become commingled with the other assets of the seller, such that they are not identifiable as the property of the purchaser, the purchaser may not be successful in reclaiming its property by way of a trust or proprietary claim made in the insolvency proceeding.

If the purchaser is deemed to only be a secured party rather than an owner of the receivables, then the stay of proceedings would generally prohibit the purchaser from taking any collection and/or enforcement action. The stay typically lasts for the whole of the proceeding. Large company reorganisation proceedings can take, on average, six to 18 months to complete. Liquidation proceedings have shorter timelines.

6.2 Insolvency Official's Powers. If there is no stay of action, under what circumstances, if any, does the insolvency official have the power to prohibit the purchaser's exercise of its ownership rights over the receivables (by means of injunction, stay order or other action)?

An insolvency official has authority to seek an order of the court prohibiting a purchaser's exercise of its ownership rights where there is a credible dispute as to the validity of the sale of receivables or the validity of the purchaser's security over such receivables. The court has jurisdiction to grant any order it deems appropriate including an injunction, stay or order resolving the dispute.

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6.3 Suspect Period (Clawback). Under what facts or circumstances could the insolvency official rescind or reverse transactions that took place during a "suspect" or "preference" period before the commencement of the seller's insolvency proceedings? What are the lengths of the "suspect" or "preference" periods in your jurisdiction for (a) transactions between unrelated parties, and (b) transactions between related parties? If the purchaser is majority-owned or controlled by the seller or an affiliate of the seller, does that render sales by the seller to the purchaser "related party transactions" for purposes of determining the length of the suspect period? If a parent company of the seller guarantee's the performance by the seller of its obligations under contracts with the purchaser, does that render sales by the seller to the purchaser "related party transactions" for purposes of determining the length of the suspect period?

Insolvency officials (and in some cases, creditors) have the power to set aside transactions that confer a preference on the debtor/seller's creditors or that constitute a transfer of property or services for no consideration (or consideration conspicuously less than fair market value). The review period under federal legislation is as follows: (i) preferences – three months (unrelated parties) and 12 months (related parties) from the commencement of the insolvency proceeding; and (ii) transfers at undervalue – 12 months (unrelated parties), one year (related parties) and five years (related parties, where the debtor was insolvent at the time of transfer) from the commencement of the insolvency proceeding. Various provincial statutes also provide remedies for preferences and fraudulent transactions. Provincial look-back periods are typically two to six years. Parties under majority ownership or control will generally be considered to be related parties. Whether a parent guarantee would render a sale to a purchaser to be a related party transaction will depend upon whether the parent and purchaser are related parties.

6.4 Substantive Consolidation. Under what facts or circumstances, if any, could the insolvency official consolidate the assets and liabilities of the purchaser with those of the seller or its affiliates in the insolvency proceeding? If the purchaser is owned by the seller or by an affiliate of the seller, does that affect the consolidation analysis?

Insolvency legislation contains no express authority for a court to grant a substantive consolidation order (except in limited circumstances not relevant hereto). However, a bankruptcy court has the inherent equitable jurisdiction to substantially consolidate the assets and liabilities of related entities in appropriate circumstances. Canadian law on the point is not settled and no clear and comprehensive test for the appropriateness of substantive consolidation has yet emerged. Orders for substantive consolidation in Canada have been rare. In those cases, courts have considered a number of factors including: (i) the financial and operational integration of the debtor entities; (ii) the degree to which the separate legal personalities of the debtor entities are respected; (iii) the balancing of economic prejudice to creditors resulting from consolidation *vs.* non-consolidation; (iv) whether consolidation would prevent a harm or confer a benefit on creditors generally; and (v) the administrative efficiencies of dealing with separate *versus* joint estates. Substantive consolidation is generally considered an extraordinary remedy and will rarely be made over the objections of prejudiced creditors. Whether the purchaser is owned by the seller (or an affiliate) will be a relevant factor in the above analysis.

6.5 Effect of Insolvency on Receivables Sales. If insolvency proceedings are commenced against the seller in your jurisdiction, what effect do those proceedings have on (a) sales of receivables that would otherwise occur after the commencement of such proceedings, or (b) on sales of receivables that only come into existence after the commencement of such proceedings?

Insolvency proceedings provide for two general categories of proceeding: reorganisation proceedings; and liquidation proceedings. Reorganisation proceedings are primarily debtor driven processes, where the debtor continues to conduct its business under the supervision of the court and an insolvency official. Liquidation proceedings are primarily creditor-driven and are characterised by the replacement of a debtor's management with an insolvency official for the purposes of liquidating the debtor's business. In reorganisation proceedings, a seller/debtor would typically have the authority to continue to perform contracts in the ordinary course, including a receivables purchase agreement for existing and future receivables. Performance under the contract may be stayed if the agreement is characterised by the court as creating a security interest in receivables, rather than a proprietary interest. The seller/debtor may also terminate the purchase agreement (if it is an executory contract), with the consent of the insolvency official or the court. In the event of termination, the purchaser may assert a damage claim in the proceeding. Finally, the seller/debtor may also assign the sales contract (if it is an executory contract) to a third party with the consent of the purchaser or by court order.

In liquidation proceedings, the seller/debtor typically ceases to perform its contracts and the purchaser may treat the contract as terminated. However, if the insolvency official continues to operate the business in order to preserve going-concern value, it may be authorised to assign the sale contract to a third party. In general, the insolvency official may terminate contracts (or cease to perform them) in a liquidation proceeding.

6.6 Effect of Limited Recourse Provisions. If a debtor's contract contains a limited recourse provision (see question 7.3 below), can the debtor nevertheless be declared insolvent on the grounds that it cannot pay its debts as they become due?

Where the purpose of the limited recourse provision is to shield parties from liability in their personal capacity (for example, a trustee or partner), then it is likely that a counterparty to the contract will be prohibited from pursuing an insolvency proceeding against such a party. The effect of such a limited recourse provision will be highly dependent on the wording of the provision.

7 Special Rules

7.1 Securitisation Law. Is there a special securitisation law (and/or special provisions in other laws) in your jurisdiction establishing a legal framework for securitisation transactions? If so, what are the basics? Is there a regulatory authority responsible for regulating securitisation transactions in your jurisdiction?

There is no specific legislative regime governing securitisations and no single regulatory authority has jurisdiction over securitisation transactions. Special legislation governs covered bonds secured by uninsured residential mortgages and issued by financial institutions

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registered with the Canada Mortgage and Housing Corporation. Various aspects of securitisation transactions may be subject to the common law and a variety of provincial and federal statutes, regulations and regulators, depending on the following:

- type of assets securitised (for example, consumer loans or government receivables);
- transaction parties (for example, federally regulated financial institutions);
- means by which the securities are offered to investors (for example, public offering or private placement); and
- location of the originator and the obligors.

General laws relevant to securitisation include the:

- PPSAs and Civil Code, as applicable;
- Bank Act (Canada) and the Office of the Superintendent of Financial Institutions (OSFI) guidelines;
- provincial securities legislation;
- federal insolvency legislation;
- provincial fraudulent conveyances and preferences legislation;
- provincial consumer protection legislation; and
- Financial Administration Act (Canada).

No single regulatory authority is responsible for regulating securitisation as such in Canada. However, as part of its supervisory function, OSFI is responsible for monitoring compliance by federally regulated financial institutions such as banks with certain prudential requirements set out in various OSFI guidelines and advisories relating to securitisations in which they may be involved as providers of liquidity or credit support or as sponsors or servicers. Adverse capital treatment may result from a failure to comply with such guidance. In addition, provincial securities regulators regulate offerings of the securities by way of prospectus or private placement, pursuant to which they have established additional disclosure requirements for securitised products.

7.2 Securitisation Entities. Does your jurisdiction have laws specifically providing for establishment of special purpose entities for securitisation? If so, what does the law provide as to: (a) requirements for establishment and management of such an entity; (b) legal attributes and benefits of the entity; and (c) any specific requirements as to the status of directors or shareholders?

No. Historically, SPVs have been structured as trusts because it is a flexible organisational form and is not subject to federal or provincial capital taxes. However, provincial capital taxes have largely been eliminated.

No specific statute governs the establishment of trusts. The requirements and attributes of a trust are generally determined under common law. A trust is not a separate legal entity, but is a relationship that arises when a person (the trustee) agrees to hold property for the benefit of other persons (the beneficiaries). The creator of the trust (either by a declaration of trust or a trust agreement) establishes the SPV.

An institutional trustee is generally appointed to carry out the activities of the trust and hold title to the trust property. The beneficiary is usually a charitable or non-taxable institution which does not retain the power to dissolve or wind up the trust. There are no regulatory requirements related to the creation of a trust (except for legislation requiring registration of business names) and there are no directors or shareholders of the trust.

A trust pays income tax at the highest marginal rate on its income, so cash flows are structured to match expenses (including interest payable to investors, deferred purchase price payable to the originator and trust expenses).

SPVs can also take the form of corporations or limited partnerships.

7.3 Location and form of Securitisation Entities. Is it typical to establish the special purpose entity in your jurisdiction or offshore? If in your jurisdiction, what are the advantages to locating the special purpose entity in your jurisdiction? If offshore, where are special purpose entities typically located for securitisations in your jurisdiction? What are the forms that the special purpose entity would normally take in your jurisdiction and how would such entity usually be owned?

Typically the SPV will be established in Canada. The advantages of locating the SPV in Canada are the familiarity that investors, underwriters and other counterparties have with domestic entities and a greater degree of certainty with respect to legal and tax consequences. For historical reasons relating to capital tax legislation which has largely been repealed, SPVs have typically been structured as common law trusts, but they can also take the form of limited partnerships or business corporations. The business trusts used as SPVs typically do not have "owners" in the conventional sense. Although technically the beneficial interest of the trust property is owned by the beneficiaries, those beneficiaries are typically not-for-profit entities that have little or no power over the administration of the trust and indeed may not even be aware of their status. If the SPV is a limited partnership or business corporation, the shares of the general partner or corporation may be owned by an affiliate of the seller but care must be taken to ensure that the assets of the SPV are not consolidated onto the balance sheet of the seller.

7.4 Limited-Recourse Clause. Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) limiting the recourse of parties to that agreement to the available assets of the relevant debtor, and providing that to the extent of any shortfall the debt of the relevant debtor is extinguished?

Yes, if the contract is governed by the laws of a Canadian province. If the agreement is governed by the laws of a foreign jurisdiction, the enforceability of such a limitation on recourse will depend on the laws of that jurisdiction, to the extent recognised and applied by the Canadian court and subject to the considerations in question 2.3.

7.5 Non-Petition Clause. Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) prohibiting the parties from: (a) taking legal action against the purchaser or another person; or (b) commencing an insolvency proceeding against the purchaser or another person?

Non-petition clauses have received very limited judicial consideration. Based on general contract law, a court would likely give effect to such provision, subject to any defences to enforceability of the contract (such as duress, mistake, etc.) and provided that the provision is otherwise enforceable under contract law.

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There is some older judicial authority for the proposition that a provision that prohibits a creditor from commencing insolvency proceedings is not enforceable as it contravenes bankruptcy laws. However, in our view, a court is not likely to follow that line of cases.

7.6 Priority of Payments "Waterfall". Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) distributing payments to parties in a certain order specified in the contract?

Yes, subject to any defences to enforceability of the contract and provided that the provision is otherwise enforceable under contract law.

7.7 Independent Director. Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) or a provision in a party's organisational documents prohibiting the directors from taking specified actions (including commencing an insolvency proceeding) without the affirmative vote of an independent director?

As fiduciaries, Canadian corporate directors may not fetter their discretion by agreeing in advance not to take certain actions. However, a court will generally give effect to such a provision in the corporation's organisational documents (which would include a unanimous shareholder agreement stripping the directors of their powers and transferring them to the shareholders). If a party fails to comply with such a provision, it does not affect the validity of the transaction but will merely give rise to a potential claim for breach of contract or a shareholder remedy.

7.8 Location of Purchaser. Is it typical to establish the purchaser in your jurisdiction or offshore? If in your jurisdiction, what are the advantages to locating the purchaser in your jurisdiction? If offshore, where are purchasers typically located for securitisations in your jurisdiction?

Purchasers are located both domestically and offshore; however, transactions with offshore purchasers may be subject to withholding taxes for certain asset classes (see question 9.1).

8 Regulatory Issues

8.1 Required Authorisations, etc. Assuming that the purchaser does no other business in your jurisdiction, will its purchase and ownership or its collection and enforcement of receivables result in its being required to qualify to do business or to obtain any licence or its being subject to regulation as a financial institution in your jurisdiction? Does the answer to the preceding question change if the purchaser does business with more than one seller in your jurisdiction?

There are no general restrictions on ownership or collection and enforcement of receivables by foreign persons; however, under the Bank Act 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 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 providing financing to a Canadian person as long as the nature and extent of its activities in Canada do not amount to engaging in or carrying on business in Canada.

The Bank Act itself does not provide guidance on the factors that OSFI may take into account in determining whether a foreign bank is engaging in or carrying on business in Canada. However, OSFI has cited the following factors as relevant in the past:

1. where the elements leading to formation of the agreements take place (i.e. location of negotiation and the decision to enter);
2. location of execution and delivery;
3. where operations are carried out;
4. where services are delivered and paid for;
5. where services are marketed; and
6. the relationship between activities that are carried on inside and outside Canada.

Such a determination is a weighing exercise, with no single factor necessarily tipping the balance. The more *indicia* pointing to a Canadian nexus, the greater the likelihood of an adverse finding.

In addition, a foreign corporation 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, factors similar 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.

8.2 Servicing. Does the seller require any licences, etc., in order to continue to enforce and collect receivables following their sale to the purchaser, including to appear before a court? Does a third-party replacement servicer require any licences, etc., in order to enforce and collect sold receivables?

Subject to question 8.1, generally a seller does not require a licence to continue to enforce and collect receivables so long as the account debtor is not notified of the sale; however, a third-party servicer will generally be required to be licensed as a collection agency under applicable provincial legislation to collect debts from an obligor on behalf of another person, unless it falls into a class exempt from such requirements, such as banks and mortgage brokers. Failure to register typically constitutes a provincial offence rendering the offender subject to fines or imprisonment. Amendments to some provincial collection agency legislation are pending that will exempt most securitisation sales from these requirements.

8.3 Data Protection. Does your jurisdiction have laws restricting the use or dissemination of data about or provided by obligors? If so, do these laws apply only to consumer obligors or also to enterprises?

The Personal Information Protection and Electronic Documents Act (Canada) (PIPEDA) regulates the collection, use and disclosure

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of personal information in the course of commercial transactions. Such protections generally apply to public and private information about identifiable individuals (as opposed to commercial entities). In addition, certain provinces have adopted comprehensive and/or industry specific privacy legislation, though in contrast the application of provincial legislation is not generally limited to commercial transactions. In those provinces which have adopted privacy legislation substantially similar to PIPEDA, the federal legislation does not apply other than with respect to areas and industries of federal jurisdiction.

8.4 Consumer Protection. If the obligors are consumers, will the purchaser (including a bank acting as purchaser) be required to comply with any consumer protection law of your jurisdiction? Briefly, what is required?

Purchasers will generally be required to comply with provincial and/or federal consumer protection legislation. Federally regulated financial institutions (e.g. banks) will be required to comply with the consumer protection provisions of federal legislation related to financial institutions, including matters related to credit cards and fees. As a result of a 2014 landmark decision of the Supreme Court of Canada, certain provincial consumer protection legislation may also apply to federally regulated institutions.

8.5 Currency Restrictions. Does your jurisdiction have laws restricting the exchange of your jurisdiction's currency for other currencies or the making of payments in your jurisdiction's currency to persons outside the country?

No; however, payments may be subject to anti-money laundering and terrorist financing legislation.

8.6 Risk Retention. Does your jurisdiction have laws or regulations relating to "risk retention"? How are securitisation transactions in your jurisdiction usually structured to satisfy those risk retention requirements?

Unlike the U.S., at present no jurisdiction in Canada has adopted rules, legislation or administrative policies requiring a sponsor or seller to retain any degree of risk in a securitisation transaction.

8.7 Regulatory Developments. Have there been any regulatory developments in your jurisdiction which are likely to have a material impact on securitisation transactions in your jurisdiction?

The implementation in Canada of new Basel III capital adequacy requirements for federally regulated financial institutions may impact investment by such institutions in asset-backed securities.

In addition, recent legislative changes to legislation governing mortgages insured by the federally-owned and guaranteed Canada Mortgage and Housing Corporation (CMHC) in effect provide that no loans insured by CMHC may be included in any securitisation program, except CMHC-sponsored programs after December 31, 2021, subject to certain transitional provisions. These changes will likely affect the composition and size of securitised mortgage pools and adversely impact the ability of mortgage lenders to fund orginations through securitisation.

Finally, some important regulatory changes relating to reporting certain trades in over-the-counter derivatives may have an impact on securitisations that make use of these instruments. In response to an agreement among G20 countries in 2009 to increase the transparency and oversight of OTC derivatives markets, many provincial securities regulators have adopted regulations requiring mandatory reporting of certain derivatives and require that some be traded on registered platforms.

9 Taxation

9.1 Withholding Taxes. Will any part of payments on receivables by the obligors to the seller or the purchaser be subject to withholding taxes in your jurisdiction? Does the answer depend on the nature of the receivables, whether they bear interest, their term to maturity, or where the seller or the purchaser is located? In the case of a sale of trade receivables at a discount, is there a risk that the discount will be recharacterised in whole or in part as interest? In the case of a sale of trade receivables where a portion of the purchase price is payable upon collection of the receivable, is there a risk that the deferred purchase price will be recharacterised in whole or in part as interest? If withholding taxes might apply, what are the typical methods for eliminating or reducing withholding taxes?

Most conventional interest payments to arm's length non-residents are not subject to withholding tax under Canadian domestic tax law. Under the Canada–United States Income Tax Convention, conventional interest payments to related non-residents entitled to claim the benefit of the Treaty are exempt from withholding (other Canadian tax treaties generally reduce the withholding rate on such interest from 25 per cent to 10 per cent). For lease payments, royalties and other financial assets that are subject to withholding tax, transactions are typically structured by way of a transaction with a domestic purchaser and a cross-border loan or note with the non-resident funding party.

9.2 Seller Tax Accounting. Does your jurisdiction require that a specific accounting policy is adopted for tax purposes by the seller or purchaser in the context of a securitisation?

Canadian taxpayers must generally compute their income for income tax purposes in accordance with Canadian generally accepted accounting principles, subject to provisions of the Income Tax Act (Canada) which permit (or require) differing treatment. Special rules apply to "Financial Institutions" who hold and dispose of "specified debt obligations" (each as defined in the Income Tax Act).

9.3 Stamp Duty, etc. Does your jurisdiction impose stamp duty or other transfer or documentary taxes on sales of receivables?

Generally, no.

9.4 Value Added Taxes. Does your jurisdiction impose value added tax, sales tax or other similar taxes on sales of goods or services, on sales of receivables or on fees for collection agent services?

Sales of financial instruments (such as loans and receivables) are generally exempt from the federal goods and services tax/

Canada

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harmonised sales tax (GST/HST) and provincial sales taxes (PST). Sales of goods and services are generally subject to the GST/HST and, in the province of Quebec, PST. In those provinces which have a PST (other than Quebec) sales of most tangible goods (and some services) are subject to PST. Collection agent services are generally subject to GST/HST. To minimise such taxes, receivables are often sold on a fully serviced basis, such that such services are not considered to be a separate supply for GST/HST purposes. This technique generally only works if the originator provides the servicing.

9.5 Purchaser Liability. If the seller is required to pay value-added tax, stamp duty or other taxes upon the sale of receivables (or on the sale of goods or services that give rise to the receivables) and the seller does not pay, then will the taxing authority be able to make claims for the unpaid tax against the purchaser or against the sold receivables or collections?

Generally, GST/HST and PST are tax liabilities of the purchaser of the goods and services giving rise to the receivables, not the seller. However, the seller will typically have an obligation to collect and remit such taxes on behalf of the relevant tax authorities. For GST/HST purposes, where a receivable includes amounts payable on account of GST/HST in respect of the sale of goods or services giving rise to the receivable, the originator is deemed to have collected, at the time of assignment, the amount of GST/HST not previously paid, and any amounts collected after such time are deemed not to be on account of GST/HST, such that the purchaser should not be liable for the seller's unremitted GST/HST.

9.6 Doing Business. Assuming that the purchaser conducts no other business in your jurisdiction, would the purchaser's purchase of the receivables, its appointment of the seller as its servicer and collection agent, or its enforcement of the receivables against the obligors, make it liable to tax in your jurisdiction?

Generally, no.

9.7 Taxable Income. If a purchaser located in your jurisdiction receives debt relief as the result of a limited recourse clause (see question 7.3 above), is that debt relief liable to tax in your jurisdiction?

Debt relief received by a purchaser as a result of a limited recourse clause agreed to by the parties at the outset should not on its own give rise to any upfront tax consequences.

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Cayman Islands

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1 Receivables Contracts

1.1 Formalities. In order to create an enforceable debt obligation of the obligor to the seller: (a) is it necessary that the sales of goods or services are evidenced by a formal receivables contract; (b) are invoices alone sufficient; and (c) can a binding contract arise as a result of the behaviour of the parties?

A formal written contract is not necessary to create an enforceable debt obligation. However, such an obligation must be created as a matter of contract or deed. Contracts may be written, oral, or partly written and partly oral. An invoice alone may be sufficient to constitute a contract between the parties if it contains the required elements of a contract. The existence and terms of an oral contract may be evidenced by the conduct of the parties. Where enforceable obligations can be identified with sufficient certainty, a contract may be implied based on a course of conduct or dealings between the parties.

1.2 Consumer Protections. Do your jurisdiction's laws: (a) limit rates of interest on consumer credit, loans or other kinds of receivables; (b) provide a statutory right to interest on late payments; (c) permit consumers to cancel receivables for a specified period of time; or (d) provide other noteworthy rights to consumers with respect to receivables owing by them?

Given the relatively small size of the consumer market and the nature of the financial services industry, there are no statutes or regulations to limit rates of interest, provide a statutory right to interest on late payments or other consumer rights. All such obligations would be governed by the relevant contract, including any obligations to pay default interest (subject to such interest not being so high as to constitute a penalty).

1.3 Government Receivables. Where the receivables contract has been entered into with the government or a government agency, are there different requirements and laws that apply to the sale or collection of those receivables?

No, although sovereign immunity laws may cause enforcement issues.

2 Choice of Law – Receivables Contracts

2.1 No Law Specified. If the seller and the obligor do not specify a choice of law in their receivables contract, what are the main principles in your jurisdiction that will determine the governing law of the contract?

Neither the Rome Convention (80/934/EEC) "Rome Convention I" nor Regulation 593/2008/EC ("Rome Convention II") on the law applicable to contractual obligations have been extended to the Cayman Islands. Absent an express choice of law provision, the applicable law of a contract will be that of the country with which it has the closest connection in light of all the material circumstances. Cayman Islands law recognises the English common law doctrine of *forum non conveniens* and it is necessary to ensure that, in commencing proceedings, the Cayman Islands court is best placed to deal with the dispute, that it will be the venue most convenient for the particular matter to be resolved and that Cayman Islands law is that with which the contract has its closest and most real connection.

2.2 Base Case. If the seller and the obligor are both resident in your jurisdiction, and the transactions giving rise to the receivables and the payment of the receivables take place in your jurisdiction, and the seller and the obligor choose the law of your jurisdiction to govern the receivables contract, is there any reason why a court in your jurisdiction would not give effect to their choice of law?

No, there is not.

2.3 Freedom to Choose Foreign Law of Non-Resident Seller or Obligor. If the seller is resident in your jurisdiction but the obligor is not, or if the obligor is resident in your jurisdiction but the seller is not, and the seller and the obligor choose the foreign law of the obligor/seller to govern their receivables contract, will a court in your jurisdiction give effect to the choice of foreign law? Are there any limitations to the recognition of foreign law (such as public policy or mandatory principles of law) that would typically apply in commercial relationships such as that between the seller and the obligor under the receivables contract?

The courts of the Cayman Islands will observe and give effect to the choice of the foreign law as the governing law of the receivables contract. The submission by a Cayman Islands obligor or seller in a

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receivables contract to the laws of another jurisdiction will be legal, valid and binding on the Cayman Islands obligor/seller assuming that the same is true under the governing law of the contract. However, the courts of the Cayman Islands will not observe and give effect to a choice of the laws of a particular jurisdiction as the governing law of a document if to do so would be contrary to the public policy of the Cayman Islands.

3 Choice of Law – Receivables Purchase Agreement

3.1 Base Case. Does your jurisdiction's law generally require the sale of receivables to be governed by the same law as the law governing the receivables themselves? If so, does that general rule apply irrespective of which law governs the receivables (i.e., your jurisdiction's laws or foreign laws)?

No, it does not. As noted in question 2.1 above, the Rome Conventions I and II have not been extended to the Cayman Islands.

3.2 Example 1: If (a) the seller and the obligor are located in your jurisdiction, (b) the receivable is governed by the law of your jurisdiction, (c) the seller sells the receivable to a purchaser located in a third country, (d) the seller and the purchaser choose the law of your jurisdiction to govern the receivables purchase agreement, and (e) the sale complies with the requirements of your jurisdiction, will a court in your jurisdiction recognise that sale as being effective against the seller, the obligor and other third parties (such as creditors or insolvency administrators of the seller and the obligor)?

Yes, it will.

3.3 Example 2: Assuming that the facts are the same as Example 1, but either the obligor or the purchaser or both are located outside your jurisdiction, will a court in your jurisdiction recognise that sale as being effective against the seller and other third parties (such as creditors or insolvency administrators of the seller), or must the foreign law requirements of the obligor's country or the purchaser's country (or both) be taken into account?

Yes, it will.

3.4 Example 3: If (a) the seller is located in your jurisdiction but the obligor is located in another country, (b) the receivable is governed by the law of the obligor's country, (c) the seller sells the receivable to a purchaser located in a third country, (d) the seller and the purchaser choose the law of the obligor's country to govern the receivables purchase agreement, and (e) the sale complies with the requirements of the obligor's country, will a court in your jurisdiction recognise that sale as being effective against the seller and other third parties (such as creditors or insolvency administrators of the seller) without the need to comply with your jurisdiction's own sale requirements?

Yes, the courts of the Cayman Islands will give effect to the choice of the law of the obligor's country as the governing law of the receivables purchase agreement. The courts would only decline to exercise jurisdiction in certain exceptional circumstances.

3.5 Example 4: If (a) the obligor is located in your jurisdiction but the seller is located in another country, (b) the receivable is governed by the law of the seller's country, (c) the seller and the purchaser choose the law of the seller's country to govern the receivables purchase agreement, and (d) the sale complies with the requirements of the seller's country, will a court in your jurisdiction recognise that sale as being effective against the obligor and other third parties (such as creditors or insolvency administrators of the obligor) without the need to comply with your jurisdiction's own sale requirements?

Yes. See questions 3.1 and 3.4 above.

3.6 Example 5: If (a) the seller is located in your jurisdiction (irrespective of the obligor's location), (b) the receivable is governed by the law of your jurisdiction, (c) the seller sells the receivable to a purchaser located in a third country, (d) the seller and the purchaser choose the law of the purchaser's country to govern the receivables purchase agreement, and (e) the sale complies with the requirements of the purchaser's country, will a court in your jurisdiction recognise that sale as being effective against the seller and other third parties (such as creditors or insolvency administrators of the seller, any obligor located in your jurisdiction and any third party creditor or insolvency administrator of any such obligor)?

Yes. See questions 3.1 and 3.4 above.

4 Asset Sales

4.1 Sale Methods Generally. In your jurisdiction what are the customary methods for a seller to sell receivables to a purchaser? What is the customary terminology – is it called a sale, transfer, assignment or something else?

The most common method of transferring receivables is by way of assignment (either equitable or legal). Alternatives to assignment include a novation (transfer of both the rights and obligations under the contract), a declaration of trust over the receivables or over the proceeds of the receivables (coupled with a power of attorney), and sub-participation (essentially a limited recourse loan to the seller in return for the economic interest in the receivables). An outright sale of receivables may be described as a "sale" or "true sale", a "transfer" or an "assignment". It is not possible, as a technical legal matter, to "assign" obligations and therefore any "assignment" should, if obligations are to be transferred, include a "novation" of those obligations.

4.2 Perfection Generally. What formalities are required generally for perfecting a sale of receivables? Are there any additional or other formalities required for the sale of receivables to be perfected against any subsequent good faith purchasers for value of the same receivables from the seller?

An assignment can be either legal or equitable, depending on the circumstances. The key requirements of a legal assignment are that it must be an absolute assignment of the chosen receivables in action and the assignment must be in writing, signed by the assignor and,

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to perfect the legal assignment, it must be notified in writing to the obligor. If the sale of a receivable does not meet these requirements, it will take effect as an equitable assignment and any subsequent legal assignment to a good faith purchaser may trump the original assignment. A novation requires the written consent of the obligor as well as the transferor and transferee.

4.3 Perfection for Promissory Notes, etc. What additional or different requirements for sale and perfection apply to sales of promissory notes, mortgage loans, consumer loans or marketable debt securities?

The express terms of the underlying receivable must be considered and any conditions met and restrictions observed relating to the transfer and assignment of the receivable, including if consent is required of the obligor. The transfer requirements for promissory notes (as well as other negotiable instruments) are governed by the Bills of Exchange Law (1997 Revision) of the Cayman Islands, which provides that they are transferable by delivery (or delivery and endorsement). There are specific requirements and formalities in relation to the legal assignment of mortgages over real property in the Cayman Islands. Generally, notes and other debt securities issued by Cayman Islands issuers are typically governed by New York or English law. In relation to Cayman Islands law-governed debt securities, an instrument in bearer form would be transferable by delivery or delivery and endorsement, or if in registered form, the terms of the instrument will generally provide that the recording of the transfer on the note or securities register evidences the transfer.

4.4 Obligor Notification or Consent. Must the seller or the purchaser notify obligors of the sale of receivables in order for the sale to be effective against the obligors and/or creditors of the seller? Must the seller or the purchaser obtain the obligors' consent to the sale of receivables in order for the sale to be an effective sale against the obligors? Whether or not notice is required to perfect a sale, are there any benefits to giving notice – such as cutting off obligor set-off rights and other obligor defences?

See questions 4.2 and 4.3 above. In addition to the risk that a third-party purchaser for value who gives notice to an obligor might be able to "trump" an earlier equitable assignment, there is a risk the obligor may be able to set off claims against the assignor prior to receiving notice of the assignment.

4.5 Notice Mechanics. If notice is to be delivered to obligors, whether at the time of sale or later, are there any requirements regarding the form the notice must take or how it must be delivered? Is there any time limit beyond which notice is ineffective – for example, can a notice of sale be delivered after the sale, and can notice be delivered after insolvency proceedings have commenced against the obligor or the seller? Does the notice apply only to specific receivables or can it apply to any and all (including future) receivables? Are there any other limitations or considerations?

Notice of a legal assignment must be given in writing. There is no time limit and notice can be delivered after sale and after insolvency proceedings have commenced. However, until notice in writing is given, the assignment will only be an equitable assignment (see question 4.4 above for some adverse consequences of failure to give notice).

4.6 Restrictions on Assignment – General Interpretation. Will a restriction in a receivables contract to the effect that "None of the [seller's] rights or obligations under this Agreement may be transferred or assigned without the consent of the [obligor]" be interpreted as prohibiting a transfer of receivables by the seller to the purchaser? Is the result the same if the restriction says "This Agreement may not be transferred or assigned by the [seller] without the consent of the [obligor]" (i.e., the restriction does not refer to rights or obligations)? Is the result the same if the restriction says "The obligations of the [seller] under this Agreement may not be transferred or assigned by the [seller] without the consent of the [obligor]" (i.e., the restriction does not refer to rights)?

If a right (or the contract generally without specifying "rights and obligations") is expressed as strictly non-assignable by contract without the consent of the obligor, specific consent must be sought from the obligor. If that consent is not obtained, any purported assignment is not valid against the obligor. As noted in question 4.1, obligations must be novated and all parties, including the obligor, must be party to a novation agreement.

4.7 Restrictions on Assignment; Liability to Obligor. If any of the restrictions in question 4.6 are binding, or if the receivables contract explicitly prohibits an assignment of receivables or "seller's rights" under the receivables contract, are such restrictions generally enforceable in your jurisdiction? Are there exceptions to this rule (e.g., for contracts between commercial entities)? If your jurisdiction recognises restrictions on sale or assignment of receivables and the seller nevertheless sells receivables to the purchaser, will either the seller or the purchaser be liable to the obligor for breach of contract or tort, or on any other basis?

See question 4.6 above. Restrictions on assignment are generally enforceable under Cayman Islands law. There are certain limited situations where an assignment may occur by operation of law, e.g. transfer to a successor upon death of the holder of the receivable.

4.8 Identification. Must the sale document specifically identify each of the receivables to be sold? If so, what specific information is required (e.g., obligor name, invoice number, invoice date, payment date, etc.)? Do the receivables being sold have to share objective characteristics? Alternatively, if the seller sells *all* of its receivables to the purchaser, is this sufficient identification of receivables? Finally, if the seller sells *all* of its receivables *other than* receivables owing by one or more specifically identified obligors, is this sufficient identification of receivables?

The transfer document must sufficiently identify the receivable(s) to be sold and "all receivables of the seller other than" the transfer instrument must be sufficiently clear to distinguish the receivables included in the transfer from those which are not.

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4.9 Recharacterisation Risk. If the parties describe their transaction in the relevant documents as an outright sale and explicitly state their intention that it be treated as an outright sale, will this description and statement of intent automatically be respected or is there a risk that the transaction could be characterised by a court as a loan with (or without) security? If recharacterisation risk exists, what characteristics of the transaction might prevent the transfer from being treated as an outright sale? Among other things, to what extent may the seller retain any of the following without jeopardising treatment as an outright sale: (a) credit risk; (b) interest rate risk; (c) control of collections of receivables; (d) a right of repurchase/redemption; (e) a right to the residual profits within the purchaser; or (f) any other term?

Generally, in the Cayman Islands, the sale and purchase of receivables under Cayman Islands law will be treated as an absolute assignment and transfer. There are no Cayman Islands authorities on whether the sale and purchase of an asset may be recharacterised as a loan secured by such asset or as some other transaction or set aside as a sham. However, based on the principles discussed in the English authorities, which would be persuasive, assuming that (i) the transfer agreement contemplates the outright sale and the outright purchase of the receivable, and (ii) there is no indication that the intention of the parties is for the sale and purchase of the receivables to be treated as a transfer by way of security, then, absent anything else in the circumstances, it is unlikely to be recharacterised as such. Factors which a Cayman Islands court would likely consider are: (i) that the seller does not have the right to reacquire any of the receivables by repaying the price received on the sale; (ii) that there is no obligation on the buyer to account to the seller for any "profit" made on the realisation of the receivables; and (iii) the buyer has no specific right of recourse to the seller if a specific asset within the receivables realises an amount less than the price paid for it.

4.10 Continuous Sales of Receivables. Can the seller agree in an enforceable manner to continuous sales of receivables (i.e., sales of receivables as and when they arise)? Would such an agreement survive and continue to transfer receivables to the purchaser following the seller's insolvency?

Yes, an assignment can provide for receivables to be automatically assigned to the purchaser as and when they come into existence. See the answer to question 6.5 below on the effect of insolvency of the seller.

4.11 Future Receivables. Can the seller commit in an enforceable manner to sell receivables to the purchaser that come into existence after the date of the receivables purchase agreement (e.g., "future flow" securitisation)? If so, how must the sale of future receivables be structured to be valid and enforceable? Is there a distinction between future receivables that arise prior to *versus* after the seller's insolvency?

Yes, see questions 4.10 above and 6.4 below.

4.12 Related Security. Must any additional formalities be fulfilled in order for the related security to be transferred concurrently with the sale of receivables? If not all related security can be enforceably transferred, what methods are customarily adopted to provide the purchaser the benefits of such related security?

Security for a receivable can usually be assigned in the same manner as the receivable itself; however, there may be additional formalities such as registration and payment of a filing fee depending upon the nature of the receivable. For example, the assignment of a mortgage or real property located in the Cayman Islands requires registration of the transfer and payment of a fee.

4.13 Set-Off; Liability to Obligor. Assuming that a receivables contract does not contain a provision whereby the obligor waives its right to set-off against amounts it owes to the seller, do the obligor's set-off rights terminate upon its receipt of notice of a sale? At any other time? If a receivables contract does not waive set-off but the obligor's set-off rights are terminated due to notice or some other action, will either the seller or the purchaser be liable to the obligor for damages caused by such termination?

If the right to set off a cross-debt arises after the obligor has received notice of the assignment, the obligor will generally be unable, from that point, to set off such cross-debt against the seller. In the absence of a breach of any contrary provision, it is unlikely that either the seller or the purchaser would be liable to the obligor for damages as a result of any of the obligor's rights of set-off terminating.

4.14 Profit Extraction. What methods are typically used in your jurisdiction to extract residual profits from the purchaser?

There are a number of options available when structuring profit extraction which, as a purely legal matter, can be debt or equity. Profit participating notes or similar instruments are common or alternatively the use of preference shares that are structured to rank above ordinary shares of a company in respect of, among other things, the payment of dividends is a popular mechanism to achieve such profit extraction.

5 Security Issues

5.1 Back-up Security. Is it customary in your jurisdiction to take a "back-up" security interest over the seller's ownership interest in the receivables and the related security, in the event that an outright sale is deemed by a court (for whatever reason) not to have occurred and have been perfected (see question 4.9 above)?

No, it is not customary to take a "back-up" security interest over the receivables. Generally, true sale opinions with respect to the sale of receivables where the governing law of the sale agreement is Cayman Islands law are commonly given and no additional security interest is required.

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5.2 Seller Security. If it is customary to take back-up security, what are the formalities for the seller granting a security interest in receivables and related security under the laws of your jurisdiction, and for such security interest to be perfected?

This is not applicable.

5.3 Purchaser Security. If the purchaser grants security over all of its assets (including purchased receivables) in favour of the providers of its funding, what formalities must the purchaser comply with in your jurisdiction to grant and perfect a security interest in purchased receivables governed by the laws of your jurisdiction and the related security?

Formalities and perfection of such security interests will depend upon the nature of the underlying assets that are subject to the security interest (the "collateral") and the applicable law of such collateral.

Special regimes apply to the taking of security over certain assets, including ships, aircraft and land.

The applicable law for receivables (being in the nature of intangible movables) is not entirely free from doubt. One view is that the applicable law is the *lex situs*. The alternative view is that the applicable law is the governing law of the security. Our view, based on English authorities and authoritative legal commentaries, is that the *lex situs* would determine proprietary issues in the case of intangible movables. This view does, however, require a fictional "*situs*" to be attributed to intangibles.

In the case of collateral in the form of general intangibles and contract rights, the *lex situs* would be the law of the place in which the rights are properly recoverable or can be enforced. This will depend upon the facts and circumstances, but is usually where the obligor or debtor in respect of the relevant claim is located. The location of the obligor or debtor is not necessarily the place of its head office or registered office. For example, if the obligor or debtor incurs the relevant obligation through a branch, it is likely to be where the branch is located.

5.4 Recognition. If the purchaser grants a security interest in receivables governed by the laws of your jurisdiction, and that security interest is valid and perfected under the laws of the purchaser's jurisdiction, will the security be treated as valid and perfected in your jurisdiction or must additional steps be taken in your jurisdiction?

Yes. No additional steps would be required; however, see also our response to question 5.3 with regard to the applicable law for perfection purposes.

5.5 Additional Formalities. What additional or different requirements apply to security interests in or connected to insurance policies, promissory notes, mortgage loans, consumer loans or marketable debt securities?

There are no specific additional formalities with respect to the taking of a security interest in such assets.

5.6 Trusts. Does your jurisdiction recognise trusts? If not, is there a mechanism whereby collections received by the seller in respect of sold receivables can be held or be deemed to be held separate and apart from the seller's own assets (so that they are not part of the seller's insolvency estate) until turned over to the purchaser?

Yes, the Cayman Islands, being a jurisdiction largely based on English law, does recognise both express and constructive trusts in a manner very similar to English law.

5.7 Bank Accounts. Does your jurisdiction recognise escrow accounts? Can security be taken over a bank account located in your jurisdiction? If so, what is the typical method? Would courts in your jurisdiction recognise a foreign law grant of security (for example, an English law debenture) taken over a bank account located in your jurisdiction?

Yes, the Cayman Islands does recognise escrow accounts and security can be taken over a bank account. The security taken is normally in the form of an equitable assignment by way of security over the bank account.

Generally, a Cayman Islands court would recognise a foreign law grant of security over a Cayman Islands bank account on the assumption that such a grant is valid, binding and enforceable as a matter of the governing law of the security interest.

5.8 Enforcement over Bank Accounts. If security over a bank account is possible and the secured party enforces that security, does the secured party control all cash flowing into the bank account from enforcement forward until the secured party is repaid in full, or are there limitations? If there are limitations, what are they?

This is a matter to be determined by the terms of the security interest granted. There are no statutory provisions that would limit the ability of a secured party to be able to enforce or realise its security interest, provided of course, that such security interest is valid, binding and enforceable as a matter of the governing law of the security interest.

5.9 Use of Cash Bank Accounts. If security over a bank account is possible, can the owner of the account have access to the funds in the account prior to enforcement without affecting the security?

Yes, although such control may affect whether or not the security interest would be treated as a fixed or floating charge. This is a fairly complex area of law but, at the most basic level, if the owner of the account is able to access the funds without the secured party having any control over the ability of the account owner to move cash in and out of the account, then such security interest is likely to be a floating charge. In an insolvency of a Cayman company or exempted limited partnership, this would mean that such security interest would rank behind any preferred debts. In the context of a securitisation transaction, however, such preferred debts are minimal and the main issue that normally arises is a question of ranking in that a subsequent fixed charge ranks ahead of a floating charge.

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6 Insolvency Laws

6.1 Stay of Action. If, after a sale of receivables that is otherwise perfected, the seller becomes subject to an insolvency proceeding, will your jurisdiction's insolvency laws automatically prohibit the purchaser from collecting, transferring or otherwise exercising ownership rights over the purchased receivables (a "stay of action")? If so, what generally is the length of that stay of action? Does the insolvency official have the ability to stay collection and enforcement actions until he determines that the sale is perfected? Would the answer be different if the purchaser is deemed to only be a secured party rather than the owner of the receivables?

No. There are no provisions under Cayman Islands law that provide for any form of automatic stay of action either with respect to a sale of receivables or if a security interest is created.

6.2 Insolvency Official's Powers. If there is no stay of action, under what circumstances, if any, does the insolvency official have the power to prohibit the purchaser's exercise of its ownership rights over the receivables (by means of injunction, stay order or other action)?

With respect to companies, which are the type of entities that one normally encounters in the context of a securitisation transaction, a liquidator of such entities in the Cayman Islands has no statutory right to disclaim onerous contracts or "cherry pick". This provision would also apply to exempted limited partnerships and limited liability companies that are occasionally used in such transactions.

6.3 Suspect Period (Clawback). Under what facts or circumstances could the insolvency official rescind or reverse transactions that took place during a "suspect" or "preference" period before the commencement of the seller's insolvency proceedings? What are the lengths of the "suspect" or "preference" periods in your jurisdiction for (a) transactions between unrelated parties, and (b) transactions between related parties? If the purchaser is majority-owned or controlled by the seller or an affiliate of the seller, does that render sales by the seller to the purchaser "related party transactions" for purposes of determining the length of the suspect period? If a parent company of the seller guarantee's the performance by the seller of its obligations under contracts with the purchaser, does that render sales by the seller to the purchaser "related party transactions" for purposes of determining the length of the suspect period?

The following provisions and suspect periods are potentially applicable in the context of a potential clawback claim in a securitisation transaction.

Voidable preference under the Companies Law – the entry by a company, a limited liability company or exempted limited partnership into a transaction at any time within the six months immediately preceding the commencement of its winding up is, depending on the exact facts, theoretically capable of constituting a voidable preference if the pre-conditions for a voidable preference under Section 145(1) of the Companies Law were present. In accordance with Section 145(1), every conveyance or transfer of property or charge therein, every payment, every obligation and every judicial proceeding made, incurred, taken or suffered by any company, limited liability company or exempted limited partnership, which is unable to pay its debts as they become due from its own monies in favour of any creditor with a view to giving such creditor a preference over the other creditors, will be invalid if made, incurred, taken or suffered within the six months immediately preceding the commencement of a liquidation.

Transactions at an undervalue under the Companies Law – in accordance with Section 146(2) of the Companies Law, every disposition of property made at an undervalue by or on behalf of a company, limited liability company or exempted limited partnership with intent to defraud its creditors, shall be voidable at the instance of its official liquidator. The burden of establishing an intent to defraud for the purposes of Section 146(2) shall be upon the official liquidator. The suspect period is six years after the date of the relevant disposition.

Intention to defraud – if, in the course of the winding up of a company or a limited liability company, it appears that any business of the company or the limited liability company has been carried on with an intent to defraud creditors of the company or the limited liability company or creditors of any other person or for any fraudulent purpose, the liquidator may apply to the court for a declaration under Section 147(1) of the Companies Law. Section 147(1) also applies to exempted limited partnerships. There is no suspect period with respect to this provision.

The Fraudulent Dispositions Law (1996 Revision) may have the effect of making a transaction or a payment or transfer voidable (although it is not an insolvency-related provision as such, as it applies both pre- and post-insolvency). Under the Fraudulent Dispositions Law (1996 Revision), any disposition of property made with an intent to defraud (which means an intention to defeat wilfully an obligation owed to another creditor) and at an undervalue is voidable at the instance of the creditor thereby prejudiced. A creditor may only commence an action under this Law within six years of the relevant disposition.

6.4 Substantive Consolidation. Under what facts or circumstances, if any, could the insolvency official consolidate the assets and liabilities of the purchaser with those of the seller or its affiliates in the insolvency proceeding? If the purchaser is owned by the seller or by an affiliate of the seller, does that affect the consolidation analysis?

There is limited reported Cayman Islands authority on the circumstances in which a Cayman Islands court might ignore the separate legal personalities of a company and its shareholder in order to enable creditors of a shareholder of the company to proceed directly against the assets of the company as well as against those of the shareholder (which would include its shareholding in the company). Such authorities as do exist follow the principles established under English common law, which the Cayman Islands court generally regards as persuasive (but not technically binding).

As a matter of English common law, it is only in exceptional circumstances that the principle of the separate legal personality of a company can be ignored, such that the court will "pierce the corporate veil". Such circumstances may exist where a person is under an existing legal obligation or liability, or subject to an existing legal restriction which he deliberately evades or whose enforcement he deliberately frustrates by interposing a company under his control. In those circumstances, the court may then pierce the corporate veil for the purpose, and only for the purpose, of depriving the company or its controller of the advantage that they would otherwise have obtained by the company's separate legal personality.

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Outside of piercing the corporate veil, the English courts have considered other circumstances in which a company may be liable for the acts of its shareholder and *vice versa*. These include where the device of incorporation is used for some illegal or improper purpose, cases of fraud or sham, certain trustee-beneficiary relationships, in certain circumstances of void or voidable transactions, and where the company can be regarded as acting simply as the agent of its shareholder. There may also be other exceptional cases in which the corporate veil may be pierced pursuant to specific foreign statutory provisions.

However, these decisions are founded on the principle that the separate legal personality is being ignored for limited purposes to fix a shareholder with a liability or responsibility or subject it to a restriction (or, in certain circumstances, giving the shareholder remedies it would not otherwise have). We can find no principle, and we are of the view that a Cayman Islands court would not find, that the separate legal personality of the company should be ignored simply to enable a third-party creditor of a shareholder or other affiliate of the company to proceed directly against assets of the company to satisfy liabilities owed by the shareholder or such other affiliate to such creditor, provided that the company has been properly established and operated as a special purpose issuer in the context of a securitisation transaction.

6.5 Effect of Insolvency on Receivables Sales. If insolvency proceedings are commenced against the seller in your jurisdiction, what effect do those proceedings have on (a) sales of receivables that would otherwise occur after the commencement of such proceedings, or (b) on sales of receivables that only come into existence after the commencement of such proceedings?

Section 99 of the Companies Law provides, *inter alia*, that when a winding up order has been made in respect of a company, any disposition of the company's property after the commencement of the winding up is, unless the court otherwise orders, void. This provision also applies to exempted limited partnerships and to limited liability companies.

6.6 Effect of Limited Recourse Provisions. If a debtor's contract contains a limited recourse provision (see question 7.3 below), can the debtor nevertheless be declared insolvent on the grounds that it cannot pay its debts as they become due?

No, provided that limited recourse provision is valid, binding and enforceable as a matter of the governing law of the relevant contract, including that the debt is extinguished.

7 Special Rules

7.1 Securitisation Law. Is there a special securitisation law (and/or special provisions in other laws) in your jurisdiction establishing a legal framework for securitisation transactions? If so, what are the basics? Is there a regulatory authority responsible for regulating securitisation transactions in your jurisdiction?

There is no special securitisation law or related regulatory authority in the Cayman Islands due to the fact that the common law and general corporate statutes provide all the necessary legal structures and protections required for cross-border international securitisations.

7.2 Securitisation Entities. Does your jurisdiction have laws specifically providing for establishment of special purpose entities for securitisation? If so, what does the law provide as to: (a) requirements for establishment and management of such an entity; (b) legal attributes and benefits of the entity; and (c) any specific requirements as to the status of directors or shareholders?

There is no special securitisation entities law; however, there are certain provisions of the Companies Law that have been adapted to make Cayman companies more attractive to use as the special purpose issuers ("SPVs") in a securitisation transaction; for example, Section 95(2) (see question 7.5 below). The Cayman Islands is generally considered to be one of the leading jurisdictions for the formation of SPVs due to its creditor-friendly insolvency regime and flexible companies law specifically enhanced to assist in the provisions of clean legal opinions with respect to bankruptcy remoteness or "ring fencing" and the clear absence of any stay or moratorium on enforcement of security interests.

The Cayman Islands has enacted the Limited Liability Companies Law, 2016 which allows for the formation of a new Cayman Islands vehicle: the limited liability company. It is a body corporate with separate legal personality but without the constraint of having share capital. Members of an LLC may have capital accounts and make capital contributions, with profits and losses allocated amongst those members as provided in the LLC agreement (which does not need to be filed with the Cayman Islands government). This offers a further structuring solution for securitisation and warehousing vehicles, in addition to the exempted company and the exempted limited partnership.

7.3 Location and form of Securitisation Entities. Is it typical to establish the special purpose entity in your jurisdiction or offshore? If in your jurisdiction, what are the advantages to locating the special purpose entity in your jurisdiction? If offshore, where are special purpose entities typically located for securitisations in your jurisdiction? What are the forms that the special purpose entity would normally take in your jurisdiction and how would such entity usually be owned?

Yes, the Cayman Islands jurisdiction is used extensively for the establishment of SPVs.

The Cayman Islands provides a tax neutral hub in a jurisdiction with a well-developed legal system for securitisation transactions, which is creditor-friendly and recognised by rating agencies. The jurisdiction has high-quality legal, professional and administrative service providers, is well known and understood by all market participants and is compliant with global regulatory standards.

The SPV will typically be a Cayman Islands exempted company. We also see the use of limited liability companies and, less frequently, exempted limited partnerships. The ordinary voting shares of the SPV would usually be owned by a licensed Cayman Islands trust company in its capacity as Share Trustee on trust for charitable purposes. The use of the charitable trust structure serves to take the SPV off the balance sheet of related transaction parties and, together with standard market structuring safeguards, serves to make the SPV's bankruptcy remote.

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7.4 Limited-Recourse Clause. Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) limiting the recourse of parties to that agreement to the available assets of the relevant debtor, and providing that to the extent of any shortfall the debt of the relevant debtor is extinguished?

Yes. A Cayman court will generally recognise a contractual limited recourse provision that, as a matter of its governing law, is valid, binding and enforceable. In the event that the contractual provision is governed by Cayman Islands law, although there is no precedent on point, we are of the view that a Cayman court would enforce such a provision that is clearly drafted to that effect based upon prior English case law which, although not binding, is strongly persuasive.

7.5 Non-Petition Clause. Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) prohibiting the parties from: (a) taking legal action against the purchaser or another person; or (b) commencing an insolvency proceeding against the purchaser or another person?

Yes. The Cayman Islands specifically introduced Section 95(2) of the Companies Law to provide that a Cayman court shall dismiss a winding up petition or adjourn the hearing of a winding up petition on the ground that the petitioner is contractually bound not to present a petition against the company. This provision would also apply to an exempted limited partnership pursuant to the Exempted Limited Partnership Law. Further, Section 39 of the Limited Liability Companies Law has an equivalent provision with respect to limited liability companies.

7.6 Priority of Payments "Waterfall". Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) distributing payments to parties in a certain order specified in the contract?

A Cayman court will generally recognise a priority of payments "waterfall" provision that as a matter of its governing law is valid, binding and enforceable. In the event that the contractual provision is governed by Cayman Islands law, although there is no precedent on this point, we are of the view that a Cayman court would enforce such a provision that is clearly drafted to that effect.

7.7 Independent Director. Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) or a provision in a party's organisational documents prohibiting the directors from taking specified actions (including commencing an insolvency proceeding) without the affirmative vote of an independent director?

Although it is possible for the articles of association to be drafted to give the directors the power to resolve to place a Cayman company into liquidation, articles of association for SPVs do not generally contain such a provision and the power to place a Cayman company remains a shareholder power. In order to ensure that such power is not exercised while a securitisation transaction is ongoing, the ordinary voting shares which carry such power are placed into an "orphan" charitable trust, the terms of which provide that the trustees cannot exercise such powers without the consent of a key transaction party (such as a trustee) so long as the notes or other form of financial instruments issued in connection with the securitisation transaction remain outstanding. Accordingly, there is no requirement for an independent director. This has been specifically recognised by the rating agencies with respect to their rating criteria for Cayman SPVs.

7.8 Location of Purchaser. Is it typical to establish the purchaser in your jurisdiction or offshore? If in your jurisdiction, what are the advantages to locating the purchaser in your jurisdiction? If offshore, where are purchasers typically located for securitisations in your jurisdiction?

It is common for purchasers to be established in the Cayman Islands whether as an exempted limited company, exempted limited partnership or as a limited liability company (or a combination of any of the three depending on the transaction). There are a number of benefits of such establishment in structured deals, including the variety of vehicles that can be used, the various tax benefits (see section 9 below) and the creditor-friendly nature of the jurisdiction (see question 7.2 above).

8 Regulatory Issues

8.1 Required Authorisations, etc. Assuming that the purchaser does no other business in your jurisdiction, will its purchase and ownership or its collection and enforcement of receivables result in its being required to qualify to do business or to obtain any licence or its being subject to regulation as a financial institution in your jurisdiction? Does the answer to the preceding question change if the purchaser does business with more than one seller in your jurisdiction?

The purchaser would only be subject to regulation if its activities are conducted pursuant to, or in connection with, a business carried on, from, in or within the Cayman Islands, i.e. regulation would not arise from the fact that the activities relate to a person domiciled in the Cayman Islands, but from the fact that the activities are being carried on in the Cayman Islands.

8.2 Servicing. Does the seller require any licences, etc., in order to continue to enforce and collect receivables following their sale to the purchaser, including to appear before a court? Does a third-party replacement servicer require any licences, etc., in order to enforce and collect sold receivables?

See question 8.1 above.

8.3 Data Protection. Does your jurisdiction have laws restricting the use or dissemination of data about or provided by obligors? If so, do these laws apply only to consumer obligors or also to enterprises?

The Confidential Information Disclosure Law, 2016 (the "CIDL") repealed the Confidential Relationships (Preservation) Law (2015 Revision) but retained its general restriction on the disclosure of confidential information. The CIDL defines "confidential information" broadly as information, arising in or brought into the Cayman Islands, concerning any property of a principal, to whom

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a duty of confidence is owed by the recipient of the information. There are certain exceptions under the CIDL to the disclosure of confidential information by such persons that owe a duty of confidence. These include disclosure of confidential information: (i) by compulsion under specific Cayman Islands law; (ii) in the normal course of business, with the implied or express consent of the principal; (iii) where such disclosure is compelled under law to a specific authority; and (iv) upon direction of the court pursuant to an application under the CIDL. The key difference between the CIDL and the prior legislation is that breach of the general restriction on the disclosure of confidential information is no longer a criminal offence under Cayman Islands law.

8.4 Consumer Protection. If the obligors are consumers, will the purchaser (including a bank acting as purchaser) be required to comply with any consumer protection law of your jurisdiction? Briefly, what is required?

See question 1.2 above. There are no specific consumer protection laws in the Cayman Islands.

8.5 Currency Restrictions. Does your jurisdiction have laws restricting the exchange of your jurisdiction's currency for other currencies or the making of payments in your jurisdiction's currency to persons outside the country?

No, there are no exchange control laws or regulations under Cayman Islands law.

8.6 Risk Retention. Does your jurisdiction have laws or regulations relating to "risk retention"? How are securitisation transactions in your jurisdiction usually structured to satisfy those risk retention requirements?

No, there are no laws or regulations relating to "risk retention" under Cayman Islands law. Cayman Islands SPVs are, however, frequently used in securitisation transactions to satisfy US and/or EU risk retention requirements.

8.7 Regulatory Developments. Have there been any regulatory developments in your jurisdiction which are likely to have a material impact on securitisation transactions in your jurisdiction?

No. While the Cayman Islands is an early adopter of regulations that comply with international standards to combat money laundering, terrorist financing and tax evasion, none of these regulations have had, or are expected to have, a material impact on securitisation transactions.

9 Taxation

9.1 Withholding Taxes. Will any part of payments on receivables by the obligors to the seller or the purchaser be subject to withholding taxes in your jurisdiction? Does the answer depend on the nature of the receivables, whether they bear interest, their term to maturity, or where the seller or the purchaser is located? In the case of a sale of trade receivables at a discount, is there a risk that the discount will be recharacterised in whole or in part as interest? In the case of a sale of trade receivables where a portion of the purchase price is payable upon collection of the receivable, is there a risk that the deferred purchase price will be recharacterised in whole or in part as interest? If withholding taxes might apply, what are the typical methods for eliminating or reducing withholding taxes?

No. The Cayman Islands currently has 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 of another taxing authority in the Cayman Islands under the laws of the Cayman Islands. Trade receivables sold at a discount will not be recharacterised under the laws of the Cayman Islands in whole or in part as interest, nor in the case of deferred purchase price for trade receivables.

9.2 Seller Tax Accounting. Does your jurisdiction require that a specific accounting policy is adopted for tax purposes by the seller or purchaser in the context of a securitisation?

No, it does not.

9.3 Stamp Duty, etc. Does your jurisdiction impose stamp duty or other transfer or documentary taxes on sales of receivables?

No stamp duties or other similar taxes or charges are payable under the laws of the Cayman Islands in respect of the execution, transfer or delivery of documents or debt securities, or the performance or enforcement of any of them, unless they are executed in, or thereafter brought within, the jurisdiction of the Cayman Islands. Mortgages over property (real and movable) situated in the Cayman Islands are subject to stamp duty.

9.4 Value Added Taxes. Does your jurisdiction impose value added tax, sales tax or other similar taxes on sales of goods or services, on sales of receivables or on fees for collection agent services?

There is no VAT, sales tax or similar tax on goods and services, sales of receivables or on fees for collection agent services within the Cayman Islands. Import taxes are payable on goods arriving in the Cayman Islands.

9.5 Purchaser Liability. If the seller is required to pay value-added tax, stamp duty or other taxes upon the sale of receivables (or on the sale of goods or services that give rise to the receivables) and the seller does not pay, then will the taxing authority be able to make claims for the unpaid tax against the purchaser or against the sold receivables or collections?

This is not applicable.

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9.6 Doing Business. Assuming that the purchaser conducts no other business in your jurisdiction, would the purchaser's purchase of the receivables, its appointment of the seller as its servicer and collection agent, or its enforcement of the receivables against the obligors, make it liable to tax in your jurisdiction?

This is not applicable; see question 9.1 above.

9.7 Taxable Income. If a purchaser located in your jurisdiction receives debt relief as the result of a limited recourse clause (see question 7.3 above), is that debt relief liable to tax in your jurisdiction?

No. See the response to question 9.1.

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China

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1 Receivables Contracts

1.1 Formalities. In order to create an enforceable debt obligation of the obligor to the seller: (a) is it necessary that the sales of goods or services are evidenced by a formal receivables contract; (b) are invoices alone sufficient; and (c) can a binding contract arise as a result of the behaviour of the parties?

Pursuant to the *General Principles of the Civil Law of the Peoples' Republic of China* ("PRC"), a debt obligation could be created by a contract. Generally speaking, PRC laws do not mandatorily request the sale of goods or services to be evidenced by a formal receivables contract; instead, the *PRC Contract Law* allows a contract to be concluded in writing (including formal written contract, letter or electronic communications), orally or other forms. Such general principle is subject to certain exceptions created by other laws, for instance, the *PRC Property Rights Law* requests a formal written contract for the transfer of land use rights.

In the PRC, invoices shall be produced in standard format and used for tax purposes only. An invoice alone is insufficient to evidence the conclusion of an enforceable debt obligation of the obligor to the seller, unless it is coupled with other evidence to prove the existence of a contractual relationship, such as communications between the parties and the conduct of the parties.

A binding contract can arise as a result of the behaviour of the parties, provided that such behaviour covers the performance of major obligations by the seller and the acceptance by the obligor in respect of the seller's such performance.

1.2 Consumer Protections. Do your jurisdiction's laws: (a) limit rates of interest on consumer credit, loans or other kinds of receivables; (b) provide a statutory right to interest on late payments; (c) permit consumers to cancel receivables for a specified period of time; or (d) provide other noteworthy rights to consumers with respect to receivables owing by them?

(a) Limit of Rates of Interest

PRC laws do not limit rates of interest on loans denominated in currencies other than RMB, the lawful currency of the PRC. Commercial banks are able to freely negotiate the interest rates of foreign exchange loans with their borrowers.

The interest rates of RMB loans extended by commercial banks are regulated by the Peoples' Bank of China ("PBOC"), which will, from time to time, issue benchmark interest rates of RMB loans for different tenors. Since October 2004, commercial banks are not subject to ceilings of interest rates on RMB loans, while since 20 July 2013, they are not subject to an interest rate floor on RMB loans either.

Pursuant to the *General Principles of Loan* issued by the PBOC in 1996, entities other than commercial banks and other financial institutions approved by the banking regulator are not allowed to extend loans in the PRC. However, PRC laws do not prohibit private lending, which means financing among natural persons, legal persons or other organisations (excluding financial institutions). The interest rates of such private lending are not subject to PBOC's regulatory requirements imposed on commercial banks, but pursuant to the *Interpretation concerning the Application of Law in the Trial of Private Lending Cases* issued by the PRC's Supreme Court on 6 August 2015 and effected on 1 September 2015, the lender's claim against the borrower for the interest will be upheld if the rate does not exceed 24% *per annum*, or if it has been paid by the borrower and its rate does not exceed 36% *per annum*.

(b) Interest on Late Payment

Pursuant to the *PBOC's Rules on Interest Rate of RMB Loan*, the late repayment of an RMB loan borrowed from commercial banks shall be subject to the default interest rate, which could vary from 130% to 150% of the interest rate as stipulated in the relevant RMB loan agreement.

Other than the default interest rate applicable to RMB loans granted by commercial banks, the default interest rate of private lending should not exceed 24% *per annum*, otherwise it will not be upheld by the People's Court pursuant to the *Interpretation concerning the Application of Law in the Trial of Private Lending Cases* issued by the PRC's Supreme Court on 6 August 2015 and effected on 1 September 2015.

Except for the above, as general principles created by the *PRC Contract Law*: (i) the parties are allowed to agree on interest on late payment in contract, provided that such interest on late payment is not excessively higher than the actual loss suffered by the non-defaulting party, otherwise the defaulting party may apply to the People's Court or Arbitration Tribunal for adjustment; and (ii) where there is no agreement regarding interest of late payment, the non-defaulting party is allowed to claim for compensation caused by such late payment through the People's Court or Arbitration Tribunal.

(c) Consumer's Rights to Cancel Receivables for a Specified Period of Time

Under the *PRC Consumer Protection Law* which was amended on 25 December 2013 and came into effect on 15 March 2014, unless

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mandatorily provided under laws and regulations or otherwise agreed upon by the parties, the consumer has the right to return the commodities within seven days from the date following receipt of the commodities, and may also return the commodities after such seven-day period should the conditions to cancel a contract be met. The State Administration of Industry and Commerce released the *Administrative Measures for Online Trading* on 26 January 2014, which came into effect on 15 March 2014. Pursuant to such rule, subject to exceptions as provided therein, where an online commodity operator sells commodities, the consumer is entitled to return the commodities within seven days from the date following receipt of the commodities without giving a reason.

In addition, there are some other regulations and provincial level rules applicable to specific marketing methods that impose "cooling-off" periods for the benefit of consumers that would enable consumers to withdraw from their commitment to transactions that they have previously entered into, for example:

(i) Pursuant to the *Regulations on Direct Selling* issued by the State Council in 2005, where the consumer purchases goods under a "direct selling", namely purchases the goods from the sales person directly hired by the manufacturer, the consumer is entitled to return the goods and get the purchase price refunded within 30 days after the purchase, provided that the goods have not been unpacked.

(ii) Pursuant to Shanghai's local rules regarding consumer protection, if the consumer purchases door-to-door goods, the consumer is entitled to return the goods and get the purchase price refunded within seven days after the purchase without any reasons.

(d) Other Noteworthy Rights of Consumers Regarding Receivables

It is noteworthy that the seller's rights to claim for the consumer's payment of receivables would be subject to the statutory limit generally applicable to all civil rights; for instance, under an international sale of goods, if the seller fails to claim for the consumer's payment of the purchase price within four years after the due date, such receivables would not be upheld by the People's Court anymore.

1.3 Government Receivables. Where the receivables contract has been entered into with the government or a government agency, are there different requirements and laws that apply to the sale or collection of those receivables?

Generally, PRC laws do not provide different requirements for the sale or collection of government receivables generated under a commercial transaction, except that the formalities of government procurement agreement shall be compliant with the *PRC Government Procurement Law*. However, it is notable that, under PRC laws, all the payments to be made by the government or a government agency shall be included in the annual budget of the central or local government, which shall be approved by the People's Congress of the corresponding level.

2 Choice of Law – Receivables Contracts

2.1 No Law Specified. If the seller and the obligor do not specify a choice of law in their receivables contract, what are the main principles in your jurisdiction that will determine the governing law of the contract?

In the absence of choice of law in a receivables contract, the main principles for determining the governing law will differentiate between domestic transactions and foreign-related transactions.

If the transaction is a purely domestic transaction, PRC law could be the only governing law to the contract.

If the transaction is a foreign-related transaction, pursuant to the *PRC Laws on Governing Law of Foreign-related Civil Relationships* effective from 1 April 2011, the governing law can be determined based on the principles of "country of the party with characteristic performance" and "country most closely connected".

Pursuant to the *Interpretation on Several Issues Concerning Application of the PRC Laws on Governing Law of Foreign-related Relationships (I)* issued by the PRC's Supreme Court on 28 December 2012, where a transaction falls under any of the following circumstances, the court may determine it to be a foreign-related transaction: (i) where any of the parties is a foreign citizen, foreign legal person or other organisation or stateless person; (ii) where the residence of any party is located outside the territory of the PRC; (iii) where the subject is outside the territory of the PRC; (iv) where the legal fact that leads to establishment, change or termination of the civil relationship happens outside the territory of the PRC; or (v) other applicable circumstances.

2.2 Base Case. If the seller and the obligor are both resident in your jurisdiction, and the transactions giving rise to the receivables and the payment of the receivables take place in your jurisdiction, and the seller and the obligor choose the law of your jurisdiction to govern the receivables contract, is there any reason why a court in your jurisdiction would not give effect to their choice of law?

No, there is no reason why a PRC court would not give effect to the parties' choice of law under such circumstances.

2.3 Freedom to Choose Foreign Law of Non-Resident Seller or Obligor. If the seller is resident in your jurisdiction but the obligor is not, or if the obligor is resident in your jurisdiction but the seller is not, and the seller and the obligor choose the foreign law of the obligor/seller to govern their receivables contract, will a court in your jurisdiction give effect to the choice of foreign law? Are there any limitations to the recognition of foreign law (such as public policy or mandatory principles of law) that would typically apply in commercial relationships such as that between the seller and the obligor under the receivables contract?

Pursuant to the *PRC Laws on Governing Law of Foreign-related Civil Relationships* and the Supreme Court's interpretation thereto issued in 2012, the above situation would enable the receivables contract to be deemed as a contract with a "foreign element", and the PRC court would generally give effect to the choice of foreign law.

The above general principle will not apply under the following circumstances:

(a) PRC laws have mandatory principles of law for this type of contract. For instance, a contract in respect of real estate shall be governed by laws where the real estate is located, and a Sino-foreign joint venture contract shall be mandatorily governed by the PRC law, etc.; and

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(b) choosing foreign law as the governing law will jeopardise the public interest of the PRC, in which case PRC law shall be the governing law.

3 Choice of Law – Receivables Purchase Agreement

3.1 Base Case. Does your jurisdiction's law generally require the sale of receivables to be governed by the same law as the law governing the receivables themselves? If so, does that general rule apply irrespective of which law governs the receivables (i.e., your jurisdiction's laws or foreign laws)?

No, PRC law does not require the sale of receivables to be governed by the same law as the law governing the receivables themselves.

3.2 Example 1: If (a) the seller and the obligor are located in your jurisdiction, (b) the receivable is governed by the law of your jurisdiction, (c) the seller sells the receivable to a purchaser located in a third country, (d) the seller and the purchaser choose the law of your jurisdiction to govern the receivables purchase agreement, and (e) the sale complies with the requirements of your jurisdiction, will a court in your jurisdiction recognise that sale as being effective against the seller, the obligor and other third parties (such as creditors or insolvency administrators of the seller and the obligor)?

Due to the foreign exchange control in the PRC, a PRC seller is not able to sell the receivables generated from a PRC obligor to an offshore purchaser.

Purely from the choice of law perspective, a PRC court would recognise the choice of PRC law to the receivables purchase agreement ("RPA"). Whether the sale is effective against the obligor is likely to be determined by the court under the PRC law as to whether the conditions under the sales contract or as a matter of law have been satisfied.

3.3 Example 2: Assuming that the facts are the same as Example 1, but either the obligor or the purchaser or both are located outside your jurisdiction, will a court in your jurisdiction recognise that sale as being effective against the seller and other third parties (such as creditors or insolvency administrators of the seller), or must the foreign law requirements of the obligor's country or the purchaser's country (or both) be taken into account?

A PRC court recognises the choice of PRC law and recognises the sale as being effective against the seller, the obligor and other third parties, provided that the relevant requirements under the PRC law for the sale have been complied with.

The foreign law requirements of the obligor's country or the purchaser's country (or both) may apply with respect to enforcement actions against the obligor or the purchaser, as applicable.

3.4 Example 3: If (a) the seller is located in your jurisdiction but the obligor is located in another country, (b) the receivable is governed by the law of the obligor's country, (c) the seller sells the receivable to a purchaser located in a third country, (d) the seller and the purchaser choose the law of the obligor's country to govern the receivables purchase agreement, and (e) the sale complies with the requirements of the obligor's country, will a court in your jurisdiction recognise that sale as being effective against the seller and other third parties (such as creditors or insolvency administrators of the seller) without the need to comply with your jurisdiction's own sale requirements?

The principles regarding the recognition of the choice of foreign law governing the sale of the receivables, as discussed in questions 2.3 and 3.1 above, will apply.

Assuming the sale is effective against the seller and other third parties in the PRC, pursuant to its governing law, a PRC court will recognise the sale as being effective against the seller and such other third parties, provided that:

(a) mandatory rules and requirements under PRC law must be complied with if, and to the extent that, they are applicable. For instance, due to foreign exchange control, the seller may be subject to the authenticity verification imposed by the foreign exchange authority for its sale of receivables to the purchaser; and

(b) when bringing enforcement actions against the seller before a PRC court, the rules regarding enforcement of foreign court judgment or arbitration awards will apply.

3.5 Example 4: If (a) the obligor is located in your jurisdiction but the seller is located in another country, (b) the receivable is governed by the law of the seller's country, (c) the seller and the purchaser choose the law of the seller's country to govern the receivables purchase agreement, and (d) the sale complies with the requirements of the seller's country, will a court in your jurisdiction recognise that sale as being effective against the obligor and other third parties (such as creditors or insolvency administrators of the obligor) without the need to comply with your jurisdiction's own sale requirements?

Please see the answer to question 3.4 above.

3.6 Example 5: If (a) the seller is located in your jurisdiction (irrespective of the obligor's location), (b) the receivable is governed by the law of your jurisdiction, (c) the seller sells the receivable to a purchaser located in a third country, (d) the seller and the purchaser choose the law of the purchaser's country to govern the receivables purchase agreement, and (e) the sale complies with the requirements of the purchaser's country, will a court in your jurisdiction recognise that sale as being effective against the seller and other third parties (such as creditors or insolvency administrators of the seller, any obligor located in your jurisdiction and any third party creditor or insolvency administrator of any such obligor)?

If the obligor is located in the PRC, please see question 3.2 above.

If the obligor is located in a country other than the PRC, please see question 3.4 above.

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4 Asset Sales

4.1 Sale Methods Generally. In your jurisdiction what are the customary methods for a seller to sell receivables to a purchaser? What is the customary terminology – is it called a sale, transfer, assignment or something else?

Sale of receivables is deemed as an assignment of contract rights under the *PRC Contract Law*. The *PRC Contract Law* stipulates that a creditor may assign its rights under a contract to a third party, subject to any assignment restrictions contained in the original contract or otherwise stated in PRC law.

The customary terminology in the PRC for the sale of receivables is "assignment".

4.2 Perfection Generally. What formalities are required generally for perfecting a sale of receivables? Are there any additional or other formalities required for the sale of receivables to be perfected against any subsequent good faith purchasers for value of the same receivables from the seller?

A sale of receivables will generally be deemed concluded between the seller and the purchaser pursuant to the RPA. Pursuant to the *PRC Contract Law*, the assignment of contract rights by a creditor will become effective against the obligor once a notice of assignment has been serviced to the obligor.

PRC laws do not request additional or other formalities for the sale of receivables to be perfected against any subsequent good faith purchasers. Although the PBOC has established an online registration system for the pledge/assignment of account receivables, such sale of receivables registration has not been vested with a public announcement function by law to claim against *bona fide* third-party purchasers.

It is notable that where the sale of receivables involves the transfer of security interest attached to the assigned receivables, the answers to questions 4.3 and 4.12 below will apply. Furthermore, where the receivables are generated under a cross-border transaction, or the sale of receivables will cause conversion of RMB to foreign currency, the answer to question 8.5 below will apply.

4.3 Perfection for Promissory Notes, etc. What additional or different requirements for sale and perfection apply to sales of promissory notes, mortgage loans, consumer loans or marketable debt securities?

Under the *PRC Instruments Law*, promissory notes are deemed as on-demand payment instruments and can only be issued by commercial banks. Transfer of promissory notes will request the endorsement from issuer or holder, as the case may be, and delivery of the same to the purchaser.

In respect of mortgage loans, pursuant to the *PRC Property Rights Law* and *PRC Security Law*, the mortgage rights enjoyed by the seller can be transferred together with the secured indebtedness, but the mortgage rights in favour of the purchaser shall be registered with the relevant registration authority.

The sale of consumer loans will not be subject to additional or different sale or perfection requirements, in addition to question 4.2 above.

The sale of marketable debt securities issued in the public market, such as bonds and notes, shall be conducted through the applicable clearing agency, such as China's Securities Depository and Clearing Corporation Limited (for bonds traded on the stock exchange) and China's Government Securities Depository Trust & Clearing Co. Ltd. (for notes traded on the National Inter-bank Market).

4.4 Obligor Notification or Consent. Must the seller or the purchaser notify obligors of the sale of receivables in order for the sale to be effective against the obligors and/or creditors of the seller? Must the seller or the purchaser obtain the obligors' consent to the sale of receivables in order for the sale to be an effective sale against the obligors? Whether or not notice is required to perfect a sale, are there any benefits to giving notice – such as cutting off obligor set-off rights and other obligor defences?

Pursuant to the *PRC Contract Law*, the assignment of contract rights by a creditor will become effective against the obligor once a notice of assignment has been served to the obligor.

The obligor's consent to the sale of receivables is normally not required for the sale to be an effective sale against the obligor unless expressly required under the original receivables contract.

The notice to the obligor will make the sale of receivables effective against the obligor, and give rise to certain benefits to the purchaser as follows:

(a) the obligor will not be able to claim for set-off rights against the seller entitled to the obligor after the service of the notice;

(b) the obligor must make payments as directed by the purchaser and the obligor can no longer discharge its obligations by making payment to the seller;

(c) enforcement actions may be taken by the purchaser against the obligor directly without involving the seller; and

(d) depending on the content of the receivables contract and notice, the obligor and the seller may no longer amend the underlying receivables contract.

Having said that, the notice will not cut off the obligor's existing rights against the seller under the receivables contract, such as claiming for the seller's non-performance of its obligation.

4.5 Notice Mechanics. If notice is to be delivered to obligors, whether at the time of sale or later, are there any requirements regarding the form the notice must take or how it must be delivered? Is there any time limit beyond which notice is ineffective – for example, can a notice of sale be delivered after the sale, and can notice be delivered after insolvency proceedings have commenced against the obligor or the seller? Does the notice apply only to specific receivables or can it apply to any and all (including future) receivables? Are there any other limitations or considerations?

There are no requirements regarding the timing of service of the notice to the obligor, nor are there any requirements regarding the form a notice must take or how the notice must be delivered in order for the notice to be legally valid and effective under PRC laws. In practice, a notice of assignment will generally be made in written form and include a request for an acknowledgment of the assignment (or, where applicable, a consent to the assignment) by the obligor for evidence purposes.

There is no time limit beyond which the delivery of notice would become ineffective. A notice may be delivered to the obligor regardless of whether an insolvency proceeding has commenced against the obligor. However, it is strongly suggested that notice be sent before the insolvency proceedings against the seller have commenced.

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A notice may relate to all, or only part of, the existing receivables between the obligor and the seller, and subject to the answer to question 4.10 below.

4.6 Restrictions on Assignment – General Interpretation. Will a restriction in a receivables contract to the effect that "None of the [seller's] rights or obligations under this Agreement may be transferred or assigned without the consent of the [obligor]" be interpreted as prohibiting a transfer of receivables by the seller to the purchaser? Is the result the same if the restriction says "This Agreement may not be transferred or assigned by the [seller] without the consent of the [obligor]" (i.e., the restriction does not refer to rights or obligations)? Is the result the same if the restriction says "The obligations of the [seller] under this Agreement may not be transferred or assigned by the [seller] without the consent of the [obligor]" (i.e., the restriction does not refer to rights)?

Yes. All the above restrictions will prohibit the seller from assigning its rights or transferring its obligations to a third party without the obligor's consent. In addition, it is explicitly provided under the *PRC Contract Law* that if the debtor transfers all or part of its obligations to a third party, the consent of the creditor shall be obtained.

4.7 Restrictions on Assignment; Liability to Obligor. If any of the restrictions in question 4.6 are binding, or if the receivables contract explicitly prohibits an assignment of receivables or "seller's rights" under the receivables contract, are such restrictions generally enforceable in your jurisdiction? Are there exceptions to this rule (e.g., for contracts between commercial entities)? If your jurisdiction recognises restrictions on sale or assignment of receivables and the seller nevertheless sells receivables to the purchaser, will either the seller or the purchaser be liable to the obligor for breach of contract or tort, or on any other basis?

Such restrictions are generally enforceable in the PRC, and we are not aware of any exceptions to this rule.

If the seller sells the receivables to the purchaser irrespective of the prohibitions in the receivables contract, it is the seller who will be liable to the obligor for breach of contract. Under such circumstances, the sale will not be effective against the obligor unless its consent is obtained.

4.8 Identification. Must the sale document specifically identify each of the receivables to be sold? If so, what specific information is required (e.g., obligor name, invoice number, invoice date, payment date, etc.)? Do the receivables being sold have to share objective characteristics? Alternatively, if the seller sells *all* of its receivables to the purchaser, is this sufficient identification of receivables? Finally, if the seller sells *all* of its receivables *other than* receivables owing by one or more specifically identified obligors, is this sufficient identification of receivables?

Under PRC laws, a sale document must provide sufficiently specific descriptions of the receivables to be sold so that they are capable of being identified at the time of the assignment. This does not necessarily require that each receivable has to be separately identified.

There is no legal requirement on what specific information is required, but in practice, in order to make the receivables identifiable, some basic information such as obligor's name, invoice date, payment date, etc., needs to be stated. The receivables being sold do not necessarily need to share objective characteristics.

A statement that the seller sells all of its receivables to the purchaser is unlikely to be deemed as sufficient identification of receivables, nor will a statement that the seller sells all of its receivables other than receivables owing by one or more specifically identified obligors, be deemed as sufficient.

4.9 Recharacterisation Risk. If the parties describe their transaction in the relevant documents as an outright sale and explicitly state their intention that it be treated as an outright sale, will this description and statement of intent automatically be respected or is there a risk that the transaction could be characterised by a court as a loan with (or without) security? If recharacterisation risk exists, what characteristics of the transaction might prevent the transfer from being treated as an outright sale? Among other things, to what extent may the seller retain any of the following without jeopardising treatment as an outright sale: (a) credit risk; (b) interest rate risk; (c) control of collections of receivables; (d) a right of repurchase/redemption; (e) a right to the residual profits within the purchaser; or (f) any other term?

As discussed in question 4.1 above, the sale of receivables is to be carried out by way of assignment of contract rights. As a general contract law principle, a PRC court would generally respect the parties' intent to honour a transaction as an assignment of contract rights. However, in certain circumstances, the PRC court may still characterise the transaction as a loan, for example:

(a) There is no receivables contract or the receivables contract is null and void. Pursuant to the *PRC Contract Law*, a contract may be deemed as null and void under the following situations:
   (i) it is concluded through the use of fraud or coercion by one party to jeopardise the interests of the State;
   (ii) malicious collusion is conducted to jeopardise the interests of the State, a collective or a third party;
   (iii) an illegitimate purpose is concealed under the guise of legitimate activities;
   (iv) damage to the public interest; or
   (v) violation of the compulsory provisions of laws and administrative regulations.

   Under such circumstances, where the court finds that the purchaser has already known the non-existence or invalidity of the receivables contract when entering into the assignment with the seller, the purchaser is likely to be deemed as granting loans to the seller.

(b) The RPA is ambiguous in respect of the assignment of receivables.

(c) The assignment of the receivables by the sellers is not a normal and fair sale with reasonable consideration and constitutes a gratuitous assignment by the sellers of its proprietary rights, or an abnormal under-sale of its assets, or an abandonment of its creditor's rights. Under such circumstances, the assignment, sale or abandonment shall be null and void if, pursuant to the *PRC Enterprise Bankruptcy Law*, such act occurs during the period commencing within one year prior to the acceptance by the People's Court of the bankruptcy case of the seller.

(d) Where the assignment of receivables is made on the condition that the seller will retain credit risk of the receivables, such assignment is very likely to be recharacterised as a loan.

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(e) Pursuant to the China Banking Regulatory Commission ("CBRC")'s notice issued in 2009, when a banking institution assigns its credit assets, it shall not retain the credit risks of the credit assets to be assigned, nor is it allowed to retain right of repurchase/redemption thereof.

(f) The PRC Law is silent on whether a right to the residual profits retained by the seller would jeopardise treatment as an outright sale.

Subject to the above, to our general understanding, where the seller retains interest rate risks and/or control of collection of receivables and/or a right to the residual profits, the assignment of receivables is unlikely to be jeopardised.

4.10 Continuous Sales of Receivables. Can the seller agree in an enforceable manner to continuous sales of receivables (i.e., sales of receivables as and when they arise)? Would such an agreement survive and continue to transfer receivables to the purchaser following the seller's insolvency?

PRC laws do not squarely deal with this issue. In our general experience, the following requirements need to be followed in order to make such continuous assignment of receivables enforceable:

(a) the RPA has clearly stated the parties' intention of continuous assignment of receivables; and

(b) the receivables shall be identifiable. Please see our answer to question 4.8 above.

While following the seller's insolvency, pursuant to the *PRC Enterprise Bankruptcy Law*, the administrator would have the power to reject or continue to perform any pre-petition executory contracts, and whether the sale agreement would survive and continue to be effective is also subject to our answer to question 6.3 below.

4.11 Future Receivables. Can the seller commit in an enforceable manner to sell receivables to the purchaser that come into existence after the date of the receivables purchase agreement (e.g., "future flow" securitisation)? If so, how must the sale of future receivables be structured to be valid and enforceable? Is there a distinction between future receivables that arise prior to *versus* after the seller's insolvency?

There is no clear legal basis under PRC laws for the enforceability of a current transfer of future receivables before the seller's insolvency. General understanding is that if (a) the future receivables arise from a presently existing receivables contract, (b) the seller has already performed its major obligations (such as delivery of goods with agreed quantity and quality), and (c) proper notice has been served to the obligor, the present sale of receivables is unlikely to be challenged.

Where the seller goes into bankruptcy, pursuant to the *PRC Enterprise Bankruptcy Law*, the administrator would have the power to reject or continue to perform any pre-petition executory contracts.

4.12 Related Security. Must any additional formalities be fulfilled in order for the related security to be transferred concurrently with the sale of receivables? If not all related security can be enforceably transferred, what methods are customarily adopted to provide the purchaser the benefits of such related security?

The nature of the assets constituting the related security will determine the additional formalities, if any, applicable to the transfer. Pursuant to the *PRC Property Rights Law* and *PRC Security Law*, the formalities applicable to transfer of security could be categorised as follows:

(a) pursuant to Article 192 of the *PRC Property Rights Law*, mortgage rights are very likely transferred simultaneously along with the transfer of the secured indebtedness and such mortgage transfer shall remain valid even without re-registration. However, such mortgage transfer, without being re-registered in favour of the new mortgagee, shall not be effective against any *bona fide* third party;

(b) for pledges of movable assets, which are established by execution of a written pledge contract and delivery of possession of the pledged object to the pledgee, the pledge rights may be transferred together with the secured indebtedness by assignment and re-delivery of the possession of the pledged assets to the pledgee;

(c) for the pledges of rights, which are established by execution of a written pledge contract and delivery of possession of rights documents, such as draft, promissory notes, cheques, bonds in the form of definitive note, depository notes, warehouse receipts, bill of lading, and pledge rights may be transferred together with the secured indebtedness only by execution of a new pledge contract and endorsement on and/or delivery (as the case may be) of the rights documents to the new pledgee; and

(d) for the pledge of rights, which are established by execution of a written pledge contract and registration with relevant registration agencies, such as securities, equity interest, IP rights, receivables, etc., pledge rights may be transferred together with the secured indebtedness only by execution of a new pledge contract and re-registration of the pledge in favour of the new pledgee.

In addition, where the creation of the existing security also involves other government authorities' approvals/registration processes, for instance, mortgages/pledges of bonded warehouse goods would require approval from customs, and security in favour of offshore creditor requests approval and/or registration from the SAFE, the transfer of such security interest shall also be subject to re-approval by and/or re-registration with relevant original approving/registration authorities.

4.13 Set-Off; Liability to Obligor. Assuming that a receivables contract does not contain a provision whereby the obligor waives its right to set-off against amounts it owes to the seller, do the obligor's set-off rights terminate upon its receipt of notice of a sale? At any other time? If a receivables contract does not waive set-off but the obligor's set-off rights are terminated due to notice or some other action, will either the seller or the purchaser be liable to the obligor for damages caused by such termination?

No. Under the *PRC Contract Law*, the obligor may set off the receivables against the amount the seller owes to it when the obligor receives the notice of assignment of the receivables provided that the latter amount is due at the same time as, or prior to that of, the receivables.

The *PRC Contract Law* is silent on when the obligor's right of set-off terminates, but it appears that if the obligor does not claim such right promptly after it receives such notice, such right will terminate. Under such circumstances, neither the seller nor the purchaser is liable to the obligor for the termination of the set-off right.

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4.14 Profit Extraction. What methods are typically used in your jurisdiction to extract residual profits from the purchaser?

In the PRC, it is not common that a right to residual profits retained by the seller is directly set in the terms of a receivables contract. However, in a receivables securitisation transaction, the seller is very likely to be the subordinated securities holder which is entitled to all residual cash after all senior securities being fully repaid. Therefore, when there are residual profits, the residual profits may be allocated to the seller as a subordinated securities holder.

5 Security Issues

5.1 Back-up Security. Is it customary in your jurisdiction to take a "back-up" security interest over the seller's ownership interest in the receivables and the related security, in the event that an outright sale is deemed by a court (for whatever reason) not to have occurred and have been perfected (see question 4.9 above)?

No, it is not customary.

5.2 Seller Security. If it is customary to take back-up security, what are the formalities for the seller granting a security interest in receivables and related security under the laws of your jurisdiction, and for such security interest to be perfected?

This is not applicable in the PRC.

5.3 Purchaser Security. If the purchaser grants security over all of its assets (including purchased receivables) in favour of the providers of its funding, what formalities must the purchaser comply with in your jurisdiction to grant and perfect a security interest in purchased receivables governed by the laws of your jurisdiction and the related security?

Pursuant to Article 228 of the *PRC Property Rights Law*, the pledgor and the pledgee shall sign a written contract for the pledge of account receivables. The pledge over account receivables comes into effect when the pledge has been duly registered with the Credit Reference Centre ("CRC") of the PBOC.

5.4 Recognition. If the purchaser grants a security interest in receivables governed by the laws of your jurisdiction, and that security interest is valid and perfected under the laws of the purchaser's jurisdiction, will the security be treated as valid and perfected in your jurisdiction or must additional steps be taken in your jurisdiction?

The security interest will not be automatically perfected under PRC laws after it is perfected under the laws of the purchaser's jurisdiction. Registration with the CRC, as mentioned in question 5.3 above, must be made in the PRC.

5.5 Additional Formalities. What additional or different requirements apply to security interests in or connected to insurance policies, promissory notes, mortgage loans, consumer loans or marketable debt securities?

There are no definitive rules with additional requirements applying to security interests in, or connected to, insurance policies under PRC law.

A security interest in promissory notes may be created by way of a pledge. Article 224 of the *PRC Property Rights Law* stipulates that the pledgor and the pledgee shall draw up a written contract for the pledge and such security interest shall be created upon the delivery of the pledged promissory note to the pledgee. In addition, pursuant to Article 98 of the *Judicial Interpretations of the PRC Security Law*, the promissory note shall be endorsed on the reverse side with the word "pledge" in order to be enforceable against a *bona fide* third party. Therefore, delivery and endorsement are the statutory requirements to create a perfected pledge on promissory notes.

A security interest in marketable debt securities, such as bonds, may also be created by way of a pledge. The pledgor and the pledgee shall enter into a written contract and such security interest shall be created upon the delivery of the certificate of marketable debt securities to the pledgee if it is in the form of a definitive note. Moreover, pursuant to Article 99 of the *Judicial Interpretations of the PRC Security Law*, the certificate shall be endorsed on the reverse side with the word "pledge" in order to be enforceable against a *bona fide* third party. Under the circumstance that there is no tangible certificate, the pledge rights shall be created upon the registration of such pledge at the relevant authority. The relevant depository and clearing institutions refer to the China Securities Depository and Clearing Corporation Limited where marketable debt securities are traded on the stock exchange, or China Government Securities Depository Trust & Clearing Co. Ltd. and Shanghai Clearing House where the marketable debt securities are traded on the National Inter-Bank Market.

PRC laws are silent on whether security interest could be created over the mortgage loans or consumer loans or not.

5.6 Trusts. Does your jurisdiction recognise trusts? If not, is there a mechanism whereby collections received by the seller in respect of sold receivables can be held or be deemed to be held separate and apart from the seller's own assets (so that they are not part of the seller's insolvency estate) until turned over to the purchaser?

Trusts are recognised under PRC laws. However, the trust in the PRC is usually in a form of special purpose trust. A CBRC-licensed trust company operates as the trustee and administrates the trust assets for the benefits of beneficiaries. A PRC court may not give effect to collection trust in relation to receivables which is conducted by virtue of "hold on trust" or "trust declaration". Before the monies turned over to the purchaser, the monetary proceeds held by the seller constitute the seller's asset, therefore there stands the commingling risk if the seller goes bankrupt. Nonetheless, if the purchaser has paid off the purchase price and the collections are deposited separately and apart from the seller's other assets, in practice the PRC courts may probably permit the purchaser to get the collections back even if the seller is insolvent.

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5.7 Bank Accounts. Does your jurisdiction recognise escrow accounts? Can security be taken over a bank account located in your jurisdiction? If so, what is the typical method? Would courts in your jurisdiction recognise a foreign law grant of security (for example, an English law debenture) taken over a bank account located in your jurisdiction?

Escrow accounts are recognised and widely used in the PRC.

Except that the pledge created by a bank as the pledgee over export tax rebate accounts is recognised by the PRC Supreme People's Court in accordance with the *Provisions of Relevant Issues Concerning the Trial of Cases Involving Loans Pledged with an Export Tax Rebate Custodian Account* promulgated by the Supreme People's Court on 22 November 2004, there is no concept of security over a bank account under PRC laws.

Bank accounts are not considered a type of property explicitly recognised by PRC law as pledgeable assets. Instead, cash is, in general, characterised as a special type of movable asset and the pledge is explicitly recognised under PRC laws. The general rule under the *PRC Security Law* is that no pledge may be created over future funds in bank accounts. Funds in a bank account for a pledge shall be ascertained and identified at the time of perfection of the pledge. Pursuant to Article 85 of the *Judicial Interpretations of the PRC Security Law*, the cash may be delivered to the creditor in its possession as security for the performance of an obligation, and the creditor may have priority in applying such cash towards the satisfaction of an obligation owed to the creditor, if the cash is "fixed" in the form of special accounts (i.e. the parties have to specify the account as well as the cash balance standing to the credit of such an account).

Any cash flow in or out after the account has been fixed will require the pledgor to re-issue a pledge notice/confirmation specifying the updated cash balance. Such confirmation letter shall be issued each time a change occurs to the account balance. Otherwise, the pledge will no longer be valid under PRC laws.

We noticed a few precedents in which the security governed by foreign laws over a PRC account was recognised by PRC courts. PRC is not a common law jurisdiction. Case precedent might not be recognised by other courts.

5.8 Enforcement over Bank Accounts. If security over a bank account is possible and the secured party enforces that security, does the secured party control all cash flowing into the bank account from enforcement forward until the secured party is repaid in full, or are there limitations? If there are limitations, what are they?

This is not applicable to bank accounts other than export tax rebate custodian accounts. In respect of the export tax rebate custodian account, pursuant to the *Provisions of Relevant Issues Concerning the Trial of Cases Involving Loans Pledged with an Export Tax Rebate Custodian Account*, the pledgee may, to the extent of the outstanding secured debt, apply all the funds in the pledged bank account to discharge such debt.

5.9 Use of Cash Bank Accounts. If security over a bank account is possible, can the owner of the account have access to the funds in the account prior to enforcement without affecting the security?

This is not applicable to bank accounts other than export tax rebate custodian accounts. In respect of the export tax rebate custodian account, the owner of the account could not access the funds in the export tax rebate account unless the pledgee agrees to release the funds in the account in whole or in part.

6 Insolvency Laws

6.1 Stay of Action. If, after a sale of receivables that is otherwise perfected, the seller becomes subject to an insolvency proceeding, will your jurisdiction's insolvency laws automatically prohibit the purchaser from collecting, transferring or otherwise exercising ownership rights over the purchased receivables (a "stay of action")? If so, what generally is the length of that stay of action? Does the insolvency official have the ability to stay collection and enforcement actions until he determines that the sale is perfected? Would the answer be different if the purchaser is deemed to only be a secured party rather than the owner of the receivables?

After a sale of receivables that is otherwise perfected, and provided that the sale of receivables is not subject to any situations as stated in question 4.8 above and the clawback discussion in question 6.3 below, the rights of a purchaser made in good faith will remain unaffected by subsequent insolvency proceedings of a seller. However, the situation would be different if:

(a) The purchaser is deemed to only be a secured party with respect to the receivables. In such circumstances, pursuant to Article 16 of the *PRC Enterprise Bankruptcy Law*, a moratorium would apply to all creditors (secured and unsecured) upon the acceptance by the PRC court of a petition of insolvency in respect of the seller. The moratorium would last until an order of insolvency and liquidation issued by the PRC court. During the moratorium, the secured creditor would be stayed from enforcing its security. Pursuant to Article 109 of the *PRC Enterprise Bankruptcy Law*, upon liquidation of the seller's estate, a secured creditor would have priority over all unsecured creditors (other than statutory preferential creditors) over the property secured.

(b) The seller goes into insolvency after it has executed the RPA with the purchaser but neither party has completed the performance of such agreement. Under such circumstances, pursuant to Article 18 of the *PRC Enterprise Bankruptcy Law*, the bankruptcy administrator will have the right to determine whether to terminate or to continue to perform such agreement. If the bankruptcy administrator fails to notify the purchaser within two months of the acceptance of any bankruptcy petition in respect of the seller, or fails to reply within 30 days upon receipt of a purchaser's demand to make such a decision, such agreement shall be deemed to be terminated. If the bankruptcy administrator determines to continue to perform such agreement, the purchaser shall perform such agreement, provided that the purchaser has a right to require the bankruptcy administrator to provide a guarantee for such performance. The agreement would be deemed to be terminated if the bankruptcy administrator refuses to provide a guarantee.

If the bankruptcy administrator determines to continue to perform such receivables contracts, the purchaser's rights under the RPA would not be affected.

On the contrary, if the bankruptcy administrator refuses to continue to perform such a receivables contract, the receivables contract would be terminated accordingly. In that case, the purchaser is only entitled to ask the underlying obligor for those receivables in relation to the obligations that have already been performed by the seller;

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whilst for the purchase price and damage corresponding to the rest parts, the purchaser may only be able to claim through distribution of bankruptcy property as an ordinary creditor of the seller.

6.2 Insolvency Official's Powers. If there is no stay of action, under what circumstances, if any, does the insolvency official have the power to prohibit the purchaser's exercise of its ownership rights over the receivables (by means of injunction, stay order or other action)?

This is not applicable in the PRC.

6.3 Suspect Period (Clawback). Under what facts or circumstances could the insolvency official rescind or reverse transactions that took place during a "suspect" or "preference" period before the commencement of the seller's insolvency proceedings? What are the lengths of the "suspect" or "preference" periods in your jurisdiction for (a) transactions between unrelated parties, and (b) transactions between related parties? If the purchaser is majority-owned or controlled by the seller or an affiliate of the seller, does that render sales by the seller to the purchaser "related party transactions" for purposes of determining the length of the suspect period? If a parent company of the seller guarantee's the performance by the seller of its obligations under contracts with the purchaser, does that render sales by the seller to the purchaser "related party transactions" for purposes of determining the length of the suspect period?

The transactions between the seller and its related or unrelated parties will be subject to the same principle of clawback.

Article 16 of the *PRC Enterprise Bankruptcy Law* restricts any payments from the debtor to its creditors once the court has accepted the bankruptcy petition in relation to the debtor. The bankruptcy administrator also has the right under Article 32 of the *PRC Enterprise Bankruptcy Law* to request the court to revoke any preferential payments made by the bankrupted entity within the six-month period prior to the court's acceptance of the bankruptcy petition, unless those payments benefit the bankrupt entity's estate.

Under Article 31 of the *PRC Enterprise Bankruptcy Law*, the bankruptcy administrator has the right to request the court to revoke any of the following acts relating to the debtor's assets to the extent occurring within one year prior to the court's acceptance of the bankruptcy petition: (a) transferring the property gratis; (b) trading at an obviously unreasonable price; (c) providing property guaranty to unsecured debts; (d) paying off debts not due; or (e) abandoning claims.

6.4 Substantive Consolidation. Under what facts or circumstances, if any, could the insolvency official consolidate the assets and liabilities of the purchaser with those of the seller or its affiliates in the insolvency proceeding? If the purchaser is owned by the seller or by an affiliate of the seller, does that affect the consolidation analysis?

There is no concept of substantive consolidation in the PRC.

6.5 Effect of Insolvency on Receivables Sales. If insolvency proceedings are commenced against the seller in your jurisdiction, what effect do those proceedings have on (a) sales of receivables that would otherwise occur after the commencement of such proceedings, or (b) on sales of receivables that only come into existence after the commencement of such proceedings?

Subject to the answer to question 4.11 above regarding the recognition of future receivables, our discussion in question 6.1 (b) above will apply.

6.6 Effect of Limited Recourse Provisions. If a debtor's contract contains a limited recourse provision (see question 7.3 below), can the debtor nevertheless be declared insolvent on the grounds that it cannot pay its debts as they become due?

Since, under the limited recourse provision, the recourse of the creditor is limited to the available assets of the debtor and if there is any shortfall the debt will be extinguished, it seems unlikely that the debtor will be declared on such grounds.

7 Special Rules

7.1 Securitisation Law. Is there a special securitisation law (and/or special provisions in other laws) in your jurisdiction establishing a legal framework for securitisation transactions? If so, what are the basics? Is there a regulatory authority responsible for regulating securitisation transactions in your jurisdiction?

Since 2005, the PRC regulatory authorities and the market participants worked out two possible securitisation structures, i.e. the special-purpose trust structure ("SPT Structure") and the asset-backed specific plan structure ("ABSP Structure", before 2014, namely the specific asset management plan structure ("SAMP Structure")).

SPT Structure − the SPT Structure is broadly used by financial institutions under the jurisdiction of the CBRC (particularly, banks and auto finance companies) to package their credit portfolio into asset-backed securities traded in the National Inter-bank Bond Market ("NIBBM"). In 2005, credit portfolio asset securitisation started with the successful debut of two pilot transactions launched, respectively, by the China Development Bank ("CDB") and the China Construction Bank ("CCB"). These two deals were made possible after years of joint efforts by multiple government bodies led by the CBRC and the PBOC. Upon closing of the first two pilot transactions, the PBOC and the CBRC jointly issued the *Administrative Measures on Pilot Projects for Securitisation of Credit Assets Procedures* on 20 April 2005. In addition, the CBRC further released the *Measures for the Supervision and Administration on Pilot Securitisation Projects of Credit Assets of Financial Institution* to set out detailed requirements and procedures for the ABS products with an SPT Structure. After a series of legal frameworks had been well set up, the CBRC issued another round of pilot approvals for securitisation projects across a range of underlying asset pools including residential mortgages, auto loans,

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SME loans and non-performing loans. By the end of 2008, 11 banks and financial institutions issued ABS in the two rounds of approvals, with a total value of RMB 67 billion. On 17 May 2012, the PBOC, the CBRC and the Ministry of Finance ("MOF") released the *Notice on Matters Regarding Further Expansion of Credit Asset Securitisation Pilot Projects* ("Pilot Notice"), whereby the Chinese regulators announced a quota of RMB 50 billion for this new round of credit assets securitisation transactions in the PRC. Pursuant to the Pilot Notice, no re-securitisation or complex synthetic products will be encouraged by the regulatory authorities, the senior tranche of ABS have to be reviewed and rated by at least two credit rating agencies, and the originators are now required to retain a certain portion of the junior tranche (in principle, no less than 5% of the total issued securities). Furthermore, the investment by one single investor should be capped within 40% of the total issuance. Pursuant to the *Circular Concerning the Filing Process of Securitization of Credit Assets* which was promulgated by CBRC on 20 November 2014, and the public announcement which was promulgated by the PBOC on 6 April 2015, the approval from CBRC is not required for relevant financial institutions anymore and has been replaced with a filing procedure with CBRC while the approval from PBOC has been replaced by a registration procedure, which both imply a loose regulatory trend in this field. The regulatory authorities of such SPT Structure are PBOC and CBRC.

SAMP Structure/ABSP Structure − Running in parallel with the ABS under SPT Structure (which is designed specifically for financial institutions), the SAMP Structure was brought to the PRC market in May 2005 under an interim rule, *Administrative Measures for Securitisation Business by Securities*, constituted by the China Securities Regulatory Commission ("CSRC"), the regulator of such structure. Furthermore, on 15 March 2013, CSRC further released the *Administrative Measures on Securitisation Business of a Securities Company* ("SAMP Rules"). Pursuant to the SAMP Rules, a securities firm launches a SAMP to issue certificates in the stock exchange (i.e., Shanghai Stock Exchange and Shenzhen Stock Exchange) to raise funds from investors. Upon completion of the offering, the SAMP will invest the proceeds in return for a specific, predominantly corporate asset with a sustainable and predicable cash flow. The scheme provides a return to the investors through a dedicated bank account. Similarly to a typical securitisation transaction, under the SAMP structure, cash flows from the asset will be the main source for repayment of principal and interest to investors. For credit enhancement, the external guarantor or liquidity supporter will be on standby and top up the cash flow or provide certain liquidity facilities in case of any shortfall. On 19 November 2014, the CSRC promulgated the *Administrative Measures on Securitisation Business of a Securities Company and Subsidiary of Fund Management Company,* together with the *Information Disclosure Guidance and Due Diligence Guidance* thereto, which has replaced the SAMP Rules and broadened the subject which could launch ABSP from a securities firm to securities firms and the subsidiary of fund management companies. Similar to the reform of the SPT Structure regime, the approval from CSRC has been cancelled and now the manager of ABSP shall instead perform the filing obligation with the Asset Management Association of China with the local bureau of CSRC copied. Apart from that, the scope of secondary market for the transfer of notes under ABSP has now been extended to the relevant Stock Exchange, National SME Share Transfer System, Interagency Quotation and Service System of Private Placement Product and OTC market, which is in line with the secondary market of corporate bonds.

7.2 Securitisation Entities. Does your jurisdiction have laws specifically providing for establishment of special purpose entities for securitisation? If so, what does the law provide as to: (a) requirements for establishment and management of such an entity; (b) legal attributes and benefits of the entity; and (c) any specific requirements as to the status of directors or shareholders?

Other than the trust scheme for SPT Structure and the asset-backed specific plan for ABSP Structure, PRC law is silent on the set-up of a special purpose vehicle in other forms for securitisation.

SPT Structure − the trust plan as a special purpose trust will be used as a vehicle to hold the legal title to the underlying assets, which constitute the trust assets. The SPT managed by the trustee (i.e. the CBRC-regulated trust company) is not a legal person under PRC law and the disposal and utilisation of all the trust assets will be managed in the name of the trustee. There is no corporate governance requirement in respect of the SPT. For the decision-making procedure, the trust document will usually specify the matters and circumstances subject to the approval of all or majority beneficiaries; the rest will be at the discretion of the trust company in a fiduciary capacity.

ABSP Structure – as with the SPT structure, the specific asset management plan is also not recognised as a legal person under PRC law. When setting up the ABSP, the investor entrusted the money into the ABSP, and the securities house or the subsidiary of the fund manager as manager of the ABSP will utilise the raised money to invest in the underlying asset. In comparison with the SPT, ABSP is less advanced in terms of legal integrity, tax neutrality and accounting clarity, a situation which in turn might affect its ability to achieve true sale and bankruptcy remoteness.

7.3 Location and form of Securitisation Entities. Is it typical to establish the special purpose entity in your jurisdiction or offshore? If in your jurisdiction, what are the advantages to locating the special purpose entity in your jurisdiction? If offshore, where are special purpose entities typically located for securitisations in your jurisdiction? What are the forms that the special purpose entity would normally take in your jurisdiction and how would such entity usually be owned?

Please see our answer to question 7.3. No offshore special purpose entity is involved in China markets.

7.4 Limited-Recourse Clause. Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) limiting the recourse of parties to that agreement to the available assets of the relevant debtor, and providing that to the extent of any shortfall the debt of the relevant debtor is extinguished?

A limited-recourse clause is an enforceable contractual arrangement under PRC law.

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7.5 Non-Petition Clause. Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) prohibiting the parties from: (a) taking legal action against the purchaser or another person; or (b) commencing an insolvency proceeding against the purchaser or another person?

PRC laws do not expressly prohibit or restrict non-petition clauses, and we believe a court would impose enforceable obligations on a party who makes a non-petition undertaking. However, there is a theoretical argument whether the rights of a claim conferred upon by the PRC laws and regulations may not be waived by the provisions contained in the agreement, and to our knowledge, such non-petition clause has not been tested in a PRC court.

7.6 Priority of Payments "Waterfall". Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) distributing payments to parties in a certain order specified in the contract?

A PRC court will generally give effect to a contractual provision on payment distribution based on the principle of freedom of contract.

7.7 Independent Director. Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) or a provision in a party's organisational documents prohibiting the directors from taking specified actions (including commencing an insolvency proceeding) without the affirmative vote of an independent director?

A PRC court generally may give effect to a contractual provision, or a provision in a party's organisational documents, prohibiting the directors from taking specified actions without the affirmative vote of an independent director. However, in the PRC, the shareholder can convene a shareholding meeting to decide the filing of bankruptcy of the company without any proposal from board level. As such, the independent director's vote cannot block the resolution of shareholders in respect of bankruptcy filing.

7.8 Location of Purchaser. Is it typical to establish the purchaser in your jurisdiction or offshore? If in your jurisdiction, what are the advantages to locating the purchaser in your jurisdiction? If offshore, where are purchasers typically located for securitisations in your jurisdiction?

Subject to the answer to question 7.2 above regarding the establishment of the special purpose entities for securitisation, neither the SPT as to SPT Structure nor the specific asset management plan as to ABSP Structure is recognised as a legal person under PRC laws.

SPT Structure – The SPT itself is not a legal person but merely a trust plan under a trust company. Under PRC laws, a trustee has to be a CBRC-regulated trust company which is established under the PRC law. Currently, PRC trust companies are not able to establish offshore trust plans.

ABSP Structure – The ABSP itself is not a legal person but a bundle of contractual rights over the underlying assets. All the relevant agreements are entered into by the securities company or the subsidiary of fund manager on behalf of the ABSP, and all the qualified securities companies or subsidiaries of fund management companies which are allowed to be managers of ABSP are incorporated in the PRC.

In short, current PRC securitisation regimes (SPT Structure and ABSP Structure) only allow onshore purchasers, except that foreign investors with the qualification of Qualified Foreign Institutional Investor can participate in SPT Structure products traded in the inter-bank market.

8 Regulatory Issues

8.1 Required Authorisations, etc. Assuming that the purchaser does no other business in your jurisdiction, will its purchase and ownership or its collection and enforcement of receivables result in its being required to qualify to do business or to obtain any licence or its being subject to regulation as a financial institution in your jurisdiction? Does the answer to the preceding question change if the purchaser does business with more than one seller in your jurisdiction?

Merely owning receivables and collecting and enforcing receivables, even purchasing from more than one seller, will not result in an offshore purchaser being subject to financial licence requirements.

Notwithstanding the above, if the purchaser is to establish a business existence in the PRC for a receivables purchase business, pursuant to the relevant regulations issued by the Ministry of Finance in 2012, it may be deemed as engaging in a commercial factoring business, which will in turn give rise to approval from the Ministry of Finance. For the reader's information, currently the foreign investment in commercial factoring is still under trial, and foreign invested commercial factoring companies are only allowed to be established in Guangzhou, Shanghai, Shenzhen, Tianjin, and particular regions of Chongqing, Jiangsu, Jiangxi and Suzhou.

8.2 Servicing. Does the seller require any licences, etc., in order to continue to enforce and collect receivables following their sale to the purchaser, including to appear before a court? Does a third-party replacement servicer require any licences, etc., in order to enforce and collect sold receivables?

The seller may, without any licence, continue to enforce and collect receivables after the completion of the sale to the purchaser.

A third party replacement servicer may or may not require any licence to enforce and collect sold receivables, depending on the nature of the underlying assets.

8.3 Data Protection. Does your jurisdiction have laws restricting the use or dissemination of data about or provided by obligors? If so, do these laws apply only to consumer obligors or also to enterprises?

The *PRC Contract Law* requires parties to a contract to act in good faith and perform obligations such as maintaining confidentiality in accordance with the nature and purpose of the contract and/or trade usage. Parties to the contracts must comply with this general principle of confidentiality.

The *Interim Provisions on the Protection of Trade Secrets of Central Enterprises*, promulgated by the State-owned Assets Supervision and Administration Commission on 25 March 2010, classifies customer information as one of the trade secrets owned by the central State-owned enterprises. It also requires such enterprises to

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enter into a confidentiality agreement with the counterparty when dealing with customer information and other trade secrets.

Where the seller is a financial institution licensed by CBRC, the seller will be subject to general confidentiality requirements applicable to financial institutions. In particular, pursuant to a notice issued by the PBOC in 2011 (YIN FA 2011 No. 17), banking institutions in the PRC are not allowed to provide any information regarding individual consumers to any offshore entities or individuals.

8.4 Consumer Protection. If the obligors are consumers, will the purchaser (including a bank acting as purchaser) be required to comply with any consumer protection law of your jurisdiction? Briefly, what is required?

Please see our answer to question 1.2 above.

8.5 Currency Restrictions. Does your jurisdiction have laws restricting the exchange of your jurisdiction's currency for other currencies or the making of payments in your jurisdiction's currency to persons outside the country?

Yes, the PRC imposes strict controls on both convertibility and transferability of the RMB, which is mainly governed by *PRC Foreign Exchange Regulations* and various rules and notices issued by the SAFE (and PBOC).

8.6 Risk Retention. Does your jurisdiction have laws or regulations relating to "risk retention"? How are securitisation transactions in your jurisdiction usually structured to satisfy those risk retention requirements?

Under SPT Structure, the originator is required to retain risk by holding at least 5% of the notes issued and at least 5% of the subordinated notes issued.

8.7 Regulatory Developments. Have there been any regulatory developments in your jurisdiction which are likely to have a material impact on securitisation transactions in your jurisdiction?

In June 2017, the Ministry of Finance, PBOC and CSRC jointly issued a circular to promote the securitisation transactions by project companies engaging in public private partnership projects. In January 2018, CBRC issued a circular on the administration of entrustment loans which will have an impact on the securitisation transactions structured through such loans.

9 Taxation

9.1 Withholding Taxes. Will any part of payments on receivables by the obligors to the seller or the purchaser be subject to withholding taxes in your jurisdiction? Does the answer depend on the nature of the receivables, whether they bear interest, their term to maturity, or where the seller or the purchaser is located? In the case of a sale of trade receivables at a discount, is there a risk that the discount will be recharacterised in whole or in part as interest? In the case of a sale of trade receivables where a portion of the purchase price is payable upon collection of the receivable, is there a risk that the deferred purchase price will be recharacterised in whole or in part as interest? If withholding taxes might apply, what are the typical methods for eliminating or reducing withholding taxes?

PRC withholding taxes may be imposed depending on the nature of the receivables and the location of the seller and purchaser. For example, pursuant to the *Enterprise Income Tax Law of the PRC* ("EIT Law") and its implementation rules, interest income derived from treasury bonds issued by the Ministry of Finance under the State Council of the PRC is exempt from EIT. Additionally, pursuant to the *Announcement on Exemption of Income Tax Levied on Interest from Local Government Bonds* (*Cai Shui* [2013] No. 5), enterprises are exempt from EIT on interest income derived from local government bonds issued in 2012 and thereafter.

Interests and royalties (including also royalties for the use of industrial and commercial equipment) sourced from the PRC and derived by a seller or purchaser being a non-tax resident will generally be subject to a withholding tax at the rate of 10%. The tax rate may be reduced or exempted by the applicable double tax treaty or other relevant documents. The obligors are obliged to withhold and settle the withholding tax with the PRC tax authority for the seller or purchaser.

Provided that the seller or the purchaser is domestically incorporated, there would be no PRC withholding taxes imposed on the payment on receivables made by a PRC obligor to the seller or purchaser.

The risk needs to be evaluated on a case-by-case basis and largely depends on the discretion of the relevant tax authorities.

The tax rate may be reduced or exempted by the applicable double tax treaty or special tax arrangements. For example, if a non-resident enterprise is a resident of Hong Kong, pursuant to the *Agreement between the Mainland of China and the Hong Kong Special Administrative Region for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Incomes* promulgated on 21 August 2016 by the State Administration of Taxation, such tax rate of interests and royalties mentioned above is reduced to 7% from 10%.

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9.2 Seller Tax Accounting. Does your jurisdiction require that a specific accounting policy is adopted for tax purposes by the seller or purchaser in the context of a securitisation?

There is no express accounting policy in the PRC adopted by the seller and purchaser for tax purposes in the context of a securitisation. The seller shall comply with the *China Accounting Standard for Enterprise* No. 23 – Derecognition of Financial Assets ("CAS No. 23"). CAS No. 23 was published by the MOF in 2006 and replaced the former circular *Accounting Provisions of Credit Assets Securitisation*.

Pursuant to the *Circular of Relevant Taxation Policy Issues Relevant to the Securitisation of Credit Assets* (*Caishui* [2006] No. 5), the originator shall realise its gains and losses derived from the sales of credit assets in a securitisation of credit assets in accordance with the EIT Law and settle the EIT accordingly.

9.3 Stamp Duty, etc. Does your jurisdiction impose stamp duty or other transfer or documentary taxes on sales of receivables?

The sale of receivables does not fall into the categories of taxable transactions, and thus will not be subject to any Stamp Duty or other transfer or documentary taxes on sales of receivables.

9.4 Value Added Taxes. Does your jurisdiction impose value added tax, sales tax or other similar taxes on sales of goods or services, on sales of receivables or on fees for collection agent services?

The sales of taxable goods and the provision of labour services in relation to the processing of goods and of repair and replacement services within the PRC are subject to Value Added Tax ("VAT"). The VAT rate ranges from 0% to 17%. The standard rate is 17%.

Business Tax ("BT") applies to the provision of services (excluding processing services and the repair and replacement services). It also applies to the transfer of intangible assets such as goodwill, patents and the sale of real estate properties in the PRC. BT rates range from 3% to 20%. BT and VAT are mutually exclusive.

The service fee received by the collection agent shall generally be subject to BT. Normally, the sales of receivables are not taxable with regard to both VAT and BT. However, the MOF and State Administration of Taxation jointly issued two circulars in 2011, officially kicking off the transformation of BT to VAT ("Transformation") for the service industry. Pursuant to the two circulars, depending on the nature of the receivables, certain categories of services previously imposed by BT may now be subject to VAT (e.g. the financial leasing sector). Thus, the sales of receivables in relation to such services technically may also be subject to VAT. Given the Transformation is still in a state of flux, the practice of turnover tax implications of the sales of receivables may vary in different locations.

9.5 Purchaser Liability. If the seller is required to pay value-added tax, stamp duty or other taxes upon the sale of receivables (or on the sale of goods or services that give rise to the receivables) and the seller does not pay, then will the taxing authority be able to make claims for the unpaid tax against the purchaser or against the sold receivables or collections?

If the tax authority deems the sale of receivables to be taxable from the VAT perspective under the new VAT scheme after the Transformation, the seller would be the taxpayer and shall undertake the obligations of filing and settling the VAT. It is not likely that the tax authority would be able to claim unpaid taxes against the purchaser or against the sold receivables, unless the receivables are considered by the tax authority to have been sold with no consideration or with an unreasonable price, under which the tax authority is entitled to petition a court to revoke such sale of receivables.

9.6 Doing Business. Assuming that the purchaser conducts no other business in your jurisdiction, would the purchaser's purchase of the receivables, its appointment of the seller as its servicer and collection agent, or its enforcement of the receivables against the obligors, make it liable to tax in your jurisdiction?

Pursuant to the EIT Law, if the purchaser is not a PRC resident for tax purposes, it is taxed only on its PRC and foreign-sourced income which is attributable to their establishments or places of business in the PRC, which shall be assessed depending on various factors (including the nature of receivables, the activities undertaken by the purchaser in the PRC, etc.). If there is a double tax treaty between the PRC and the country (or region) where the purchaser is located, the provisions of such treaty shall prevail.

Assuming the purchaser is located outside the PRC, generally the purchaser will not be liable to tax in the PRC from the EIT perspective provided that: (i) its activities are limited only to purchasing receivables, appointing the seller as its servicer and collection agent, or enforcing against the obligors; and (ii) it conducts no other business in the PRC, unless such activities undertaken by the purchaser constitute a permanent establishment as prescribed by the applicable double tax treaty. Please refer to questions 9.3 and 9.4 above for the implications of turnover taxes and Stamp Duty.

9.7 Taxable Income. If a purchaser located in your jurisdiction receives debt relief as the result of a limited recourse clause (see question 7.3 above), is that debt relief liable to tax in your jurisdiction?

Pursuant to the *Notice on the Work of Annual Report of Year 2008 on the Implementation of Accounting Standards Enterprises* (*Caihuihan* [2008] No. 60) issued by the Ministry of Finance, debt exemptions accepted by an enterprise, which meet the conditions for recognition in accordance with the provisions of the accounting standards, should normally be recognised as current income and therefore are subject to EIT.

If the debt relief as the result of a limited recourse clause meets the conditions for recognition in accordance with the provisions of the accounting standards, such relief shall be subject to EIT.

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England & Wales

Rupert Wall

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Roisin Nagle

1 Receivables Contracts

1.1 Formalities. In order to create an enforceable debt obligation of the obligor to the seller: (a) is it necessary that the sales of goods or services are evidenced by a formal receivables contract; (b) are invoices alone sufficient; and (c) can a binding contract arise as a result of the behaviour of the parties?

With the exception of certain debts arising under regulated consumer credit arrangements and contracts for sale of land (or interests therein), debts need not be in writing to be enforceable against obligors. Contracts may be written, oral, or partly written and partly oral provided the key elements to form a contract coincide. An invoice may itself represent, or evidence a debt arising pursuant to, a contract between parties. Where a contract is oral, evidence of the parties' conduct is admissible to ascertain the terms of such contract. A contract may also be implied between parties based on a course of conduct or dealings where the obligations arising from the alleged implied contract are sufficiently certain to be contractually enforceable.

1.2 Consumer Protections. Do your jurisdiction's laws: (a) limit rates of interest on consumer credit, loans or other kinds of receivables; (b) provide a statutory right to interest on late payments; (c) permit consumers to cancel receivables for a specified period of time; or (d) provide other noteworthy rights to consumers with respect to receivables owing by them?

Consumer credit in the UK is regulated under three regimes:

(a) the residential mortgage regime, which governs regulated mortgage activities with respect to mortgages secured by a first charge loan, which (from 21 March 2016) has been expanded to include second charge mortgages;

(b) the consumer credit regime, which covers unsecured credit facilities and (prior to 21 March 2016, subject to certain exemptions) secured loans not covered by the regulated residential mortgage regime; and

(c) the consumer buy-to-let (the **CBTL**) regime, which governs secured (first or second charge) and unsecured forms of consumer credit agreements entered into on or after 21 March 2016 relating to property that will in part, or whole, be occupied as a dwelling on the basis of a rental agreement.

Both residential mortgage contracts and consumer credit agreements are regulated by the Financial Conduct Authority (the **FCA**) under the Financial Services and Markets Act 2000 (the **FSMA**) and its secondary legislation, in particular the Financial Services and Markets Act 2000 (Regulated Activities Order) 2001 (the **RAO**). Additionally, consumer credit agreements are also regulated by the Consumer Credit Act 1974 (the **CCA**). Consumer buy-to-let mortgages are regulated by the FCA under the Mortgage Credit Directive Order 2015 (SI 2015/910) (the **MCD Order**).

(a) Other than in the context of high-cost, short-term loans (discussed below), there are no usury laws in the UK capping the rates of interest that can be charged under regulated residential mortgages or consumer credit loans. However, in the case of high-cost, short-term loans, the FCA has introduced a "cap" on interest and other charges levied by lenders under such loans (broadly, unsecured credit agreements where the borrower must repay, or substantially repay, credit advanced within a maximum of 12 months from such advance and for which the annualised percentage rate of interest is 100% or more). This "cap" on the cost of credit for such loans has three components:

  (i) "total cost cap": the total interest, fees and charges payable by the borrower must not exceed 100% of the amount borrowed;

  (ii) "initial cost cap": interest and other charges payable by the borrower must not exceed 0.8% per day of the outstanding principal during the agreed loan duration and any refinancing; and

  (iii) "default fee cap": default fees must not exceed £15.

  In November 2016, the FCA published a "call for input" in order to review the high-cost short-term price cap. Following this call for input, the FCA decided, in July 2017, to maintain the price cap at its current level with a commitment to review the cap again within three years to ensure that it remains effective.

(b) There is no statutory prohibition regarding interest on late payments in respect of regulated mortgage contracts or consumer credit agreements. However, all FCA regulated entities are subject to the principle that a firm must pay due regard to the interests of its customers and treat them fairly. With this in mind, under the FCA's conduct of business sourcebooks with respect to regulated mortgage contracts (**MCOB**) and consumer credit agreements (**CONC**), a lender may only levy charges in relation to a borrower's default or arrears that are necessary to cover its reasonable costs.

(c) Under a regulated consumer credit agreement (an **RCA**), there are two forms of withdrawal rights that may apply to that RCA. The requirements are complex and vary between different categories of RCAs, but in summary:

  (i) except in the case of an excluded agreement, borrowers may withdraw from an RCA within 14 days of the "effective date", subject to any outstanding interest and

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principal being repaid within 30 days of withdrawal. The effective date is most commonly the date of execution of the RCA; and

(ii) borrowers under unsecured excluded agreements that are deemed "cancellable agreements" under section 67 of the CCA have a minimum five-day cooling off period during which the RCA is cancellable by the borrower. For these purposes, an excluded agreement includes an agreement under which the amount borrowed exceeds a certain statutory limit (being £60,260 at the time of writing). The conditions as to whether an agreement is deemed "cancellable" are complex and should be considered carefully in the context of section 67 of the CCA.

From 21 March 2016 onwards, mortgage lenders under regulated mortgage contracts have been required to make a binding offer and give borrowers a reflection period of at least seven days to consider it. During this time the offer is binding on the lender, not the borrower.

(d) Terms in residential mortgage contracts and consumer credit agreements which are deemed to be unfair, or which are entered into as a result of unfair trading practices, will be deemed unenforceable against the consumer (see question 8.4). It should be noted that residential regulated mortgage contracts and consumer credit agreements may also be rendered unenforceable in other circumstances, including if they are made:

(i) by a lender who is not authorised by the FCA;

(ii) by a lender authorised by the FCA, but without permission to carry on certain credit-related activities (including servicing);

(iii) by a lender authorised by the FCA, but where the regulated mortgage contract or consumer credit agreement has been introduced via a third party who is either not authorised by the FCA or does not have permission to carry on certain credit related activities; and

(iv) in the case of an RCA, in circumstances where the agreement has not been documented and/or executed in compliance with the CCA and a court declines to make an enforcement order with respect to it.

1.3 Government Receivables. Where the receivables contract has been entered into with the government or a government agency, are there different requirements and laws that apply to the sale or collection of those receivables?

Not specifically, although there may be enforcement issues due to laws pertaining to sovereign immunity.

2 Choice of Law – Receivables Contracts

2.1 No Law Specified. If the seller and the obligor do not specify a choice of law in their receivables contract, what are the main principles in your jurisdiction that will determine the governing law of the contract?

For contracts entered into on or after 17 December 2009, the position is governed by Regulation 593/2008/EC of 17 June 2008 (**Rome I**). For contracts entered into prior to 17 December 2009, a different regime applied.

Under Rome I, absent a choice of governing law by the parties, and subject to specific rules governing contracts of carriage, consumer contracts, insurance contracts and individual employment contracts, the law governing the contract is determined in four stages. First, Rome I sets out rules in relation to specific types of contracts. For example, that a contract for the sale of goods is governed by the law of the country where the seller has their habitual residence. Second, if the governing law cannot be determined by reference to the specific rules, then the contract is governed by the law of the country where the party required to effect the characteristic performance of the contract has their habitual residence. However, if it is clear that the contract is manifestly more closely connected with a country other than that determined in accordance with the first two stages, then the law of that other country applies. Finally, if the governing law is not determined by the first three stages, then the contract is governed by the law of the country with which the contract is most closely connected.

2.2 Base Case. If the seller and the obligor are both resident in your jurisdiction, and the transactions giving rise to the receivables and the payment of the receivables take place in your jurisdiction, and the seller and the obligor choose the law of your jurisdiction to govern the receivables contract, is there any reason why a court in your jurisdiction would not give effect to their choice of law?

No, there is not.

2.3 Freedom to Choose Foreign Law of Non-Resident Seller or Obligor. If the seller is resident in your jurisdiction but the obligor is not, or if the obligor is resident in your jurisdiction but the seller is not, and the seller and the obligor choose the foreign law of the obligor/seller to govern their receivables contract, will a court in your jurisdiction give effect to the choice of foreign law? Are there any limitations to the recognition of foreign law (such as public policy or mandatory principles of law) that would typically apply in commercial relationships such as that between the seller and the obligor under the receivables contract?

Rome I stresses the importance of parties' freedom to choose the law of their contract (including a foreign law). Such choice may be expressed or implied. Rome I does, however, restrict the effect of the choice parties make as follows: (i) where all elements relevant to the contract (other than the choice of law) are located in a country other than the country whose law has been chosen by the parties and that country has rules which cannot be derogated from by agreement (in which case the court will apply those rules); (ii) where all elements relevant to the contract (other than the choice of law) are located in one or more EU Member States, the parties' choice of applicable law other than that of a Member State shall not prejudice the application of provisions of EU law which cannot be derogated from by agreement; (iii) to the extent that the law chosen conflicts with overriding mandatory rules of English law (as the law of the forum); (iv) where the applicable foreign law is manifestly incompatible with English public policy; or (v) where the overriding mandatory rules of the country where the obligations arising out of the contract have to be or have been performed render performance of the contract unlawful. When giving effect to any such choice of foreign law, the courts of England and Wales will consider and rule upon the substantive effects of such foreign law as matters of expert evidence.

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3 Choice of Law – Receivables Purchase Agreement

3.1 Base Case. Does your jurisdiction's law generally require the sale of receivables to be governed by the same law as the law governing the receivables themselves? If so, does that general rule apply irrespective of which law governs the receivables (i.e., your jurisdiction's laws or foreign laws)?

As discussed above, under Rome I (subject to the limited exceptions described in question 2.3) the parties to a contract are free to agree that the contract be governed by the law of any country, irrespective of the law governing the receivables. The law governing the sale agreement, together with mandatory rules of the jurisdiction of the relevant forum and/or the country where the contract is performed, will govern the effectiveness of the sale between the seller and the purchaser, whilst the governing law of the receivables will govern perfection of that sale and the relationship between the purchaser and the underlying obligor.

3.2 Example 1: If (a) the seller and the obligor are located in your jurisdiction, (b) the receivable is governed by the law of your jurisdiction, (c) the seller sells the receivable to a purchaser located in a third country, (d) the seller and the purchaser choose the law of your jurisdiction to govern the receivables purchase agreement, and (e) the sale complies with the requirements of your jurisdiction, will a court in your jurisdiction recognise that sale as being effective against the seller, the obligor and other third parties (such as creditors or insolvency administrators of the seller and the obligor)?

In general this would be the case; however, as noted in question 2.3 above, there are limited circumstances where certain legal provisions of countries other than the country whose law was selected to govern the receivables purchase agreement may (but need not) be taken into account by English courts. For example, as noted in part (v) of the answer to question 2.3 above, the court may give effect to overriding mandatory rules of the jurisdiction in which the purchaser is located, if such rules render unlawful the performance of obligations under the contract which are to be performed in that foreign jurisdiction. As noted in the response to question 2.3 above, the courts of England and Wales will consider and rule upon the substantive effects of foreign law as matters of expert evidence.

3.3 Example 2: Assuming that the facts are the same as Example 1, but either the obligor or the purchaser or both are located outside your jurisdiction, will a court in your jurisdiction recognise that sale as being effective against the seller and other third parties (such as creditors or insolvency administrators of the seller), or must the foreign law requirements of the obligor's country or the purchaser's country (or both) be taken into account?

See questions 3.1 and 3.2 above. The court would respect the parties' choice of law to govern the receivables purchase agreement, subject to the restrictions noted at question 2.3 above. As noted above, the court may give effect to overriding mandatory rules of the jurisdiction in which the obligor or the purchaser or both are located, if such rules render unlawful the performance of obligations under the contract which are to be performed in such foreign jurisdiction(s).

3.4 Example 3: If (a) the seller is located in your jurisdiction but the obligor is located in another country, (b) the receivable is governed by the law of the obligor's country, (c) the seller sells the receivable to a purchaser located in a third country, (d) the seller and the purchaser choose the law of the obligor's country to govern the receivables purchase agreement, and (e) the sale complies with the requirements of the obligor's country, will a court in your jurisdiction recognise that sale as being effective against the seller and other third parties (such as creditors or insolvency administrators of the seller) without the need to comply with your jurisdiction's own sale requirements?

In assessing the validity of the receivables purchase agreement as between the seller and the purchaser, the English courts would apply the law of the receivables purchase agreement (in this case, the law of the obligor's country). When considering the perfection of the sale under the receivables purchase agreement, the English courts would apply the governing law of the receivables (in this case, also the law of the obligor's country) and consider and rule upon such perfection as a matter of expert evidence. However, as discussed in question 2.3 above, certain mandatory principles of the law of England and Wales (such as mandatory principles of insolvency law in the seller's insolvency) would not be capable of disapplication by the parties' choice of a foreign law. Further, the courts would not apply the parties' choice of a foreign law to the extent it conflicted with those mandatory principles, or was manifestly incompatible with public policy.

3.5 Example 4: If (a) the obligor is located in your jurisdiction but the seller is located in another country, (b) the receivable is governed by the law of the seller's country, (c) the seller and the purchaser choose the law of the seller's country to govern the receivables purchase agreement, and (d) the sale complies with the requirements of the seller's country, will a court in your jurisdiction recognise that sale as being effective against the obligor and other third parties (such as creditors or insolvency administrators of the obligor) without the need to comply with your jurisdiction's own sale requirements?

See questions 3.1 and 3.4 above. The English courts would recognise the sale as effective against the obligor as it complies with the requirements of the law governing the receivable (in this case the law of the seller's country). In addition, certain mandatory principles of the law of England and Wales may apply to govern the relationship between the purchaser and the obligor (such as mandatory principles of insolvency in the obligor's insolvency).

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3.6 Example 5: If (a) the seller is located in your jurisdiction (irrespective of the obligor's location), (b) the receivable is governed by the law of your jurisdiction, (c) the seller sells the receivable to a purchaser located in a third country, (d) the seller and the purchaser choose the law of the purchaser's country to govern the receivables purchase agreement, and (e) the sale complies with the requirements of the purchaser's country, will a court in your jurisdiction recognise that sale as being effective against the seller and other third parties (such as creditors or insolvency administrators of the seller, any obligor located in your jurisdiction and any third party creditor or insolvency administrator of any such obligor)?

See questions 3.1 to 3.5 above. The sale would be effective against the seller provided it complied with the perfection requirements of the governing law of the receivables (in this case, English law). In addition, certain principles of English law may apply to govern the relationship between the purchaser and the obligor and in any insolvency proceedings of the seller and/or obligor in England and Wales.

4 Asset Sales

4.1 Sale Methods Generally. In your jurisdiction what are the customary methods for a seller to sell receivables to a purchaser? What is the customary terminology – is it called a sale, transfer, assignment or something else?

The most common method of selling receivables is by way of assignment (which can be equitable or legal), novation (a transfer of both the rights and obligations) or by creating a trust over the receivables (coupled with a power of attorney). Creating a trust over the proceeds of the receivables or sub-participation (a limited recourse loan to the seller in return for the economic interest in the receivables) will not effect a sale.

An outright sale of receivables may be described as a "sale" or (subject to the considerations set out in question 4.9) a "true sale", a "transfer" or an "assignment". The term "true sale" usually connotes a sale not subject to recharacterisation as a secured loan or any clawback risk, an "assignment" most often indicates a transfer of rights, but not obligations, whilst the term "transfer" usually indicates a transfer of rights and obligations by novation. The term "security assignment" is often used to distinguish a transfer by way of security from an outright assignment.

4.2 Perfection Generally. What formalities are required generally for perfecting a sale of receivables? Are there any additional or other formalities required for the sale of receivables to be perfected against any subsequent good faith purchasers for value of the same receivables from the seller?

In order for an assignment of receivables to take effect in law, rather than equity, s.136 of the Law of Property Act 1925 (the **LPA**) provides that the assignment must be: (i) in writing and signed by the assignor; (ii) of the whole of the debt; (iii) absolute and unconditional and not by way of charge; and (iv) notified in writing to the person from whom the assignor would have been entitled to claim the debt. Where the sale of a receivable does not meet all of these requirements, it will take effect as an equitable assignment only and any subsequent assignment effected by the seller and notified to the obligor prior to the date on which the original assignment is notified to the obligor, will take priority.

A novation of receivables (pursuant to which both the rights and obligations are transferred) requires the written consent of the obligor as well as the transferor and transferee.

4.3 Perfection for Promissory Notes, etc. What additional or different requirements for sale and perfection apply to sales of promissory notes, mortgage loans, consumer loans or marketable debt securities?

The transfer requirements for promissory notes (and other negotiable instruments) are governed by the Bills of Exchange Act 1882, which provides that they are transferable by delivery (or delivery and endorsement).

Mortgage loans and their related mortgages may be transferred by assignment. With respect to a mortgage over real property in England and/or Wales, as well as the giving of notice, certain other formalities need to be complied with in order to effect a legal assignment; for example, registration of the transfer at H.M. Land Registry as required by the Land Registration Act 2002. Most residential mortgage securitisations are structured as an equitable assignment of mortgage loans and their related mortgages to avoid the burden of giving notice to the mortgagors and registering the transfer. However, until notice has been given and the formalities satisfied, the rights of an assignee of a mortgage may be adversely affected by dealings in the underlying property or the mortgage, as described in question 4.4 below.

See questions 8.1 to 8.4 below for specific regulatory requirements in relation to consumer loans.

Transfers of marketable securities in bearer form will be achieved by delivery or delivery and endorsement and, if in registered form, by registration of the transferee in the relevant register. Dematerialised marketable securities held in a clearing system and represented by book-entries may be transferred by debiting the clearing system account of the relevant seller and crediting the clearing system account of the purchaser (or, in each case, its custodian or intermediary).

Specific statutory requirements may also apply for assignments of receivables such as intellectual property rights and certain policies of insurance.

4.4 Obligor Notification or Consent. Must the seller or the purchaser notify obligors of the sale of receivables in order for the sale to be effective against the obligors and/or creditors of the seller? Must the seller or the purchaser obtain the obligors' consent to the sale of receivables in order for the sale to be an effective sale against the obligors? Whether or not notice is required to perfect a sale, are there any benefits to giving notice – such as cutting off obligor set-off rights and other obligor defences?

Assuming the receivable does not fall into a select category of contractual rights which are incapable of assignment (e.g. as a matter of public policy or because the rights are of a personal nature) then, in the absence of an express contractual prohibition or restriction on assignment, receivables may be assigned without notification to, or consent of, the obligor.

The absence of notice has certain implications as follows: (i) obligors may continue to discharge their debts by making payments to the seller (being the lender of record); (ii) obligors may set off claims

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against the seller arising prior to receipt by the obligors of the notice of assignment; (iii) a subsequent assignee of (or fixed chargeholder over) a receivable without notice of the prior assignment by the seller would take priority over the claims of the initial purchaser; (iv) the seller may amend the agreement governing the terms of the receivable without the purchaser's consent; and (v) the purchaser cannot sue the obligor in its own name (although this is rarely an impediment in practice).

4.5 Notice Mechanics. If notice is to be delivered to obligors, whether at the time of sale or later, are there any requirements regarding the form the notice must take or how it must be delivered? Is there any time limit beyond which notice is ineffective – for example, can a notice of sale be delivered after the sale, and can notice be delivered after insolvency proceedings have commenced against the obligor or the seller? Does the notice apply only to specific receivables or can it apply to any and all (including future) receivables? Are there any other limitations or considerations?

Whilst no particular form of notice is required, it must be in writing, given by the seller or the purchaser to the obligor, and must not be conditional. The notice does not need to give the date of the assignment, but to the extent that a date is so specified, it must be accurate. The main requirement is that the notice is clear that the obligor should pay the assignee going forward.

There is no specific time limit for the giving of notices set down in the LPA and notice can be given to obligors post-insolvency of the seller (including pursuant to an irrevocable power of attorney granted by the seller) or of the obligor. The giving of such notice should not be prohibited by English insolvency law, although failure to give notice will have the effects set out in question 4.4 above.

4.6 Restrictions on Assignment – General Interpretation. Will a restriction in a receivables contract to the effect that "None of the [seller's] rights or obligations under this Agreement may be transferred or assigned without the consent of the [obligor]" be interpreted as prohibiting a transfer of receivables by the seller to the purchaser? Is the result the same if the restriction says "This Agreement may not be transferred or assigned by the [seller] without the consent of the [obligor]" (i.e., the restriction does not refer to rights or obligations)? Is the result the same if the restriction says "The obligations of the [seller] under this Agreement may not be transferred or assigned by the [seller] without the consent of the [obligor]" (i.e., the restriction does not refer to rights)?

As a general matter, it is not possible under English law to transfer or assign the burden (i.e. obligations, as distinct from rights) under a contract without the consent of the obligor. Obtaining this consent constitutes a novation. A novation is not, strictly speaking, a transfer, but is the replacement of the old contract with an identical new contract between the new party and continuing party. Therefore, where a contract refers to the "assignment of an agreement", an English court would likely find that this refers either to a novation of the rights and obligations thereunder or an assignment of rights coupled with the sub-contracting of obligations from the purported assignor to the purported assignee.

As such, whilst the appropriate classification will ultimately be a question of construction on any given set of facts:

(a) the first restriction (an explicit restriction on transfer or assignment of rights or obligations) would likely be interpreted as prohibiting a transfer of receivables by the seller to the purchaser (absent consent);

(b) the second restriction (an explicit restriction on transfer or assignment, but no explicit reference to rights or obligations) would likely be interpreted in the same way provided that, at the time the receivables contract was entered into, the intention of the seller and the obligor was to restrict both the transfer of the performance of the receivables contract (e.g. the right to require performance of the receivables contract) as well as the transfer of any rights and/or obligations under that contract (e.g. accrued rights of action or rights to receive payments); and

(c) the third restriction (explicit restriction on transfer or assignment of obligations but no explicit reference to rights) is more likely to be viewed as permitting a transfer of receivables by the seller to the purchaser.

Notwithstanding the above, it should be noted that there have been recent legislative proposals in the UK aimed at prohibiting restrictions included in business contracts that prevent the assignment of receivables (subject to certain exceptions). The government is yet to publish final regulations implementing these measures.

See also questions 4.1 and 4.4 above and 4.7 below.

4.7 Restrictions on Assignment; Liability to Obligor. If any of the restrictions in question 4.6 are binding, or if the receivables contract explicitly prohibits an assignment of receivables or "seller's rights" under the receivables contract, are such restrictions generally enforceable in your jurisdiction? Are there exceptions to this rule (e.g., for contracts between commercial entities)? If your jurisdiction recognises restrictions on sale or assignment of receivables and the seller nevertheless sells receivables to the purchaser, will either the seller or the purchaser be liable to the obligor for breach of contract or tort, or on any other basis?

Restrictions on assignments or transfers of receivables are generally enforceable. If a contract is silent on assignability, then such contract and the receivables arising thereunder will be (with certain limited exceptions related to personal contracts where the specific identity of a contracting party goes to the heart of the contract, such as contracts of service) freely assignable. In very limited circumstances, such as upon the death of an individual or in certain limited statutory transfers, assignment may take place by operation of law, overriding an express contractual provision prohibiting assignment. It may be possible to utilise a trust arrangement where non-assignment provisions within contracts would otherwise prevent assignment.

If an assignment is effected in breach of a contractual prohibition on assignment, although ineffective as between the obligor and the seller (to whom the obligor can still look for performance of the contract), the prohibition will not invalidate the contract between the seller and purchaser if in compliance with the governing law and explicit terms of the receivables purchase agreement itself, such that the seller may still be liable to account to the purchaser for the obligor's payment; the seller may hold any such proceeds received on trust for the purchaser; the seller may subrogate the purchaser to its rights under the invoice due for payment by the obligor; and the seller may grant the purchaser a funded sub-participation in respect of the rights to receive payment of the relevant part of the receivable. Furthermore, if the seller can establish that the obligor has accepted the assignment either through its conduct or by waiver (for example, by course of dealing) then the obligor may be estopped from denying the assignment, even where there is a contractual prohibition on assignment.

See also questions 4.1, 4.4 and 4.6 above.

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4.8 Identification. Must the sale document specifically identify each of the receivables to be sold? If so, what specific information is required (e.g., obligor name, invoice number, invoice date, payment date, etc.)? Do the receivables being sold have to share objective characteristics? Alternatively, if the seller sells *all* of its receivables to the purchaser, is this sufficient identification of receivables? Finally, if the seller sells *all* of its receivables *other than* receivables owing by one or more specifically identified obligors, is this sufficient identification of receivables?

The sale document must describe the receivables (or provide for details of the receivables to be provided at the point of sale) with sufficient specificity that the receivables can be identified and distinguished from the rest of the seller's estate. For reasons relating to confidentiality and data protection law (see question 8.3 below), it is atypical for obligors' names to be included in the information provided to the purchaser.

4.9 Recharacterisation Risk. If the parties describe their transaction in the relevant documents as an outright sale and explicitly state their intention that it be treated as an outright sale, will this description and statement of intent automatically be respected or is there a risk that the transaction could be characterised by a court as a loan with (or without) security? If recharacterisation risk exists, what characteristics of the transaction might prevent the transfer from being treated as an outright sale? Among other things, to what extent may the seller retain any of the following without jeopardising treatment as an outright sale: (a) credit risk; (b) interest rate risk; (c) control of collections of receivables; (d) a right of repurchase/redemption; (e) a right to the residual profits within the purchaser; or (f) any other term?

A transaction expressed to be a sale will be recharacterised as a secured financing if it is found to be a "sham", i.e. if the documents do not represent the true intentions between the parties and are intended to mask the true agreement. Irrespective of the label given to a transaction by the parties, the court will look at its substance and examine whether it creates rights and obligations consistent with a sale.

Case law has established a number of key questions to be considered when concluding that a transaction is a sale rather than a secured financing:

1) Do the transaction documents accurately reflect the intention of the parties and are the terms of the transaction documents consistent with a sale as opposed to a secured financing?
2) Does the seller have the right to repurchase the receivables sold?
3) Does the purchaser have to account for any profit made on any disposition by it of the receivables?
4) Is the seller required to compensate the purchaser if it ultimately realises the acquired receivables for an amount less than the amount paid?

However, a transaction may still be upheld as a sale notwithstanding the presence of one or more of these factors. As a result, the intention of the parties, their conduct after the original contract, and the express terms of the contract are all factors a court will take into account, as a whole, when determining whether or not a contract is inconsistent with that of a sale.

The seller remaining the servicer/collection agent of the receivables post-sale, the seller entering into arm's length interest-rate hedging with the purchaser, the seller assuming some degree of credit risk by assuming a first loss position, the right of a seller to repurchase receivables in limited circumstances and the right of a seller to extract residual profits from the purchaser are not generally considered to be inherently inconsistent with sale treatment. The seller retaining an equity of redemption in respect of a transfer of receivables or retaining all risk and reward in the receivables may, however, lead a court to the conclusion that the transaction is a loan arrangement (with or without security) rather than an outright transfer.

If the sale is recharacterised as a financing, the assets "sold" will remain on the seller's balance sheet and the loan will be treated as a liability of the seller. In addition, given the practice in England and Wales not to make "back-up" security filings, the security may not have been registered and may, therefore, be void in a seller insolvency for lack of registration (subject to the application of the FCR as referred to and defined in question 5.3 below).

In addition to recharacterisation, sale transactions are also vulnerable under certain sections of the Insolvency Act 1986 (**Insolvency Act**) such as those relating to transactions at an undervalue and preferences.

4.10 Continuous Sales of Receivables. Can the seller agree in an enforceable manner to continuous sales of receivables (i.e., sales of receivables as and when they arise)? Would such an agreement survive and continue to transfer receivables to the purchaser following the seller's insolvency?

An agreement pursuant to which a seller agrees to sell receivables on a continuous basis prior to the occurrence of certain specified events will take effect, as between the seller and purchaser, as an agreement to assign. The receivables will be automatically assigned to the purchaser as and when they come into existence.

See the answer to question 6.5 below on the effect of an insolvency of the seller on an agreement to assign a receivable not yet in existence.

4.11 Future Receivables. Can the seller commit in an enforceable manner to sell receivables to the purchaser that come into existence after the date of the receivables purchase agreement (e.g., "future flow" securitisation)? If so, how must the sale of future receivables be structured to be valid and enforceable? Is there a distinction between future receivables that arise prior to *versus* after the seller's insolvency?

An assignment for value of an identifiable receivable, which is not in existence at the time of the receivables purchase agreement, but which will be clearly ascertainable in the future, is treated as an agreement to assign which will give rise to an equitable assignment of the receivable as soon as it comes into existence.

See the answer to question 6.5 below on the effect of an insolvency of the seller on an agreement to assign a receivable not yet in existence.

4.12 Related Security. Must any additional formalities be fulfilled in order for the related security to be transferred concurrently with the sale of receivables? If not all related security can be enforceably transferred, what methods are customarily adopted to provide the purchaser the benefits of such related security?

Security for a receivable will typically be capable of being assigned in the same manner as the receivable itself. The transfer or assignment

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of some types of security may require additional formalities such as registration or payment of a fee as referred to in question 4.3 above.

4.13 Set-Off; Liability to Obligor. Assuming that a receivables contract does not contain a provision whereby the obligor waives its right to set-off against amounts it owes to the seller, do the obligor's set-off rights terminate upon its receipt of notice of a sale? At any other time? If a receivables contract does not waive set-off but the obligor's set-off rights are terminated due to notice or some other action, will either the seller or the purchaser be liable to the obligor for damages caused by such termination?

Generally speaking, an obligor's right to set-off: (i) amounts owing to it from the seller; against (ii) amounts it owes to the seller, under that receivables contract will survive receipt of notice of a sale against the assignee of the receivables contract provided that the obligor's cross-debt arose before the obligor received notice of the sale. The assignee takes the benefit of the receivables contract subject to any rights of set-off in existence between the obligor and seller at the time the obligor receives notice of the sale.

If a cross-debt arises after the obligor has received notice of the sale, an obligor will generally be unable to set off such cross-debt against the purchaser unless the claims of the obligor and the purchaser are sufficiently closely connected.

An obligor's right to set-off under a receivables contract may terminate if the cross-debt becomes unenforceable or time-barred. In the absence of a breach of any provision to the contrary, it is unlikely that either the seller or the purchaser would be liable to the obligor for damages as a result of an obligor's rights of set-off terminating by operation of law.

4.14 Profit Extraction. What methods are typically used in your jurisdiction to extract residual profits from the purchaser?

Techniques that are typically used to extract profit from the purchaser include: paying the seller fees (for example, for acting as servicer and/or collection agent of the receivables or for acting as a swap counterparty); paying deferred purchase price or consideration to the seller for the receivables purchased; making repayments or interest payments to the seller in respect of subordinated loans granted by the seller; and/or the seller holding equity securities/ the most subordinated tranche of securities in the purchaser. The method of extracting the retained profit in any given securitisation will depend on a number of factors, including the nature of the assets in the securitised pool, the types of credit enhancement used, rating agency and timing considerations and the consequences to accounting, regulatory capital and tax treatment.

5 Security Issues

5.1 Back-up Security. Is it customary in your jurisdiction to take a "back-up" security interest over the seller's ownership interest in the receivables and the related security, in the event that an outright sale is deemed by a court (for whatever reason) not to have occurred and have been perfected (see question 4.9 above)?

It is not customary to create "back-up" security over a seller's ownership interest in receivables and related security when an outright sale is intended, although a seller may create a trust over the receivables in favour of the purchaser to the extent that any outright sale is held not to have occurred or is held to be void or is subsequently recharacterised.

5.2 Seller Security. If it is customary to take back-up security, what are the formalities for the seller granting a security interest in receivables and related security under the laws of your jurisdiction, and for such security interest to be perfected?

See questions 5.1 above and 5.3 below.

5.3 Purchaser Security. If the purchaser grants security over all of its assets (including purchased receivables) in favour of the providers of its funding, what formalities must the purchaser comply with in your jurisdiction to grant and perfect a security interest in purchased receivables governed by the laws of your jurisdiction and the related security?

Although security may be taken over receivables by way of novation, attornment, pledge (in the case of documentary receivables capable of being delivered) or by retention of title arrangements, security is most commonly taken over receivables by way of mortgage or charge.

Receivables assigned by way of security together with a condition for re-assignment on redemption or discharge of the underlying secured obligations will create a mortgage over the receivables which will either be legal (if the procedural requirements of the LPA identified in question 4.2 above are satisfied) or, in the absence of satisfaction of these requirements (or where the subject property is not currently owned or in existence), equitable in nature. Prior to the perfection of an equitable mortgage, the assignee's security will be subject to prior equities (such as rights of set-off and other defences), will be liable to take priority behind a later assignment granted over the same assets where the later assignee did not have notice of the earlier assignment and himself gives notice to the obligor, and the obligor will be capable of making good discharge of its debt by paying the assignor directly (see questions 4.4 and 4.5 above).

Alternatively, the receivables may be made the subject of a fixed or floating charge. In comparison to a mortgage (which is a transfer of title together with a condition for re-assignment on redemption), a charge is a mere encumbrance on the receivables, giving the chargee a preferential right to payment out of the fund of receivables in priority to other creditors in the event of liquidation or administration. A practical distinction between a mortgage and a charge over receivables is the inability of a chargee to claim a right of action in his own name against the obligor. In practice this distinction is diminished by including a right to convert the charge into a mortgage together with a power of attorney to compel transfer of the receivables to the chargee. Additionally, the statutory rights conferred by Section 101 of the LPA allowing the chargee to appoint a receiver in respect of charges created by deed and the other rights provided to holders of some "qualifying floating charges", provide further enforcement rights for a chargee.

The degree of priority given to a chargee depends on whether the charge is fixed or floating. Whilst definitive definitions have remained elusive, the hallmarks of a fixed charge are that it attaches to the ascertainable receivables over which it is subject immediately upon its creation (or upon the receivable coming into existence). In comparison, a floating charge is a present security over a class or fund of assets (both present and future) which, prior to the occurrence of a specified crystallisation event, can continue to be

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managed in the ordinary course of the chargor's business. On the occurrence of a specified crystallisation event the floating charge will attach to the assets then presently in the fund, effectively becoming a fixed charge over those assets. Case law emphasises control of the receivable as the determining factor in distinguishing between a fixed or floating charge whilst asserting that it is the substance of the security created, rather than how it is described or named, that is important.

The distinction is important: on an insolvency of the chargor, a fixed chargeholder will rank in priority to all unsecured claims, whilst a floating chargeholder will rank behind both preferential creditors and fixed chargeholders and equally with a statutory "prescribed part" (up to a maximum amount of £600,000) made available to unsecured creditors; a floating charge granted within 12 months (or 24 months if granted to a "connected" person) prior to the commencement of administration or liquidation will be void except as to new value given; and whereas a fixed chargeholder will obtain an immediate right over definitive assets which can only be defeated by a purchaser in good faith of the legal interest for value without notice of the existing charge (which, as summarised below, is uncommon to the extent that registration provides notice), in contrast, disposing of an asset subject to an uncrystallised floating charge will, apart from certain exceptions, generally result in the purchaser taking the receivables free of the charge.

For charges or mortgages created by an English company (or LLP) on or after 6 April 2013, there is a registration regime allowing (with some very limited exceptions) the chargor or anyone interested in the charge to register (in some cases electronically) the charge within 21 calendar days (beginning with the day following the creation of the charge) with the registrar of companies at the registry for companies incorporated in England and Wales (**Companies House**) by delivering a statement of particulars of that charge. This regime applies whether the charge is over an asset situated in or outside the UK. A different regime applies to charges created by English companies (or LLPs): (i) if the charge was created before 1 October 2009 (whereby the Companies Act 1985 (**CA 1985**) applies); and/or (ii) if the charge was created on and from 1 October 2009 but before 6 April 2013 (whereby the Companies Act 2006 (the **CA 2006**, and together with the CA 1985, the **Companies Act**) applies) under which regimes certain categories of charge had to be registered at Companies House.

For charges created by an overseas company over UK assets on or after 1 October 2011, there is no requirement to register such charges at Companies House. A different regime applies to charges created by an overseas company: (i) if the charge was created before 1 October 2009 (whereby the CA 1985 applies); and/or (ii) if the charge was created on and from 1 October 2009 to and on 30 September 2011 (whereby the CA 2006 and the Overseas Companies (Execution of Documents and Registration of Charges) Regulations 2009 applies).

Where certain security arrangements exist over financial collateral (cash, financial instruments and credit claims) between two non-natural persons, the Financial Collateral Arrangements (No. 2) Regulations 2003 (as amended, including pursuant to the Financial Markets and Insolvency (Settlement Finality and Financial Collateral Arrangements) (Amendment) Regulations 2010 that came into force in England and Wales on 6 April 2011) (the **FCR**) which implement EU Directive 2002/47/EC (the **EU Collateral Directive**) into English law, disapply certain statutory requirements in relation to that security arrangement (such as the requirement to register security at Companies House under the CA 2006 as well as certain provisions of English insolvency law). It should be noted, however, that the status of the FCR, as it applies to financial collateral arrangements in respect of which neither party falls within one of the categories referred to in the EU Collateral Directive, has been brought into doubt as a result of *obiter dicta* in the UK Supreme Court decision of *United States of America v Nolan* [2015] UKSC 63.

Except as noted above with regard to the FCR, failure to register a registrable charge within the prescribed statutory period will (both pre and post 6 April 2013) result in that security interest being void as against a liquidator, administrator or creditors in a liquidation or administration. As such, and notwithstanding the potential application of the FCR, mortgages and charges, whether or not clearly within the categories listed in the Companies Act or a financial collateral arrangement, are habitually registered at Companies House. As registration of a charge is a perfection requirement (and not a requirement for attachment of security), an unregistered charge will still be valid as against the chargor, provided the chargor is not in winding-up or administration. Similarly, registration under the Companies Act is not determinative as to priority such that, in the case of two competing charges, provided that both are registered within the statutory 21-day period after creation, the prior created charge will take priority over the subsequently created charge even where that prior charge is registered second.

5.4 Recognition. If the purchaser grants a security interest in receivables governed by the laws of your jurisdiction, and that security interest is valid and perfected under the laws of the purchaser's jurisdiction, will the security be treated as valid and perfected in your jurisdiction or must additional steps be taken in your jurisdiction?

Notwithstanding the choice of law governing the purchaser's security, the law governing the receivable itself will govern the proprietary rights and obligations between the security holder and the obligor and between the security granter and the security holder (including as to matters of validity, priority and perfection).

The relevant security must therefore be valid and perfected under the laws of England and Wales, as well as valid and perfected under the laws of the governing law of the security, in order for it to be given effect by the English courts. In addition, English courts will also apply certain mandatory rules of English law which may affect the validity of any foreign law-governed security created.

5.5 Additional Formalities. What additional or different requirements apply to security interests in or connected to insurance policies, promissory notes, mortgage loans, consumer loans or marketable debt securities?

Security over contractual rights under insurance policies is usually created by security assignment. Security over mortgage loans or consumer loans will be created by mortgage or charge. Creating security over the mortgage securing a mortgage loan is generally accomplished by equitable mortgage.

Security over marketable debt securities or negotiable instruments (including promissory notes and bearer debt securities) is a complicated area and the most appropriate form of security depends on whether the relevant securities are bearer or registered, certificated, immobilised (i.e. represented by a single global note) or dematerialised and/or directly-held or indirectly-held. In (brief) summary: (i) directly-held and certificated debt securities, where registered, may generally be secured by legal mortgage (by entry of the mortgagee on the relevant register) or by equitable mortgage or charge (by security transfer or by agreement for transfer or charge); (ii) security over bearer debt securities may be created by mortgage

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or pledge (by delivery together with a memorandum of deposit) or charge (by agreement to charge) and in certain limited circumstances a lien may arise; and (iii) security may be created over indirectly-held certificated debt securities by legal mortgage (by transfer, either to an account of the mortgagee at the same intermediary or by transfer to the mortgagee's intermediary or nominee via a common intermediary) or by equitable mortgage or charge (by agreement of the intermediary to operate a relevant securities account in the name of the mortgagor containing the debt securities to the order/control of the chargee).

The FCR (which removes certain requirements in relation to the creation and registration of security and disapplies certain rules of English insolvency law) will apply to any security which is a "financial collateral arrangement" involving "financial collateral". See question 5.3 above.

5.6 Trusts. Does your jurisdiction recognise trusts? If not, is there a mechanism whereby collections received by the seller in respect of sold receivables can be held or be deemed to be held separate and apart from the seller's own assets (so that they are not part of the seller's insolvency estate) until turned over to the purchaser?

Trusts over collections received by the seller in respect of sold receivables are recognised under the laws of England and Wales, provided that the trust is itself validly constituted.

5.7 Bank Accounts. Does your jurisdiction recognise escrow accounts? Can security be taken over a bank account located in your jurisdiction? If so, what is the typical method? Would courts in your jurisdiction recognise a foreign law grant of security taken over a bank account located in your jurisdiction?

English law recognises the concept of money held in a bank account in escrow. Security granted by a depositor for a third party is typically taken over the debt represented by the credit balance by way of charge or (provided the securityholder is not the same bank at which the cash is deposited) an assignment by way of security. Security over a credit balance granted in favour of the bank at which the deposit is held can only be achieved by way of charge (not by assignment) and is usually supplemented by quasi-security such as a flawed asset arrangement, a contractual right of set-off and/or a charge in favour of the bank over the depositor's claims for payment of the deposit. The more usual approach is for the parties to ensure that the bank holding the deposit is a separate entity from the beneficiary of the security interest in such deposit. To the extent that the security is a security financial collateral arrangement over cash, as provided for in the FCR, those regulations will apply. The security interest is habitually perfected by registration, as mentioned in question 5.3 above.

As an alternative, quasi-security may be created over a bank account by way of a trust structure pursuant to which a declaration of trust is made by the account holder (as trustee) who holds the cash deposits on trust for the beneficiary. Care must be taken that such a trust is both validly constituted and not recharacterised as a charge which is then void for non-registration.

Foreign law-governed security over a bank account located in England and Wales must be valid under the laws of England and Wales, as well as its own governing law, in order for it to be given effect by the English courts.

5.8 Enforcement over Bank Accounts. If security over a bank account is possible and the secured party enforces that security, does the secured party control all cash flowing into the bank account from enforcement forward until the secured party is repaid in full, or are there limitations? If there are limitations, what are they?

This is a complicated question that will depend upon (amongst other things) the nature of the security over the bank account (whether on its facts it is a fixed or floating charge or a security assignment and whether it is drafted to cover amounts on credit from time to time), whether there are any competing security interests or trust arrangements over the bank account, the extent of any commingling of cash in the bank account, whether any security interest is also a security financial collateral arrangement under the FCR and whether the account holder is the subject of insolvency proceedings. Where a security financial collateral arrangement under the FCR exists, the parties may agree that the collateral-taker can appropriate the financial collateral, giving the right to become the absolute owner of the collateral should the security become enforceable.

5.9 Use of Cash Bank Accounts. If security over a bank account is possible, can the owner of the account have access to the funds in the account prior to enforcement without affecting the security?

Any charge over a cash bank account is likely to be a floating charge rather than a fixed charge where the owner has access to the funds prior to enforcement because the chargee is unlikely to have sufficient control over the bank account in order to create a fixed charge. The ramifications of this distinction are set out in question 5.3 above.

Whether a floating charge over financial collateral qualifies as a security financial collateral arrangement under the FCR (with the advantages that this may bring to a chargeholder) remains uncertain. The issue relates to the level of rights a collateral provider can retain in order for a security financial collateral arrangement to exist (in particular there is uncertainty over the terms "possession", "control" and "excess financial collateral"). In 2015, the UK's Financial Markets Law Committee set out the impact of this uncertainty on the UK financial markets in a letter to HM Treasury. While a 2016 ruling by the European Court of Justice confirmed that a security financial collateral arrangement may exist over cash in a bank account, it did not clarify the uncertainty over the level of rights a collateral provider may retain. Therefore, in the absence of continued definitive judicial or legislatory clarification, each case must be taken on its particular facts.

6 Insolvency Laws

6.1 Stay of Action. If, after a sale of receivables that is otherwise perfected, the seller becomes subject to an insolvency proceeding, will your jurisdiction's insolvency laws automatically prohibit the purchaser from collecting, transferring or otherwise exercising ownership rights over the purchased receivables (a "stay of action")? If so, what generally is the length of that stay of action? Does the insolvency official have the ability to stay collection and enforcement actions until he determines that the sale is perfected? Would the answer be different if the purchaser is deemed to only be a secured party rather than the owner of the receivables?

Most formal insolvency procedures have an automatic stay of action

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against the insolvent entity. The stay will typically apply for the duration of the proceeding from the time it is effective, unless the court grants leave to lift the stay. An automatic interim moratorium applies between the instigation of administration proceedings and the company entering administration. However, on a winding-up petition, no interim moratorium applies until the court grants a winding-up order, unless a provisional liquidator is appointed.

If the right to the receivables has been transferred by legal assignment, the sale will be perfected, the purchaser will have the right to enforce his assigned rights in his own name and a stay of action on the insolvency of the seller should not affect the purchaser's ability to collect income from the receivables.

If the seller is appointed as servicer for the receivables, the stay of action may prevent the purchaser from taking action to enforce the servicing contract and any proceeds held by the servicer, other than in a binding trust arrangement, may be deemed to be the property of the servicer, not the purchaser.

If the receivables have been sold by equitable assignment and notice has not been given to an obligor, such obligor may continue to pay the seller. Typically, such proceeds will be subject to a trust in favour of the purchaser. If such a trust has not been imposed on the collections, the purchaser will be an unsecured creditor of the seller with respect to such collections.

6.2 Insolvency Official's Powers. If there is no stay of action, under what circumstances, if any, does the insolvency official have the power to prohibit the purchaser's exercise of its ownership rights over the receivables (by means of injunction, stay order or other action)?

Assuming the receivables have been sold by legal assignment or perfected equitable assignment, an insolvency official appointed over the seller would not be able to prohibit the purchaser's exercise of its ownership rights over the receivables, unless there had been fraud or another breach of duty or applicable law (such as the antecedent transaction regime described in question 6.3 below).

6.3 Suspect Period (Clawback). Under what facts or circumstances could the insolvency official rescind or reverse transactions that took place during a "suspect" or "preference" period before the commencement of the seller's insolvency proceedings? What are the lengths of the "suspect" or "preference" periods in your jurisdiction for (a) transactions between unrelated parties, and (b) transactions between related parties? If the purchaser is majority-owned or controlled by the seller or an affiliate of the seller, does that render sales by the seller to the purchaser "related party transactions" for purposes of determining the length of the suspect period? If a parent company of the seller guarantee's the performance by the seller of its obligations under contracts with the purchaser, does that render sales by the seller to the purchaser "related party transactions" for purposes of determining the length of the suspect period?

The insolvency official would need a court order to reverse an antecedent transaction, except for a disposition of property made after a winding-up petition has been presented (assuming a winding-up order is subsequently made). Such dispositions are void and, unless validated by a court order, any receivables purportedly transferred during that period would remain the property of the seller.

Otherwise, the court may set aside a transaction made at an undervalue in the two years ending with the commencement of the administration or liquidation (the **onset of insolvency**) if the company was, at that time, or as a result of the transaction became, unable to pay its debts (either as they fall due or on a balance sheet basis). This inability to pay debts is presumed where the transaction is with a connected person, unless proven otherwise. There is a defence if the court is satisfied that the company entered into the transaction in good faith with reasonable grounds for believing that it would benefit the company. If a transaction at an undervalue is done with the purpose of putting assets beyond the reach of creditors, there is no requirement to show the company was or became insolvent, and no time limit for bringing court proceedings.

A transaction which would put a creditor or guarantor of the seller into a better position than it would otherwise have been in a winding-up can be set aside by the court if such preference is made: (i) in the two years ending with the onset of insolvency (in the case of a preference to a person "connected" with the company); or (ii) in the six months ending with the onset of insolvency (in the case of any other preference). It is necessary to show that a preference was made with a desire to prefer the creditor or guarantor, though this need not be the dominant intention. The desire to prefer is presumed where the preference is with a "connected" person unless proved otherwise. As with a transaction at an undervalue, it is also necessary for a preference to have been made at a time when the company was unable to pay its debts, either as they fall due or on a balance sheet basis. Other transactions which can be challenged by liquidators or administrators are voidable floating charges and transactions to defraud creditors.

The seller and the purchaser will be "connected" persons if either of them has "control" of the other (in that the directors of one company (or of another company which has control of it) are accustomed to act in accordance with the instructions of the other company or that at least one-third of the voting power at any general meeting of one company (or of another company which has control of it) can be exercised by the other company). They will also be connected if they are both controlled by another company or by companies which are connected with each other. The seller and the purchaser will be connected persons if the purchaser is majority-owned or controlled by the seller or an affiliate of the seller. The transaction will not constitute a related party transaction if the parent company of the seller guarantees the performance by the seller of its obligations under contracts with the purchaser as the seller (and the parent company of the seller) and the purchaser are not connected persons.

6.4 Substantive Consolidation. Under what facts or circumstances, if any, could the insolvency official consolidate the assets and liabilities of the purchaser with those of the seller or its affiliates in the insolvency proceeding? If the purchaser is owned by the seller or by an affiliate of the seller, does that affect the consolidation analysis?

The equitable remedy of substantive consolidation, which permits the court to treat the assets and liabilities of one entity as though they were those of another, is not recognised by the English courts. Only in circumstances where the assets and liabilities of two companies were indistinguishably amalgamated together, and where to do so would be in the interests of both companies' creditors, might the court sanction an arrangement reached by the insolvency official and those creditors. There is no presumption that substantive consolidation would apply where the purchaser is owned by the seller or by an affiliate of the seller or is otherwise "connected" with the seller.

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It is a fundamental principle of English law that a company has a legal personality distinct from its shareholders (a "corporate veil") emanating from the House of Lords decision in *Salomon v A Salomon & Co Ltd* [1897] AC 22. The separate legal personality of a company will only be ignored in very limited circumstances. Examples include fraud, illegality, where a company is formed to evade contractual obligations or defeat creditors' claims or where an agency or nominee relationship is found to exist.

Securitisation transactions habitually attempt to minimise the risk of a court treating the assets of an SPV as those of an originator or other third-party seller to that SPV, or of a creditor or liquidator of a third party being found to have a claim on the SPV's assets, by ensuring (either structurally or contractually) that some or all of the following apply:

- There are no grounds for setting aside any transaction entered into between the SPV and another company under the Insolvency Act.
- The SPV has not given any surety or security for the obligations of another company.
- There are no grounds for holding that one company is a shadow director of the other and could be held to be liable for wrongful or fraudulent trading if the other company is in liquidation.
- No financial support direction or contribution notice could be issued under UK pensions legislation and the SPV is not jointly and severally liable with any other company under any relevant tax legislation.
- Corporate activities of the SPV are kept separate from those of other transaction parties, and constitutional and other decision-making formalities of the SPV (such as board minutes) are accurately kept and filed separately from those of any other party.
- There is limited or no pooling or intermingling of assets (with the SPV having segregated and/or ring-fenced bank accounts).
- The corporate veil is not used for improper or dishonest purposes (such as to conceal illegal activities, deception or evasion of certain SPV obligations).
- The SPV has, and holds itself out as having, a distinct, independent existence and can acquire and hold assets and carry on business in a manner separate to any other party (achieved, among other things, by the SPV conducting its business in its own name, paying debts out of its own funds and maintaining arm's length relationships with other parties).
- The SPV has independent directors or other management and produces separate (non-consolidated) accounts.

6.5 Effect of Insolvency on Receivables Sales. If insolvency proceedings are commenced against the seller in your jurisdiction, what effect do those proceedings have on (a) sales of receivables that would otherwise occur after the commencement of such proceedings, or (b) on sales of receivables that only come into existence after the commencement of such proceedings?

If the receivables purchase agreement provides that no further action is required by the seller for the receivables (including receivables arising in the future) to be transferred, the agreement will generally continue to be effective to transfer the receivables even after the initiation of insolvency proceedings. However, either party could exercise a contractual right to terminate.

Further, in certain circumstances, a liquidator might be able to, under the Insolvency Act, disclaim (and thereby terminate) an ongoing receivables purchase agreement if it were an "unprofitable contract". If the agreement requires further action from the seller, the insolvency official may choose not to take that action and, in that situation, the purchaser's remedy is likely to be limited to an unsecured claim in any insolvency proceedings.

6.6 Effect of Limited Recourse Provisions. If a debtor's contract contains a limited recourse provision (see question 7.3 below), can the debtor nevertheless be declared insolvent on the grounds that it cannot pay its debts as they become due?

Historically, it has generally been understood that provisions providing creditors limited recourse to the assets of a debtor would be effective in making the debtor insolvency-remote, provided that, on the face of the contractual documents, this was the clearly expressed intention of the parties.

Although, on an unopposed application by a debtor to initiate insolvency proceedings (*ARM Asset Backed Securities S.A.* [2013] EWHC 3351 (Ch) (9 October 2013) (**ARM**)), a debtor was held to be insolvent in spite of the fact that its debts were limited in recourse (although the court did not question the provision's effectiveness as a matter of contract), this judgment is capable of being limited to its context on a number of factual and legal grounds.

7 Special Rules

7.1 Securitisation Law. Is there a special securitisation law (and/or special provisions in other laws) in your jurisdiction establishing a legal framework for securitisation transactions? If so, what are the basics? Is there a regulatory authority responsible for regulating securitisation transactions in your jurisdiction?

Other than certain tax laws (see question 9.2 below in relation to special purpose entities which are "securitisation companies" and their treatment for tax purposes), there is (currently) no single regulatory regime covering UK securitisations specifically. Instead, the market is regulated by a number of EU directives and regulations, domestic legislation and the rules of the UK financial regulators. As well as legislative rule-making authorities, there are also market-sponsored bodies that issue guidelines, codes of conduct and other rules that are relevant to securitisation market participants.

FSMA sets out the basis of the UK financial services regulatory framework, including the general prohibition of carrying out a regulated activity unless authorised or exempt. FSMA therefore addresses which parties to a securitisation transaction may need to be authorised under FSMA in order to carry out a regulated activity in the UK or communicate a financial promotion capable of having an effect in the UK. The UK FCA and the UK Prudential Regulation Authority (**PRA**) are the two UK regulators for these purposes. Depending on the nature of the activities to be carried out by a firm, they may need to be regulated by both the FCA and the PRA, or just the FCA.

In addition, the FCA has been designated as the competent authority for the purposes of making the Listing Rules, Prospectus Rules and Disclosure Guidance and Transparency Rules, which may apply in respect of UK securitisations. The FCA (as the UK Listing Authority) is responsible for vetting and approving prospectuses for the purposes of the Prospectus Directive as implemented in the UK.

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7.2 Securitisation Entities. Does your jurisdiction have laws specifically providing for establishment of special purpose entities for securitisation? If so, what does the law provide as to: (a) requirements for establishment and management of such an entity; (b) legal attributes and benefits of the entity; and (c) any specific requirements as to the status of directors or shareholders?

English law does not specifically provide for the establishment of special purpose entities for securitisation transactions (although see question 9.2 below in relation to special purpose entities which are "securitisation companies" and their treatment for tax purposes).

7.3 Location and form of Securitisation Entities. Is it typical to establish the special purpose entity in your jurisdiction or offshore? If in your jurisdiction, what are the advantages to locating the special purpose entity in your jurisdiction? If offshore, where are special purpose entities typically located for securitisations in your jurisdiction? What are the forms that the special purpose entity would normally take in your jurisdiction and how would such entity usually be owned?

For securitisations of assets or businesses located in England and Wales (such as securitisations of commercial or residential mortgages), the securitisation entity will often be incorporated in England due to market familiarity with the established and respected legal framework applicable to English corporate entities, as well as for various tax reasons relating to underlying assets physically located in the UK (such as UK real estate).

In these circumstances, it is usual for the securitisation entity to be formed either as a public or private company limited by shares, or a limited liability partnership (LLP). Both limited companies and LLPs are treated as body corporates with a separate legal personality where the liability of a shareholder/member is limited. Common with other established jurisdictions, the securitisation entity is normally (but not always) formed as an orphan "special purpose vehicle" or "SPV", such that is does not form part of the same corporate group as any other transaction party. This is normally achieved through the shares or membership interests of the SPV being held by an entity on trust for discretionary charitable purposes. It should be noted that such interests are typically nominal.

In response to specific commercial, regulatory, tax, administrative, structural and/or legal reasons, securitisation entities are often incorporated outside of England and Wales. Common jurisdictions include the Cayman Islands, Ireland, Jersey, Luxembourg and the Netherlands, with the choice of jurisdiction influenced by factors including:

- The timing/cost of establishing and maintaining the securitisation entity.
- Minimum capitalisation requirements for the securitisation entity.
- Initial/ongoing disclosure or regulatory requirements (such as requirements for audited accounts).
- Taxation of the securitisation entity and its assets in that jurisdiction, including corporate tax on any minimum required retained profits, deductibility of interest payments made by the securitisation entity, and issues relating to withholding tax (including availability of tax treaty relief in relation to interest and other payments on underlying assets as well as payments of interest on the securities issued by the securitisation entity), VAT or other taxes.
- Licensing and authorisation requirements.
- Insolvency law considerations.

7.4 Limited-Recourse Clause. Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) limiting the recourse of parties to that agreement to the available assets of the relevant debtor, and providing that to the extent of any shortfall the debt of the relevant debtor is extinguished?

Provisions limiting the recourse of a creditor to the net proceeds of disposal or enforcement of specified assets owned by the obligor or its available funds are likely to be valid under English law, and an English court is likely to hold that, to the extent of any shortfall, the debt of the obligor is extinguished. Whilst the decision of the High Court in ARM, referenced in question 6.6 above, brought into question whether a limited recourse provision will be effective to prevent a debtor from being held unable to pay its debts, with the judge in ARM stating that a useful test as to whether a company is insolvent is to consider the amounts for which bondholders would prove in a liquidation (being the face value of, and interest payable on, their bonds), the judge also confirmed the effectiveness of a limited recourse provision as a matter of contract, stating that "the rights of the creditors to recover payment will be, as a matter of legal right as well as a practical reality, restricted to the available assets, and … the obligations [of the debtor] will be extinguished after the distribution of available funds".

Where an agreement is governed by the law of another country and the English courts have cause to consider its efficacy under that foreign law, the analysis as to whether such a clause would be upheld will be the same as that discussed in questions 3.4 and 3.5 above, namely that the English courts would apply the relevant foreign governing law to determine whether the limited recourse provision was effective.

7.5 Non-Petition Clause. Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) prohibiting the parties from: (a) taking legal action against the purchaser or another person; or (b) commencing an insolvency proceeding against the purchaser or another person?

Although there is little authority in English law, it is likely that an English court would give effect to contractual non-petition clauses prohibiting the parties to the relevant contract from taking legal action, or commencing an insolvency proceeding, against the purchaser or another person. The most effective method for enforcing such a clause would be injunctive relief which, as an equitable remedy, is at the discretion of the court. A court will exercise its discretion and would have to consider whether such a clause was contrary to public policy as an attempt to oust the jurisdiction of the court and/or English insolvency laws. It is possible that an English court would deal with a winding-up petition even if it were presented in breach of a non-petition clause. A party may have statutory or constitutional rights to take legal action against the purchaser or such other person which may not be contractually disapplied.

Where an agreement is governed by the law of another country and the English courts have cause to consider its efficacy under that foreign law, the analysis as to whether such a clause would be upheld will be the same as that discussed in questions 3.4 and 3.5 above, namely that the English courts would apply the relevant foreign governing law to determine whether the non-petition clause was effective.

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7.6 Priority of Payments "Waterfall". Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) distributing payments to parties in a certain order specified in the contract?

In respect of English law-governed priorities of payments in secured transactions, as a general matter, the courts of England and Wales will seek to give effect to contractual provisions that sophisticated commercial parties have agreed, except where to do so is contrary to applicable law or public policy.

The English Supreme Court decision in *Belmont Park Investments Pty Limited v BNY Corporate Trustee Services Limited and Lehman Brothers Special Financing Inc. [2011] UKSC 38* (**Belmont**) considered whether a contractual provision subordinating a creditor's rights to payment on the occurrence of an insolvency event in relation to that creditor (termed a "flip clause") was contrary to applicable English law, specifically the "anti-deprivation" rule (a sub-set of a general principle that parties cannot contract out of insolvency legislation, and specifically that a company cannot be improperly deprived of an asset by virtue of a liquidation or other insolvency process affecting that company to the detriment of the company's creditors). The Belmont judgment noted that the "anti-deprivation" rule is a principle of public policy although there are no clear rules as to the circumstances in which the principle will apply. However, certain guidelines were set out in Belmont, including that: (i) the "anti-deprivation" rule applied where there was an intention to obtain an advantage over creditors in the winding-up or other insolvency process but that such question should be tested in a commercially sensible manner, taking into account the policy of party autonomy and the upholding of proper commercial bargains; (ii) the identity of the persons that provided the property to which the insolvent company was deprived by such provision was relevant in considering the point raised at (i) (in Belmont the party seeking to rely on the provision (certain noteholders) had provided the collateral of which the creditor in question was deprived); and (iii) the "anti-deprivation" rule only applies where the trigger for the deprivation is a winding-up or other insolvency process affecting the deprived party. In Belmont, the "flip clause" was upheld notwithstanding the fact that the subordination provision was triggered by the insolvency of the creditor and particular emphasis, was placed on items (i) and (ii) above. In finding that the flip clause in question was part of a good faith commercial transaction that did not have as its purpose the evasion of the anti-deprivation principle, the court relied, among other things, on the facts that there was a wide range of possible events other than insolvency that would trigger the flip clause and that there was a valid commercial reason for the flip clause (namely to deal with the risk of the swap provider defaulting).

By contrast, the US Bankruptcy Court for the Southern District of New York held in parallel proceedings (*Lehman Brothers Special Financing Inc. v BNY Corporate Trustee Services Ltd (In re Lehman Brothers Holding Inc.) 422 B.R. 407, 420 (Bankr S.D.N.Y. 2010) (BNY)*) that the English law-governed "flip clause" in question was unenforceable as a violation of the US Bankruptcy Code.

These competing decisions caused uncertainty as to whether an adverse foreign judgment in respect of the enforceability of a flip clause in a priority of payments would be recognised and given effect by the English courts in a cross-border insolvency case. However, in June 2016, the US Bankruptcy Court substantially distinguished its decision in the BNY case, finding that, subject to the precise drafting of the terms establishing the payment priorities (and the related "flip clause"), such terms would not violate the US Bankruptcy Code (*Lehman Brothers Special Financing Inc. v Bank of America, N.A. (In re Lehman Brothers Holding Inc.), Adv. No.10—3547 (SCC), --- B.R.---- (Bankr S.D.N.Y. June 28, 2016)*). This decision was affirmed by the US District Court on appeal, albeit on different grounds (No. 17 Civ 1224 (LGS), 2018 WL 1322225 (S.D.N.Y. March 14, 2018)) and substantially harmonised US bankruptcy law with English insolvency law in relation to the treatment of certain types of "flip clauses", although it is worth noting that the decision remains subject to further possible appeal and there are several other actions which have commenced in the US courts relating to "flip clauses".

Where the priority of payments provision is governed by a law other than the laws of England and Wales and the English courts have cause to consider its efficacy under that foreign law, the analysis as to whether such a clause would be upheld will be the same as that discussed in questions 3.4 and 3.5 above, namely that the English courts would apply the relevant foreign governing law to determine whether the priority of payments provision was effective.

7.7 Independent Director. Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) or a provision in a party's organisational documents prohibiting the directors from taking specified actions (including commencing an insolvency proceeding) without the affirmative vote of an independent director?

The articles of association of a company or a contract entered into by a company may, in principle, restrict the authority of its directors and it is likely that an English court would give effect to such a provision or article. However, any restriction or limitation on the ability of the directors to bring insolvency proceedings may be invalid as a matter of public policy or incompatible with certain statutory duties of the directors.

7.8 Location of Purchaser. Is it typical to establish the purchaser in your jurisdiction or offshore? If in your jurisdiction, what are the advantages to locating the purchaser in your jurisdiction? If offshore, where are purchasers typically located for securitisations in your jurisdiction?

See question 7.3 above.

8 Regulatory Issues

8.1 Required Authorisations, etc. Assuming that the purchaser does no other business in your jurisdiction, will its purchase and ownership or its collection and enforcement of receivables result in its being required to qualify to do business or to obtain any licence or its being subject to regulation as a financial institution in your jurisdiction? Does the answer to the preceding question change if the purchaser does business with more than one seller in your jurisdiction?

A purchaser of regulated consumer loans and regulated residential and CBTL mortgage contracts may require authorisation under the FSMA and/or the MCD Order by the FCA, insofar as it proposes to advance new loans, make further advances on existing facilities or vary existing loans and/or mortgage contracts in such a way so as to give rise to a new loan and/or regulated mortgage contract. As regards activities relating to the collection and enforcement of receivables and other administrative functions (such as serving

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notices on obligors), there are certain exemptions available where a purchaser enters into a servicing agreement with an appropriately authorised third party in relation to the receivables and certain other conditions are met. The purchaser may also be obliged to notify its data processing activities to the UK's Information Commissioner's Office under the Data Protection Act 1998 (the **DPA**). It makes no difference whether or not the purchaser does business with other sellers in England and Wales.

8.2 Servicing. Does the seller require any licences, etc., in order to continue to enforce and collect receivables following their sale to the purchaser, including to appear before a court? Does a third-party replacement servicer require any licences, etc., in order to enforce and collect sold receivables?

The requirements will vary with respect to the seller depending on the regulated facility in question and whether the receivables have been sold by way of an equitable assignment or legal transfer. They can be summarised as follows:

(a) in the case of regulated consumer credit loans and consumer hire facilities, where the receivables are assigned by way of an equitable transfer, provided that the seller retains its authorisation to enter into regulated consumer credit and/or hire agreements as a lender/owner, the seller should not be required to be specifically authorised to undertake regulated enforcement and collection activities with respect to the receivables, given that the seller still retains legal title to the loans and may continue to administer those loans in its capacity as a lender;

(b) in the case of regulated consumer credit loans and consumer hire facilities, where the receivables are sold by way of a legal transfer but the seller retains the servicing function, the seller will require authorisation under the FSMA for the regulated activities of debt administration and debt collection; and

(c) in the case of regulated mortgage contracts, the seller will require authorisation under the FSMA (with respect to residential mortgage contracts) and/or the MCD Order (with respect to CBTL mortgage contracts) for the regulated activity of administering regulated mortgage contracts, and possibly advising on these in order to be able to advise an obligor on varying the terms of its mortgage contract. These authorisation requirements would apply irrespective of whether the loan has been transferred by way of a legal or equitable assignment.

Any standby or replacement servicer will require the authorisations detailed in (b) and (c) above before taking any action to enforce or collect monies owed under regulated credit agreements or regulated mortgage contracts.

Both the seller and third-party servicer will also be subject to registration requirements under the DPA.

8.3 Data Protection. Does your jurisdiction have laws restricting the use or dissemination of data about or provided by obligors? If so, do these laws apply only to consumer obligors or also to enterprises?

The handling and processing of information on living, identifiable individuals (**personal data**) is regulated by the DPA. The DPA only applies to personal data, so it affects data on individual, living and identifiable obligors and not enterprises. The DPA specifies that a data controller is any legal or natural person who (either alone or jointly) determines the purposes for which, and the manner in which, any personal data is to be processed, and so may well include a purchaser of receivables serviced by the seller. A data controller in the UK must comply with the requirements under the DPA. From 25 May 2018, the EU General Data Protection Regulation (**GDPR**) will become effective. The UK is in the process of finalising the Data Protection Bill which will implement the GDPR in the UK and will replace the DPA. The GDPR introduces a number of new and onerous obligations and imposes significant potential fines of up to 4% of annual worldwide turnover for non-compliance.

8.4 Consumer Protection. If the obligors are consumers, will the purchaser (including a bank acting as purchaser) be required to comply with any consumer protection law of your jurisdiction? Briefly, what is required?

In addition to the authorisation requirements discussed above, there is a large number of statutes, regulations, rules and guidance governing consumer interests within the context of regulated consumer credit and consumer hire agreements and regulated mortgage contracts. These include amongst others:

- The CCA (and delegated legislation thereunder), which continues to apply to consumer credit and consumer hire agreements and contains several important requirements for lenders/owners under regulated consumer credit/hire agreements. In addition to the requirements of the CCA, firms authorised under the FSMA to carry on consumer credit and consumer hire-related regulated activities must comply with the FCA's Handbook of rules and guidance, including CONC. These rules are aimed at ensuring the fair treatment of consumers and hirers, and contain prescriptive rules and guidance relating to all aspects of the product lifecycle, including in relation to arrears management.
- First and second charge residential mortgage lenders authorised under the FSMA are also required to comply with the FCA's Handbook, including MCOB. The rules in MCOB cover, amongst other things, certain pre-origination matters such as financial promotion and pre-application illustrations, pre-contract, start-of-contract and post-contract disclosure, contract changes, charges and arrears and repossessions.
- The MCD Order, which sets out conduct of business requirements for firms registered to undertake regulated activities in respect of CBTL mortgage contracts. Like MCOB, these include amongst other things, requirements pertaining to the provision of information to consumers, calculation of the annual percentage rate of charge, early repayments, arrears and repossessions.
- The Unfair Contracts Terms Act 1977, which restricts the limitation of liability by a party. Liability for death or personal injury caused by negligence cannot be limited and any clauses that limit liability for other damage caused by negligence must satisfy a reasonableness test.
- The Consumer Rights Act 2015 (the **CRA**), which harmonises and simplifies domestic legislation in relation to consumer protection legislation in the UK. The CRA came into force on 1 October 2015 and contains important provisions relating to unfair contract terms in agreements and notices. A term is "unfair" if it causes a significant imbalance in the parties' rights and obligations under the contract to the detriment of the consumer. Such an unfair term will not be binding on the consumer. A consumer for these purposes is an individual acting for purposes that are wholly or mainly outside that individual's trade, business, craft or profession.
- The Consumer Protection from Unfair Trading Regulations 2008 (**CPUTRs**), which affect all contracts entered into with persons who are natural persons and acting for purposes outside their respective business. The CPUTRs have a general prohibition on unfair commercial practices, but also contain provisions aimed at aggressive and misleading

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practices (including, but not limited to: (i) pressure selling; (ii) misleading marketing (whether by action or omission); and (iii) falsely claiming to be a signatory to a code of conduct) and a list of practices which will in all cases be considered unfair.

8.5 Currency Restrictions. Does your jurisdiction have laws restricting the exchange of your jurisdiction's currency for other currencies or the making of payments in your jurisdiction's currency to persons outside the country?

No, subject to any restrictions and financial sanctions imposed by the United Nations and the European Union. It is a criminal offence to breach a financial sanction without an appropriate licence or authorisation from HM Treasury.

8.6 Risk Retention. Does your jurisdiction have laws or regulations relating to "risk retention"? How are securitisation transactions in your jurisdiction usually structured to satisfy those risk retention requirements?

Articles 404–410 of the EU Capital Requirements Regulation (Regulation (EU) No 575/2013 (as supplemented by Commission Delegated Regulation (EU) No 625/2014 and Commission Implementing Regulation (EU) No 602/2014) (**CRR**) set out the relevant risk retention requirements and apply, in general, to newly issued asset-backed securities after 1 January 2011, and to asset-backed securities issued on or before that date from 31 December 2014 to the extent that new underlying exposures are added or substituted after 31 December 2014.

The CRR restricts a credit institution and investment firm regulated in a Member State of the European Economic Area (**EEA**) and consolidated group affiliates thereof (each, a **CRR Investor**) from investing in a securitisation (as defined by the CRR) unless the originator, sponsor or original lender in respect of that securitisation has explicitly disclosed to the CRR Investor that it will retain, on an ongoing basis, a material net economic interest of not less than 5% in that securitisation in the manner contemplated by Article 405 of the CRR. The CRR also requires that a CRR Investor be able to demonstrate that it has undertaken certain due diligence in respect of, amongst other things, the securities it has acquired and the underlying exposures, and that procedures have been established for monitoring the performance of the underlying exposures on an ongoing basis.

Article 17 of the EU Alternative Investment Fund Managers Directive (Directive 2011/61/EU) (as supplemented by Section 5 of Chapter III of Commission Delegated Regulation (EU) No 231/2013) (the **AIFMD**) and Article 135(2) of the EU Solvency II Directive 2009/138/EC (as supplemented by Articles 254–257 of Commission Delegated Regulation (EU) No 2015/35) (**Solvency II**) contain requirements similar to those set out in Articles 404–410 of the CRR and apply, respectively, to EEA regulated alternative investment fund managers and EEA regulated insurance/reinsurance undertakings. While such requirements are similar to those in the CRR, they are not identical and, in particular, additional due diligence obligations apply to relevant alternative investment fund managers and insurance and reinsurance companies. The risk retention requirements prescribed by the CRR, together with those under the AIFMD and Solvency II are collectively referred to here as the **EU Retention Regulations**.

Under the EU Retention Regulations, the risk retention must be by way of one of the five specified methods, which are:

(a) retention of no less than 5% of the nominal value of each of the tranches sold or transferred to the investors;

(b) in the case of securitisations of revolving exposures, retention of the originator's interest of no less than 5% of the nominal value of the securitised exposures;

(c) retention of randomly selected exposures, equivalent to no less than 5% of the nominal value of the securitised exposures, where such exposures would otherwise have been securitised in the securitisation, provided that the number of potentially securitised exposures is no less than 100 at origination;

(d) retention of the first loss tranche and, if necessary, other tranches having the same or a more severe risk profile than those transferred or sold to investors and not maturing any earlier than those transferred or sold to investors, so that the retention equals in total no less than 5% of the nominal value of the securitised exposures; and

(e) retention of a first loss exposure not less than 5% of every securitised exposure in the securitisation.

8.7 Regulatory Developments. Have there been any regulatory developments in your jurisdiction which are likely to have a material impact on securitisation transactions in your jurisdiction?

A new EU risk retention regime will apply, in place of the existing EU Retention Regulations, to securitisations in respect of which the relevant securities are issued on or after January 1, 2019. There will be material differences between that new regime and the existing requirements. The new regime will be implemented primarily by Regulation (EU) No 2017/2402 (the **Securitisation Regulation**), which will (amongst other things):

- impose restrictions on investment in securitisations and requirements as to due diligence; and
- apply to EEA investors currently subject to the existing EU Retention Regulations and also to: (i) certain investment companies authorised in accordance with Directive 2009/65/EC, and managing companies as defined in that Directive (together, **UCITS**); and (ii) institutions for occupational retirement provision falling within the scope of Directive (EU) 2016/2341 (subject to certain exceptions), and certain investment managers and authorised entities appointed by such institutions (together, **IORPS**).

The Securitisation Regulation also sets out a framework and criteria for identifying "simple transparent and standardised securitisations" (**STS securitisations**). Exposures to STS securitisations will generally be given preferential regulatory capital treatment when compared with exposures to non-STS securitisations.

Certain aspects of the Securitisation Regulation will be supplemented by regulatory technical standards that are currently being consulted on by the European Banking Authority. At the time of writing it is not certain as to what form the final regulatory technical standards may take or when they will be adopted.

Further, while the Securitisation Regulation (being an EU Regulation) will apply directly in all EU Member States without the need for national implementation, consideration will need to be given to the potential implications of Brexit. There is currently a great deal of uncertainty surrounding the likely final form of any Brexit and various aspects of the UK financial services regulatory regime (not just relating to securitisation) may, potentially, be significantly affected.

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9 Taxation

9.1 Withholding Taxes. Will any part of payments on receivables by the obligors to the seller or the purchaser be subject to withholding taxes in your jurisdiction? Does the answer depend on the nature of the receivables, whether they bear interest, their term to maturity, or where the seller or the purchaser is located? In the case of a sale of trade receivables at a discount, is there a risk that the discount will be recharacterised in whole or in part as interest? In the case of a sale of trade receivables where a portion of the purchase price is payable upon collection of the receivable, is there a risk that the deferred purchase price will be recharacterised in whole or in part as interest? If withholding taxes might apply, what are the typical methods for eliminating or reducing withholding taxes?

The withholding tax treatment of UK receivables depends not only on their nature, but on the nature of the recipient to whom they are paid. Very broadly, payments of interest with a UK source may be paid without withholding to a purchaser which is either resident in the UK or carries on business in the UK through a permanent establishment. Payments of interest to a non-UK resident purchaser may often be subject to withholding, subject to any available treaty relief pursuant to a double taxation convention. Typically, where such treaty relief is available, an application must first be made by the non-UK resident purchaser to H.M. Revenue & Customs (**HMRC**) who will issue a direction to the relevant obligor to make payments free of withholding tax. The administrative process for claiming treaty relief is different, however, if the non-UK resident purchaser holds a passport under HMRC's double taxation treaty passport scheme. Generally, however, (except in the case of large serviced static pools of assets where there have been some recent administrative advances for some transactions) the use of relief under a double taxation convention where there are multiple assets may be administratively challenging. Accordingly, loan receivables are typically securitised through the use of a UK resident purchasing company.

Generally, trade receivables payments and lease rental payments are not subject to UK withholding unless they provide for the payment of interest, in which case the interest element will be subject to withholding in the same way as interest on loan relationships. The recharacterisation of deferred purchase price as interest depends upon the facts of the case in question, but is not a typical outcome under the UK rules.

9.2 Seller Tax Accounting. Does your jurisdiction require that a specific accounting policy is adopted for tax purposes by the seller or purchaser in the context of a securitisation?

The tax treatment of a company within the charge to UK corporation tax would be expected, at least as a starting point, to follow its accounting treatment. For a company purchasing receivables, in many cases the rules imposed by the appropriate accounting regime would be expected to result in the creation of accounting profits, and accordingly taxable profits, which do not reflect the actual cash position of the company in question.

For accounting periods commencing on, or after, 1 January 2007, the Taxation of Securitisation Companies Regulations have been in force. These regulations apply to companies which are "securitisation companies" (as defined in the regulations) and permit a securitisation company to be subject to tax treatment reflecting the cash position of its securitisation arrangements, such that it is taxed only on the cash profit retained within the company after the payment of its transaction disbursements according to the transaction waterfall. As such, balanced tax treatment can be achieved and the regime has been seen as providing effective relief from the complex or anomalous tax rules which could otherwise apply to UK incorporated special purpose vehicles.

9.3 Stamp Duty, etc. Does your jurisdiction impose stamp duty or other transfer or documentary taxes on sales of receivables?

Stamp duty exists in the UK and is chargeable on documents in certain circumstances. Transactions may also be subject to UK Stamp Duty Reserve Tax (**SDRT**) levied on transfers of certain types of securities whether effected by document or otherwise. Generally, transfers of loans (which are not convertible and have no "equity" type characteristics such as profit-related interest), trade and lease receivables should not be subject to UK stamp duty or SDRT.

9.4 Value Added Taxes. Does your jurisdiction impose value added tax, sales tax or other similar taxes on sales of goods or services, on sales of receivables or on fees for collection agent services?

UK value added tax (**VAT**) is chargeable on supplies of goods and services which take place in the UK and which are made by "taxable persons" in the course or furtherance of a business. The standard rate of VAT is currently 20%, although certain supplies (including the supply of certain financial services) are exempt from VAT.

In *MBNA Europe Bank Ltd v HMRC* [2006] it was decided by the UK High Court that the transfer of credit card receivables by an originator in a securitisation was not a supply for VAT purposes. However, that decision may not apply to all such transfers. To the extent that the decision does not apply, a transfer of financial receivables would generally be treated as an exempt supply for VAT purposes.

Generally, fees payable for collection agent services are not exempt from VAT and will usually give rise to VAT at the standard rate, to the extent they are treated as taking place in the UK.

9.5 Purchaser Liability. If the seller is required to pay value-added tax, stamp duty or other taxes upon the sale of receivables (or on the sale of goods or services that give rise to the receivables) and the seller does not pay, then will the taxing authority be able to make claims for the unpaid tax against the purchaser or against the sold receivables or collections?

As described above, the transfer of financial receivables would usually either constitute an exempt supply for VAT purposes, or fall outside the scope of VAT altogether. However, a seller might incur VAT on a supply of assets which does not fall within any of the exemptions: for example, property or trading assets on a true sale securitisation. If so, the seller would generally be liable to account for such VAT to HMRC.

Broadly, HMRC would not be able to require the purchaser to account for VAT unless the purchaser was a member of the same group as the seller for VAT purposes. Although there are limited exceptions to this general position, it is unlikely that such exceptions would apply in a securitisation context.

Where charged, stamp duty and SDRT are generally payable by the purchaser.

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9.6 Doing Business. Assuming that the purchaser conducts no other business in your jurisdiction, would the purchaser's purchase of the receivables, its appointment of the seller as its servicer and collection agent, or its enforcement of the receivables against the obligors, make it liable to tax in your jurisdiction?

Generally, the purchase of receivables will not give rise to tax liabilities for a purchaser conducting no other business in the UK, and the appointment of a servicer by the purchaser which carries out normal administrative activities on its behalf should not result in tax liabilities for the purchaser. The question of enforcement would need to be considered in the light of the particular circumstances.

9.7 Taxable Income. If a purchaser located in your jurisdiction receives debt relief as the result of a limited recourse clause (see question 7.3 above), is that debt relief liable to tax in your jurisdiction?

A purchaser which is a "securitisation company" falling within the Taxation of Securitisation Company Regulations will, generally, only be subject to tax on its retained cash profit, as provided for in the transaction waterfall (see further question 9.2 above). The tax treatment of a purchaser which does not fall within the Taxation of Securitisation Company Regulations will (as referred to in question 9.2 above) generally follow its accounting treatment for its loan relationships. In certain circumstances, such a company may be taxed on an amount of a debt from which it is released. This is subject to exemptions for specified insolvency and restructuring situations.

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Rupert Wall advises arrangers, originators, asset and investment managers and investors on all aspects of securitisation, structured finance and derivatives. He also advises counterparties in relation to general capital markets issuances, leveraged finance transactions and portfolio sales.

Rupert has been recognised in legal directories as "*one of the brightest young partners in the market*" and as "*responsive, commercially minded*" with "*considerable experience and talent*". In *The Legal 500 UK* 2017 he is recognised as a Leading Individual for Securitisation and is recommended for Derivatives & Structured Products, with clients describing him as "*a standout lawyer for ABS and CLO deals*", and whom one client describes as "*a subject matter expert with the ability to get straight to the point; he has a brain the size of a planet and works very well in high pressure situations*". In addition, Rupert is ranked in *Chambers UK* 2018 for Capital Markets: Structured Finance & Derivatives and recommended for Capital Markets: Securitisation, with clients saying he "*stands out as being a valued adviser who, as well as being hugely bright and intellectual, has a unique ability to listen carefully to the often complex commercial dynamics that we require of a transaction and meld those seamlessly into its structure*". A source from the 2017 edition of *IFLR 1000* told the publication Rupert has "*excellent product knowledge*" and is a "*very good communicator*". A year prior, sources told the publication "*he demonstrated the right balance between legal understanding and commercial awareness. We would highly recommend him*".

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Roisin Nagle has a main area of focus advising on derivatives and structured finance transactions. In particular, Roisin has advised asset managers, investment firms and other financial institutions on the regulation of derivatives under the European Market Infrastructure Regulation (EMIR) and MiFID II, the regulation of securities financing transactions under the Securities Financing Transactions Regulation (SFTR), and general structured finance transactions.

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SIDLEY has been at the forefront of the European securitisation market since the early 1990s and since that time has been involved in a number of ground-breaking securitisation products and structures in numerous European jurisdictions, including establishing domestic and pan-European CMBS platforms, asset-backed commercial paper and securities conduits, RMBS-related products, whole business securitisations and covered bonds as well as a deep experience in advising arrangers, managers and investors on CLO and CDO transactions. Sidley's securitisation lawyers in Europe and the US have a well-established practice in all areas of securitisation, structured finance and derivatives, with market-leading experience of the full gamut of asset classes and structures including securitisations and secured financings involving corporate (mid-market and syndicated) loans, rental fleets, consumer assets such as personal loans, auto loans and leases and credit cards, trade and other more specialised receivables, and more recently in the emerging market for financings involving online marketplace and peer-to-peer lending and blockchain and distributed ledger technology. Sidley has also been at the cutting edge of structuring financings of innovative and esoteric asset classes such as solar energy and renewables, insurance products and IP securitisations amongst many others.

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Finland

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1 Receivables Contracts

1.1 Formalities. In order to create an enforceable debt obligation of the obligor to the seller: (a) is it necessary that the sales of goods or services are evidenced by a formal receivables contract; (b) are invoices alone sufficient; and (c) can a binding contract arise as a result of the behaviour of the parties?

There are no requirements on a receivable contract to create an enforceable debt obligation, although documentation is recommended because a written receivable contract is generally considered complete evidence as to the existence of the receivable. The same general rules apply to receivables evidenced by a written receivable contract or an invoice, as well as receivables agreed upon orally or deemed to exist as a result of the behaviour of the parties. In order for a receivable contract to qualify as a negotiable promissory note, there are certain formal requirements on the receivables contract. A consumer credit must be made in written or electronic form.

1.2 Consumer Protections. Do your jurisdiction's laws: (a) limit rates of interest on consumer credit, loans or other kinds of receivables; (b) provide a statutory right to interest on late payments; (c) permit consumers to cancel receivables for a specified period of time; or (d) provide other noteworthy rights to consumers with respect to receivables owing by them?

Finland has implemented Directive 2008/48/EC on credit agreements for consumers and Directive 2014/17/EU on credit agreements for consumers relating to residential immovable property.

Consumer credits in an amount or with a credit limit below EUR 2,000 are subject to a mandatory interest rate ceiling. The maximum interest rate on such consumer credits may not exceed the statutory reference rate (in January 2018: 0.0%) plus 50 percentage points. For the purposes of the interest rate ceiling, the interest rate is calculated as the total cost of the credit (thus also including commissions, taxes and any other kind of fees which the consumer is required to pay in connection with the credit agreement) to the consumer and expressed as an annual percentage of the total credit amount made available to the consumer. The interest rate ceiling does not apply to linked credit agreements, unless the linked credit agreement provides for the possibility to borrow funds also in cash.

With regard to default interest, unless otherwise agreed, any due and payable receivable bears default interest at a rate being seven percentage units higher than the statutory reference rate or at the regular interest rate if this is higher than the statutory default interest rate. This provision may be contracted out both to the benefit and detriment of the debtor, unless the receivable consists of consumer debt, in which case it can only be contracted out to the benefit of the consumer, i.e., any default interest exceeding the above-mentioned rate would be ineffective. In respect of consumer credits, if the regular interest rate of the loan was higher than the statutory default interest rate, the creditor may charge the higher regular interest for a maximum period of 180 days or until an enforceable court judgment is received.

Other than as set out above, there are no specific rules limiting rates of interest, but it should be noted that the general principles of equity apply also to interest rates.

Consumers may cancel most types of consumer credits during a period of 14 days from receiving the required details of the terms and conditions of the credit.

Finnish consumer law also permits the consumer to always prepay a consumer credit and limits the costs that may be charged in this case. There are also limitations on when the creditor is entitled to accelerate a consumer credit.

1.3 Government Receivables. Where the receivables contract has been entered into with the government or a government agency, are there different requirements and laws that apply to the sale or collection of those receivables?

No, there are no different laws or requirements in the case of a receivable contract with the government.

2 Choice of Law – Receivables Contracts

2.1 No Law Specified. If the seller and the obligor do not specify a choice of law in their receivables contract, what are the main principles in your jurisdiction that will determine the governing law of the contract?

Finland has ratified the Rome Convention on the Law Applicable to Contractual Obligations and is also bound by the Rome I Regulation. Consequently, the choice of law rules set out therein would be applied.

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2.2 Base Case. If the seller and the obligor are both resident in your jurisdiction, and the transactions giving rise to the receivables and the payment of the receivables take place in your jurisdiction, and the seller and the obligor choose the law of your jurisdiction to govern the receivables contract, is there any reason why a court in your jurisdiction would not give effect to their choice of law?

No, there are no such reasons.

2.3 Freedom to Choose Foreign Law of Non-Resident Seller or Obligor. If the seller is resident in your jurisdiction but the obligor is not, or if the obligor is resident in your jurisdiction but the seller is not, and the seller and the obligor choose the foreign law of the obligor/seller to govern their receivables contract, will a court in your jurisdiction give effect to the choice of foreign law? Are there any limitations to the recognition of foreign law (such as public policy or mandatory principles of law) that would typically apply in commercial relationships such as that between the seller and the obligor under the receivables contract?

As provided by the Rome I Regulation, the parties are generally free to choose the governing law of the contract, subject to the exceptions (such as mandatory consumer protection and *ordre public*) provided by the Regulation. From Finnish procedure law, it follows that if the parties do not provide sufficient evidence of how the matter would be determined under the chosen law, a Finnish court could apply Finnish law instead.

3 Choice of Law – Receivables Purchase Agreement

3.1 Base Case. Does your jurisdiction's law generally require the sale of receivables to be governed by the same law as the law governing the receivables themselves? If so, does that general rule apply irrespective of which law governs the receivables (i.e., your jurisdiction's laws or foreign laws)?

There is no such requirement.

3.2 Example 1: If (a) the seller and the obligor are located in your jurisdiction, (b) the receivable is governed by the law of your jurisdiction, (c) the seller sells the receivable to a purchaser located in a third country, (d) the seller and the purchaser choose the law of your jurisdiction to govern the receivables purchase agreement, and (e) the sale complies with the requirements of your jurisdiction, will a court in your jurisdiction recognise that sale as being effective against the seller, the obligor and other third parties (such as creditors or insolvency administrators of the seller and the obligor)?

Yes, the sale would be effective.

3.3 Example 2: Assuming that the facts are the same as Example 1, but either the obligor or the purchaser or both are located outside your jurisdiction, will a court in your jurisdiction recognise that sale as being effective against the seller and other third parties (such as creditors or insolvency administrators of the seller), or must the foreign law requirements of the obligor's country or the purchaser's country (or both) be taken into account?

Finnish courts normally apply the "*lex rei sitae*" principle to the effectiveness of a sale of receivables in relation to, *inter alia*, third-party creditors, according to which principle the relationship to third parties is determined in accordance with the laws of the jurisdiction where the relevant asset is located.

However, the "location" of a receivable is not expressly addressed in Finnish statutory law and there is also limited case law of relevance. The predominant view in the legal doctrine is that the applicable law is the law of the jurisdiction of the obligor of the receivable, and the answers to questions 3.1–5 above and below, as well as to the questions in section 5, are based on this view. It should be, however, noted that it is a common precautionary measure to comply with the requirements of all relevant jurisdictions should there be differences in the perfection requirements.

Based on the above, in this example the requirements of the obligor's domicile would have to be complied with in order for the sale to be effective against third parties.

3.4 Example 3: If (a) the seller is located in your jurisdiction but the obligor is located in another country, (b) the receivable is governed by the law of the obligor's country, (c) the seller sells the receivable to a purchaser located in a third country, (d) the seller and the purchaser choose the law of the obligor's country to govern the receivables purchase agreement, and (e) the sale complies with the requirements of the obligor's country, will a court in your jurisdiction recognise that sale as being effective against the seller and other third parties (such as creditors or insolvency administrators of the seller) without the need to comply with your jurisdiction's own sale requirements?

While Finnish bankruptcy law would determine which assets are available to the creditors of the seller, the "*lex rei sitae*" principle would normally be applied. If the requirements of the obligor's country are met, a court in Finland would therefore recognise the sale as being effective against all the parties.

3.5 Example 4: If (a) the obligor is located in your jurisdiction but the seller is located in another country, (b) the receivable is governed by the law of the seller's country, (c) the seller and the purchaser choose the law of the seller's country to govern the receivables purchase agreement, and (d) the sale complies with the requirements of the seller's country, will a court in your jurisdiction recognise that sale as being effective against the obligor and other third parties (such as creditors or insolvency administrators of the obligor) without the need to comply with your jurisdiction's own sale requirements?

A court in Finland would recognise the sale as being effective between the seller and the purchaser, and, pursuant to Article 14 of the Rome I Regulation, also against the obligor. However, as regards

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to enforceability against the seller's creditors or its successors, if the laws of the seller's domicile refer to the laws of Finland, Finland's sale requirements would have to be followed.

3.6 Example 5: If (a) the seller is located in your jurisdiction (irrespective of the obligor's location), (b) the receivable is governed by the law of your jurisdiction, (c) the seller sells the receivable to a purchaser located in a third country, (d) the seller and the purchaser choose the law of the purchaser's country to govern the receivables purchase agreement, and (e) the sale complies with the requirements of the purchaser's country, will a court in your jurisdiction recognise that sale as being effective against the seller and other third parties (such as creditors or insolvency administrators of the seller, any obligor located in your jurisdiction and any third party creditor or insolvency administrator of any such obligor)?

The sale would not be effective against the seller's creditors or its successors unless the sale is perfected in accordance with the laws of the obligor's domicile. Effectiveness against the obligor would, pursuant to Article 14 of the Rome I Regulation, be determined in accordance with the law governing the receivable, being in this example Finnish law and therefore requiring a notice to the obligor as described in question 4.4.

4 Asset Sales

4.1 Sale Methods Generally. In your jurisdiction what are the customary methods for a seller to sell receivables to a purchaser? What is the customary terminology – is it called a sale, transfer, assignment or something else?

There must be a binding sale agreement between the seller and the purchaser. No formal requirements exist for a sale agreement, but, for evidence purposes, a written agreement is of course recommendable. The terms sale, transfer and assignment are all commonly used.

4.2 Perfection Generally. What formalities are required generally for perfecting a sale of receivables? Are there any additional or other formalities required for the sale of receivables to be perfected against any subsequent good faith purchasers for value of the same receivables from the seller?

To achieve effectiveness of a transfer of ownership of receivables in relation to third-party creditors of the seller, in addition to a valid and binding sale agreement between the seller and the purchaser, there must be a due perfection of the transfer in accordance with the law applicable on the basis of the "*lex rei sitae*" rule and where that law is Finnish law, further in accordance with the rules applicable to the relevant category of asset. Under Finnish law, the transfer of a receivable is perfected by means of serving the debtor with a qualifying notice of assignment or, in respect of receivables in the form of negotiable promissory notes, by a physical transfer of the promissory note to the possession of the purchaser, with the exception that where the seller is a bank, the sale of a promissory note is effective against other creditors of that bank even though the promissory note remains in the custody of that bank. A notice of assignment should clearly state that the receivable (which must be sufficiently individualised) has been transferred, and also state the name of the transferee and date of the transfer. There are no other formalities required to ensure effectiveness of the sale of receivables against subsequent purchasers that were not and should not have been aware of the first sale having taken place.

In respect of a transfer of receivables that have not yet been earned, i.e., future receivables, historically the prevailing view in Finnish legal literature and doctrine has been that a one-off notification to the debtor at the outset is not likely to suffice but instead each individual assignment should be separately notified to the relevant debtor upon the receivable becoming earned. More recent legal literature and doctrines, however, seem to support the view that a transfer of identifiable but yet unearned receivables (in respect of which a one-off notification is duly served on the debtor) would be effective in relation to third-party creditors of the seller, without the need to take new perfection steps when such receivables have been earned. However, there is no established legal rule in this respect.

Due to commercial considerations, the parties may sometimes feel comfortable with notifying the debtors of the transfer only upon the occurrence of a trigger event. The critical question then, is when the trigger event occurs, so as to enable timely perfection prior to insolvency.

4.3 Perfection for Promissory Notes, etc. What additional or different requirements for sale and perfection apply to sales of promissory notes, mortgage loans, consumer loans or marketable debt securities?

The perfection of a transfer of ownership in negotiable promissory notes is carried out by physical delivery of the promissory notes to the purchaser, with the exception that where the seller is a bank, the sale of a promissory note is effective against other creditors of that bank even though the promissory note remains in the custody of that bank. Marketable debt securities are typically dematerialised in the form of book-entry securities, and perfection of a transfer of ownership in book-entry securities is carried out by registering the book-entry securities on the purchaser's book-entry account.

As regards perfection of an assignment of mortgage loans, perfection is achieved either by serving the debtor a notice of assignment or by delivery of the negotiable promissory note as set out in question 4.2 above, depending on the form of the receivables contract. The right to any collateral securing the loan is transferred to the purchaser simultaneously unless otherwise agreed either between the seller and the purchaser or between the seller and the security provider.

A consumer must be notified of the transfer (even if, e.g., the transfer is otherwise intended to be perfected only on the occurrence of a trigger event), unless the seller continues to act as a representative of the seller *vis-à-vis* the consumer.

4.4 Obligor Notification or Consent. Must the seller or the purchaser notify obligors of the sale of receivables in order for the sale to be effective against the obligors and/or creditors of the seller? Must the seller or the purchaser obtain the obligors' consent to the sale of receivables in order for the sale to be an effective sale against the obligors? Whether or not notice is required to perfect a sale, are there any benefits to giving notice – such as cutting off obligor set-off rights and other obligor defences?

By default, receivables are freely transferable without the obligor's consent, and this is the case if transfers are not expressly prohibited or permitted. However, the parties are free to restrict the transferability or to agree that the obligor's consent is required. The insolvency

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of the obligor does not affect the situation (unless contractually so agreed), while the seller's insolvency would generally prevent the transfer from being perfected by the notice.

The notice of assignment and, in the case of receivables with restricted transferability, the consent of the obligor, are necessary: (i) to allow the purchaser to enforce the debts directly against the obligor; (ii) to prevent the obligor and the seller from amending the receivable contract without the purchaser's consent; (iii) to restrict the obligor's right to set off receivables against the obligations of the seller to the obligor; and (iv) to require the obligor to pay the purchaser rather than the seller. Even after receipt of the notice of assignment, the obligor has, under certain circumstances, the right to set off receivables against the obligations of the seller to the obligor.

As regards negotiable promissory notes, it is not a formal requirement to notify the obligor of the sale in order for the sale to be effective against the obligor, but instead the promissory notes must be delivered to the purchaser to achieve the same effect. However, to avoid that payments are made to the seller or that the receivables contract is amended by the seller and the obligor, it is also recommended that an obligor under a negotiable promissory note be notified.

4.5 Notice Mechanics. If notice is to be delivered to obligors, whether at the time of sale or later, are there any requirements regarding the form the notice must take or how it must be delivered? Is there any time limit beyond which notice is ineffective – for example, can a notice of sale be delivered after the sale, and can notice be delivered after insolvency proceedings have commenced against the obligor or the seller? Does the notice apply only to specific receivables or can it apply to any and all (including future) receivables? Are there any other limitations or considerations?

The notice must sufficiently identify the transferred receivables and the transferee and, as discussed below in more detail, should instruct the obligor to pay only to the transferee. It is recommended that the notice is delivered in writing for evidence purposes. Further, it is also recommended that a written acknowledgment of the notice is required so as to confirm the obligor's awareness of the sale. In respect of receivables evidenced by invoices, the usual practice is to print or stamp the notification and payment instructions on the invoice.

Future receivables can be included in a notice, but it is not clear under Finnish law whether a further notice would nevertheless be required to be delivered to the obligor after the receivable has been earned to achieve perfection. Referring to question 4.10, it must be noted that a transfer of "future" or "unearned" receivables is generally not binding upon the insolvency of the Finnish seller despite a sale agreement which is binding between the parties.

A notice delivered after the commencement of insolvency proceedings against the seller would be regarded as ineffective, and the receivables would be deemed to belong to the seller's estate.

If the obligor is subject to insolvency proceedings, proof regarding the sale of receivables must be provided to the obligor's estate (e.g., in the case of bankruptcy, by way of a lodgement letter). The content requirements for the lodgement letter (or equivalent) and administration thereof are stipulated in the relevant insolvency law.

4.6 Restrictions on Assignment – General Interpretation. Will a restriction in a receivables contract to the effect that "None of the [seller's] rights or obligations under this Agreement may be transferred or assigned without the consent of the [obligor]" be interpreted as prohibiting a transfer of receivables by the seller to the purchaser? Is the result the same if the restriction says "This Agreement may not be transferred or assigned by the [seller] without the consent of the [obligor]" (i.e., the restriction does not refer to rights or obligations)? Is the result the same if the restriction says "The obligations of the [seller] under this Agreement may not be transferred or assigned by the [seller] without the consent of the [obligor]" (i.e., the restriction does not refer to rights)?

Unless the circumstances and/or the actual behaviour of the parties indicate otherwise, contractual language prohibiting the assignment of the seller's rights or obligations under an agreement will be taken to mean that the rights may not and, therefore, cannot be assigned. Similarly, contractual language prohibiting the "agreement" from being assigned would also likely be construed as a prohibition against the assignment of the seller's rights, which, therefore, could not be assigned.

4.7 Restrictions on Assignment; Liability to Obligor. If any of the restrictions in question 4.6 are binding, or if the receivables contract explicitly prohibits an assignment of receivables or "seller's rights" under the receivables contract, are such restrictions generally enforceable in your jurisdiction? Are there exceptions to this rule (e.g., for contracts between commercial entities)? If your jurisdiction recognises restrictions on sale or assignment of receivables and the seller nevertheless sells receivables to the purchaser, will either the seller or the purchaser be liable to the obligor for breach of contract or tort, or on any other basis?

As discussed above in question 4.4, the parties are free to restrict assignment and such restrictions are generally enforceable. The seller would be liable for breach of contract to the obligor. If the purchaser was aware of the transfer prohibition, it is likely that the transfer is not binding on the obligor. This is less clear if the purchaser acted in good faith or if the assignment prohibition is unreasonable.

4.8 Identification. Must the sale document specifically identify each of the receivables to be sold? If so, what specific information is required (e.g., obligor name, invoice number, invoice date, payment date, etc.)? Do the receivables being sold have to share objective characteristics? Alternatively, if the seller sells *all* of its receivables to the purchaser, is this sufficient identification of receivables? Finally, if the seller sells *all* of its receivables *other than* receivables owing by one or more specifically identified obligors, is this sufficient identification of receivables?

Yes, the sale agreement must contain sufficient information to identify the transferred receivables; such information can be details of the underlying receivable contract or invoice and the name of the obligor but identification without the name of the obligor may also be possible. The receivables being sold do not have to share objective characteristics. The sale of all, or all but certain specified receivables, would most likely not be sufficient identification.

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4.9 Recharacterisation Risk. If the parties describe their transaction in the relevant documents as an outright sale and explicitly state their intention that it be treated as an outright sale, will this description and statement of intent automatically be respected or is there a risk that the transaction could be characterised by a court as a loan with (or without) security? If recharacterisation risk exists, what characteristics of the transaction might prevent the transfer from being treated as an outright sale? Among other things, to what extent may the seller retain any of the following without jeopardising treatment as an outright sale: (a) credit risk; (b) interest rate risk; (c) control of collections of receivables; (d) a right of repurchase/redemption; (e) a right to the residual profits within the purchaser; or (f) any other term?

Although Finnish civil law in general can be characterised as fairly legalistic, the substance-over-form doctrine is well-established when assessing whether a sale of an asset should be considered as having been entered into for the purposes of creating a security interest over the asset in question. In a receivables securitisation, the insolvency estate of the seller could argue that the parties did not intend to transfer ownership of the receivables, but rather to create security over the receivables in order to secure the construed loan advanced by the purchaser to the seller. Unfortunately, Finnish case law does not clearly specify the grounds for recharacterising a particular transaction. As a matter of principle, the key question is whether the economic risks and rewards associated with ownership have, to a sufficient extent, been transferred to the purchaser. Various repurchase obligations, excessive reserve requirements, participation to residual profits within the purchaser and other similar features often encountered in securitisation transactions all serve as an indication that the seller has retained economic interest in the receivables; thus, they may endanger the true sale analysis.

Various collection agency arrangements may cause difficulties if the seller becomes insolvent. First, the continued receipt of collections by the seller could effectively be construed as evidence that the seller has not been deprived of its control over the receivables. This could be argued to adversely affect the true sale. Second, if collections have been commingled with the seller's other funds, then the collection funds would be considered part of the assets of the seller's insolvency estate. To overcome these challenges, a separate collection account should be established and collections accruing from the securitised receivables should be channelled to this separate bank account. Furthermore, effective controls should be put in place to prevent the seller from dealing with the money held in the collection account. Apart from contractual undertakings to such effect, there should be a cash sweep, preferably on a daily basis, from the collection account to a seller-remote transaction bank account. As an alternative, a pledge could be created over the collection account. As in the case of customer-debtor transfer notifications, the use of a collection agency would normally involve a trigger event mechanism whereby, after a trigger event, collections are directly channelled into a transaction bank account which is remote from the seller.

4.10 Continuous Sales of Receivables. Can the seller agree in an enforceable manner to continuous sales of receivables (i.e., sales of receivables as and when they arise)? Would such an agreement survive and continue to transfer receivables to the purchaser following the seller's insolvency?

The seller can agree to continuous sales of receivables, but each transfer will only become effective upon identification of the receivables and be subject to the perfection requirements discussed above under questions 4.2–4.5 and 4.8 above and question 4.11 below.

4.11 Future Receivables. Can the seller commit in an enforceable manner to sell receivables to the purchaser that come into existence after the date of the receivables purchase agreement (e.g., "future flow" securitisation)? If so, how must the sale of future receivables be structured to be valid and enforceable? Is there a distinction between future receivables that arise prior to *versus* after the seller's insolvency?

A transfer of "future" or "unearned" receivables is generally not binding upon the insolvency of the Finnish seller. Consequently, any receivables earned after the commencement of the seller's insolvency proceedings, as well as any receivables earned before the insolvency but in respect of which the transfer has not been perfected prior to the insolvency, would be considered the seller's property, despite a sale agreement which is binding between the parties. In determining whether a receivable is in existence or whether it is unearned, the decisive factor normally is whether the seller has fulfilled the contractual obligation that gives rise to the receivable. In the case of a trade receivable, for instance, the assessment is made based on whether the seller has delivered the goods to the customer-debtor, thus earning the receivable.

To ensure that the transfers are effective to as great an extent as possible, the sale should be structured so that transfers are perfected immediately when the receivable arises and again upon the receivables becoming earned. However, it should be noted that the effectiveness of the transfer of receivables arising or earned after the commencement of insolvency proceedings, would not be accomplished even in this structure.

4.12 Related Security. Must any additional formalities be fulfilled in order for the related security to be transferred concurrently with the sale of receivables? If not all related security can be enforceably transferred, what methods are customarily adopted to provide the purchaser the benefits of such related security?

This matter is not conclusively addressed in Finnish law, but views have been expressed in legal literature that the transfer of the collateral needs to be perfected in accordance with the rules applicable to the relevant category of assets, i.e., by serving the obligor a qualifying notice, by transfer of possession to the purchaser, or by registration.

4.13 Set-Off; Liability to Obligor. Assuming that a receivables contract does not contain a provision whereby the obligor waives its right to set-off against amounts it owes to the seller, do the obligor's set-off rights terminate upon its receipt of notice of a sale? At any other time? If a receivables contract does not waive set-off but the obligor's set-off rights are terminated due to notice or some other action, will either the seller or the purchaser be liable to the obligor for damages caused by such termination?

With regard to receivables documented as non-negotiable promissory notes, a notice of sale will cut off the obligor's right to set-off with a counterclaim against the seller, if (i) the counterclaim was acquired after receipt of the notice, or (ii) the counterclaim falls and is due for payment after both the transferred receivable and receipt of the notice. In case the obligor's counterclaim and the

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transferred receivable originate from the same legal relationship, the obligor may enjoy a wider right to set-off as described above.

In respect of receivables documented as negotiable promissory notes, the set-off right generally terminates upon perfected transfer of the notes.

The obligor's set-off rights cannot be terminated by the seller or the purchaser other than as described above, and such termination will not make the seller or the purchaser liable for damages (although the obligor will still hold its counterclaim against the seller).

4.14 Profit Extraction. What methods are typically used in your jurisdiction to extract residual profits from the purchaser?

The seller may subscribe to a class of notes which receive the residual income or, where the seller acts as servicer, a variable recovery fee may be used.

5 Security Issues

5.1 Back-up Security. Is it customary in your jurisdiction to take a "back-up" security interest over the seller's ownership interest in the receivables and the related security, in the event that an outright sale is deemed by a court (for whatever reason) not to have occurred and have been perfected (see question 4.9 above)?

No; under Finnish law the perfection requirements for a sale of receivables and the granting of a security interest over receivables are substantially the same.

5.2 Seller Security. If it is customary to take back-up security, what are the formalities for the seller granting a security interest in receivables and related security under the laws of your jurisdiction, and for such security interest to be perfected?

Please refer to questions 4.2–4.5 as regards the receivables, and to question 4.12 as regards the related security. Further, when creating security over a security interest, the original security provider would have to be notified before the security interest is given, and the seller cannot pledge the security interest as security for liabilities larger than those secured by the original security interest.

5.3 Purchaser Security. If the purchaser grants security over all of its assets (including purchased receivables) in favour of the providers of its funding, what formalities must the purchaser comply with in your jurisdiction to grant and perfect a security interest in purchased receivables governed by the laws of your jurisdiction and the related security?

Under Finnish law the perfection requirements for a sale of receivables and the granting of a security interest over receivables are substantially the same. Please refer to questions 4.2–4.5 as regards the receivables, and to question 4.12 as regards the related security.

For a Finnish pledgor, it is possible to grant security over substantially all of the pledgor's movable assets (including receivables) through an enterprise mortgage (Fi: *yrityskiinnitys*). The enterprise mortgage is, however, limited to the assets of the pledgor at the time of enforcement. It ranks also behind more specific security interests (such as pledges) in assets for which they compete, and in statutory insolvency proceedings a claim secured by an enterprise mortgage enjoys a priority of only up to 50% of the liquidation value of the assets covered by the enterprise mortgage.

5.4 Recognition. If the purchaser grants a security interest in receivables governed by the laws of your jurisdiction, and that security interest is valid and perfected under the laws of the purchaser's jurisdiction, will the security be treated as valid and perfected in your jurisdiction or must additional steps be taken in your jurisdiction?

Finnish courts normally apply the "*lex rei sitae*" principle to the effectiveness of a security interest in relation to, *inter alia*, third-party creditors, according to which principle effectiveness of a security interest over a receivable would generally be determined in accordance with the laws of the jurisdiction of the debtor of the receivable. If the obligor was based in Finland, the perfection of the transfer would generally be determined in accordance with the laws of Finland. Additional steps may therefore have to be taken, and as mentioned in question 3.3, a common precautionary measure is to comply with the requirements of all relevant jurisdictions should there be differences in the perfection requirements.

5.5 Additional Formalities. What additional or different requirements apply to security interests in or connected to insurance policies, promissory notes, mortgage loans, consumer loans or marketable debt securities?

The same requirements as for a sale of such assets apply (see questions 4.3 and 5.2) with the exception that security over marketable debt securities in the form of book-entry securities would be created by a pledge over the book-entry account on which such securities are recorded and such pledge would be perfected by recording a pledge on the book-entry account.

5.6 Trusts. Does your jurisdiction recognise trusts? If not, is there a mechanism whereby collections received by the seller in respect of sold receivables can be held or be deemed to be held separate and apart from the seller's own assets (so that they are not part of the seller's insolvency estate) until turned over to the purchaser?

Finnish law does not recognise the concept of a trust. If the seller receives funds in the capacity of servicer, it may be possible to separate these collections from the seller's own assets in an insolvency scenario if the collections are not commingled with the seller's assets. In practice, a separate account would most likely be needed. If, on the other hand, the collections are received in error (i.e., the obligor, having been instructed to pay to the purchaser, makes payments to the seller), the collections, if not commingled with the seller's own assets, would have to be turned over. Finally, if the collections are paid to a bank account which has been pledged and such pledge duly perfected (i.e., the seller has no access to the account), the collections would be held separate.

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5.7 Bank Accounts. Does your jurisdiction recognise escrow accounts? Can security be taken over a bank account located in your jurisdiction? If so, what is the typical method? Would courts in your jurisdiction recognise a foreign law grant of security (for example, an English law debenture) taken over a bank account located in your jurisdiction?

Contractual escrow account arrangements are possible under Finnish law, and it is also possible to take security over a bank account located in Finland. The typical method is a Finnish law pledge agreement, and the perfection requirement is notification to the account bank, blocking the pledgor's access to the bank account. For practical reasons, this perfection measure is typically postponed until the occurrence of a trigger event.

Subject to the qualifications under question 2.3 above, a Finnish court would recognise a foreign law security over a bank account, provided that the creation and effectiveness of the security would always be determined in accordance with Finnish law where the account bank is a Finnish entity.

5.8 Enforcement over Bank Accounts. If security over a bank account is possible and the secured party enforces that security, does the secured party control all cash flowing into the bank account from enforcement forward until the secured party is repaid in full, or are there limitations? If there are limitations, what are they?

The account bank may exercise a set-off right with respect to the cash held on the bank account, if the requirements for set-off were already met prior to perfection of the security over the bank account (see also question 4.13). A bank's right to set off cash held on a bank account is more limited in connection with statutory insolvency proceedings.

5.9 Use of Cash Bank Accounts. If security over a bank account is possible, can the owner of the account have access to the funds in the account prior to enforcement without affecting the security?

No. The pledgor must be prevented from being able to make withdrawals or in any other way deal with monies credited to the pledged account. However, the pledgee may agree, on a case-by-case basis, to release amounts covered by the pledge (provided, however, that such agreement is not granted as a matter of course).

If the pledgor needs to access the funds in order to operate its day-to-day business, a common solution is to include a provision that the pledgor will only be cut off from access to the account upon the occurrence of a trigger event. Such arrangement may be vulnerable to a clawback action on the basis that the perfection of the security has been delayed (see question 6.3).

6 Insolvency Laws

6.1 Stay of Action. If, after a sale of receivables that is otherwise perfected, the seller becomes subject to an insolvency proceeding, will your jurisdiction's insolvency laws automatically prohibit the purchaser from collecting, transferring or otherwise exercising ownership rights over the purchased receivables (a "stay of action")? If so, what generally is the length of that stay of action? Does the insolvency official have the ability to stay collection and enforcement actions until he determines that the sale is perfected? Would the answer be different if the purchaser is deemed to only be a secured party rather than the owner of the receivables?

Upon initiation of insolvency proceedings against the seller, the seller may no longer dispose of its assets. In the case of a duly perfected true sale, Finnish laws do not prohibit the purchaser from exercising ownership rights over the receivables as long as the assets of the purchaser are separable from the assets of the seller. Due perfection generally requires that the payment of receivables be directed to the purchaser or to a third party sufficiently remote from the seller, such as a collection agent or a bank account subject to a perfected pledge in favour of the purchaser or such collection agent. As regards future receivables in insolvency, please see question 4.11.

In the event that a transfer of receivables is recharacterised by a Finnish court upon insolvency of the seller, the transfer would most likely be treated as a loan secured by the receivables. In such case, the purchaser would, however, have first priority to receive payment for the 'loan' from the proceeds of the receivables, provided that due perfection has been carried out prior to the initiation of insolvency proceedings and there are no grounds for recovery of the "security".

In reorganisation proceedings, both the business operations and the debts of a company may be reorganised and restructured. The initiation of the reorganisation proceedings imposes a moratorium on all legal proceedings and other enforcement actions against the debtor. The district court's decision on the commencement of reorganisation proceedings results in a general prohibition on the payment, collection and execution of debts, which applies to all creditors. As a main rule, no creditor, including a secured creditor, has the right to enforce its rights in respect of any collateral, or to collect any debts after the initiation of the reorganisation. However, relief to the above rule may be granted to a secured creditor for enforcing its rights in respect of collateral, if (i) it is apparent that the secured asset is not necessary for the reorganisation proceedings, or (ii) the debtor is in default with interest payments and other credit payments falling due after the date of the reorganisation application or the debtor is liable for negligent care of the secured object or has omitted proper insuring of the security. The moratorium remains in force until the reorganisation plan has been confirmed.

In the case of bankruptcy, the purchaser, recharacterised as a secured creditor, would enjoy the proceeds of the receivables in respect of which the security has been perfected prior to the initiation of the insolvency proceedings to the extent necessary to amortise the underlying construed debt, but would have to take the unsecured

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creditors' interests into consideration when exercising any of its rights as the holder of the security interest. The insolvency official may order the enforcement of security to be stopped for a period of up to two months if the secured creditor's right to the receivables needs to be clarified or the stay is necessary for protecting the bankruptcy estate's interests.

6.2 Insolvency Official's Powers. If there is no stay of action, under what circumstances, if any, does the insolvency official have the power to prohibit the purchaser's exercise of its ownership rights over the receivables (by means of injunction, stay order or other action)?

In the case of a duly perfected true sale, under no circumstances would an insolvency official have the power to prohibit a purchaser's ownership rights over receivables, provided that the assets of the purchaser are separable from the assets belonging to the seller. In the case of recharacterisation, the secured creditor may be subject to up to two months' prohibition to exercise its rights to enforce the security mentioned above.

6.3 Suspect Period (Clawback). Under what facts or circumstances could the insolvency official rescind or reverse transactions that took place during a "suspect" or "preference" period before the commencement of the seller's insolvency proceedings? What are the lengths of the "suspect" or "preference" periods in your jurisdiction for (a) transactions between unrelated parties, and (b) transactions between related parties? If the purchaser is majority-owned or controlled by the seller or an affiliate of the seller, does that render sales by the seller to the purchaser "related party transactions" for purposes of determining the length of the suspect period? If a parent company of the seller guarantee's the performance by the seller of its obligations under contracts with the purchaser, does that render sales by the seller to the purchaser "related party transactions" for purposes of determining the length of the suspect period?

A transaction can be revoked if the transaction unduly favours a particular creditor to the detriment of another creditor, or transfers property out of the reach of the creditors, or increases the debts of the debtor to the detriment of the creditors, always provided: (i) that the debtor was insolvent at the time the transaction was concluded, or the transaction contributed to the debtor's insolvency; and (ii) that the other party knew or should have known of the insolvency or of the impact of such transaction on the debtor's financial state, as well as of the circumstances due to which the transaction was unsuitable. If such a transaction was concluded more than five years before the application for bankruptcy or reorganisation was filed with the competent court, the transaction may be revoked only if the secured party was someone closely related to the debtor.

In the case of recharacterisation of a receivables securitisation, any security interest granted can also be recovered by the grantor's bankruptcy estate or by the administrator of the grantor in reorganisation, if such security interest was perfected within a certain period of time prior to the commencement of the insolvency and provided that: (i) such security interest was not agreed on at the time the debt came into existence; or (ii) the transfer of possession, notice of assignment or other means of perfecting the security interest was not carried out without undue delay after the origination of the debt. An administrator, receiver or creditor of the debtor may bring an action for recovery.

The suspect period for the granting of security is three months between unrelated parties and two years between related parties. In case the purchaser is an affiliate of, or majority owned or otherwise subject to substantial control by, the seller, a transaction between the seller and such purchaser would be regarded as a related party transaction for the purposes of Finnish clawback rules. A guarantee by the seller's parent (provided that the parent is also unrelated to the purchaser) should not.

6.4 Substantive Consolidation. Under what facts or circumstances, if any, could the insolvency official consolidate the assets and liabilities of the purchaser with those of the seller or its affiliates in the insolvency proceeding? If the purchaser is owned by the seller or by an affiliate of the seller, does that affect the consolidation analysis?

Each company will be strictly treated as an isolated economic entity for Finnish insolvency law purposes, but there is limited case law where a parent entity has been found liable for specific obligations of its subsidiary. Also in circumstances where collections have been commingled with the seller's other funds, the collection funds would be considered part of the assets of the seller's insolvency estate (see question 4.9, second paragraph).

6.5 Effect of Insolvency on Receivables Sales. If insolvency proceedings are commenced against the seller in your jurisdiction, what effect do those proceedings have on (a) sales of receivables that would otherwise occur after the commencement of such proceedings, or (b) on sales of receivables that only come into existence after the commencement of such proceedings?

A sale (or, in case of recharacterisation, a pledge) of receivables becomes effective in relation to third-party creditors of the seller/pledgor upon perfection of the sale/pledge. Upon initiation of insolvency proceedings, the relevant debtor may no longer dispose of its assets. Consequently, the effect of the initiation of insolvency proceedings in respect of the seller/pledgor of future receivables is that any receivables not earned, as well as any receivables earned but in respect of which the transfer/pledge has not been perfected at that time, will belong to the bankruptcy estate of the seller.

6.6 Effect of Limited Recourse Provisions. If a debtor's contract contains a limited recourse provision (see question 7.3 below), can the debtor nevertheless be declared insolvent on the grounds that it cannot pay its debts as they become due?

While the definition of "insolvency" slightly varies depending on the context in which insolvency is evaluated (e.g., whether for Finnish corporate law purposes or for Finnish insolvency law purposes), the assessment whether a Finnish debtor is/was insolvent has generally been based on a longer-term evaluation on the debtor's overall financial situation. Therefore, it is not possible to directly exclude insolvency by using any particular contractual language, although limited recourse provisions could serve as evidence of the actual solvency of the debtor. Further and more generally, by appropriately restricting the debtor's business activities (and assuming that the debtor adheres to those restrictions), the creditors may reduce the likelihood that the circumstances that would constitute insolvency for the debtor would arise.

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7 Special Rules

7.1 Securitisation Law. Is there a special securitisation law (and/or special provisions in other laws) in your jurisdiction establishing a legal framework for securitisation transactions? If so, what are the basics? Is there a regulatory authority responsible for regulating securitisation transactions in your jurisdiction?

No, Finland has not enacted any such law, but at the EU level the Capital Requirements Regulation includes complex provisions regarding capital adequacy and exposure requirements in connection with securitisation, and similar requirements are included in various laws applicable to certain regulated entities in Finland. It should be also noted that further EU level legislative measures on securitisation have also been initiated within the framework of the European Commission's Capital Markets Union Action Plan. There is no regulatory authority responsible for regulating securitisation transactions in Finland.

7.2 Securitisation Entities. Does your jurisdiction have laws specifically providing for establishment of special purpose entities for securitisation? If so, what does the law provide as to: (a) requirements for establishment and management of such an entity; (b) legal attributes and benefits of the entity; and (c) any specific requirements as to the status of directors or shareholders?

No, Finland does not have such laws.

7.3 Location and form of Securitisation Entities. Is it typical to establish the special purpose entity in your jurisdiction or offshore? If in your jurisdiction, what are the advantages to locating the special purpose entity in your jurisdiction? If offshore, where are special purpose entities typically located for securitisations in your jurisdiction? What are the forms that the special purpose entity would normally take in your jurisdiction and how would such entity usually be owned?

Securitisation entities are not typically established in Finland, although Irish special purpose entities have recently been used in securitisations involving Finnish assets.

7.4 Limited-Recourse Clause. Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) limiting the recourse of parties to that agreement to the available assets of the relevant debtor, and providing that to the extent of any shortfall the debt of the relevant debtor is extinguished?

A contractual limitation of the liabilities to certain funds of an entity would be valid as such between such entity and the other contracting parties, but enforcement of such a provision could be limited by general principles of equity.

7.5 Non-Petition Clause. Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) prohibiting the parties from: (a) taking legal action against the purchaser or another person; or (b) commencing an insolvency proceeding against the purchaser or another person?

An agreement not to take legal action would as such be valid as between the parties thereto, but could result in an unreasonable outcome and might therefore be unenforceable due to general principles of equity.

7.6 Priority of Payments "Waterfall". Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) distributing payments to parties in a certain order specified in the contract?

Generally yes, although if the party making the distribution is subject to insolvency proceedings, it is possible that the insolvency administrator would ignore the waterfall and distribute funds in accordance with the general *pro rata* distribution principle applied in Finnish insolvency law.

7.7 Independent Director. Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) or a provision in a party's organisational documents prohibiting the directors from taking specified actions (including commencing an insolvency proceeding) without the affirmative vote of an independent director?

Generally, the parties would be allowed to agree on such limitations, although the directors owe certain fiduciary duties towards the company. It is unclear whether this prohibition would, e.g., cause an otherwise valid bankruptcy filing to be dismissed by the bankruptcy court. The most likely outcome is that the breaching party would be liable for damages but the action as such would stand, especially if the provision forces a director to act in breach of its fiduciary duties.

7.8 Location of Purchaser. Is it typical to establish the purchaser in your jurisdiction or offshore? If in your jurisdiction, what are the advantages to locating the purchaser in your jurisdiction? If offshore, where are purchasers typically located for securitisations in your jurisdiction?

The purchaser would usually be established offshore, e.g., in Ireland. As Finnish law does not recognise trusts, there is no clear method for establishing orphan or bankruptcy remote purchaser entities.

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8 Regulatory Issues

8.1 Required Authorisations, etc. Assuming that the purchaser does no other business in your jurisdiction, will its purchase and ownership or its collection and enforcement of receivables result in its being required to qualify to do business or to obtain any licence or its being subject to regulation as a financial institution in your jurisdiction? Does the answer to the preceding question change if the purchaser does business with more than one seller in your jurisdiction?

Mere purchase and ownership of receivables does not result in the purchaser being required to qualify to do business or obtain a licence for collecting receivables.

The Finnish Credit Institutions Act and guidelines issued by the Finnish Financial Supervisory Authority (the "FSA") indicate that, where a Finnish special purpose entity established solely for the purpose of acquiring and administering receivables is purchasing receivables from a Finnish credit institution on an other than incidental basis, the special purpose entity may, depending on the circumstances, be considered as conducting activities requiring a licence required under such Act. In such circumstances, it would be recommendable to conduct at least unofficial discussions with the FSA in order to ensure compliance with the Credit Institutions Act. If the purchaser buys receivables from multiple sellers in Finland, it is more likely that a licence under the Credit Institutions Act or the Debt Collection Business Act is required and it is more likely that this service is subject to VAT (see question 9.4 below).

8.2 Servicing. Does the seller require any licences, etc., in order to continue to enforce and collect receivables following their sale to the purchaser, including to appear before a court? Does a third-party replacement servicer require any licences, etc., in order to enforce and collect sold receivables?

Voluntary debt collection actions, i.e., actions aiming to get the debtor to voluntarily pay the matured debt of the creditor, are governed by the Finnish Act on Collection of Receivables. The debt collection business, defined as the collection of receivables on behalf of a third party, as well as the collection of the collector's own receivables when it is apparent that such receivables have been obtained by the collector exclusively for the purpose of collecting them, is, in addition to the Act on Collection of Receivables, also governed by the Finnish Debt Collection Business Act and requires a licence. Appearing before a court does not require a separate licence.

8.3 Data Protection. Does your jurisdiction have laws restricting the use or dissemination of data about or provided by obligors? If so, do these laws apply only to consumer obligors or also to enterprises?

When dealing with receivables where the debtors are individuals, data protection is an issue to address if the transaction entails the transfer of personal data from the seller to the special purpose entity. Even if the transaction would entail some transfer of customer-related data, it should normally be possible to structure the transaction so that no filings or approvals with the data protection authorities are required. Prior discussions with the authorities may, however, be recommendable.

The Finnish Personal Data Act (the "PDA") implements the EU Data Protection Directive (95/46/EC) and is a general Act applicable to the use and transfer of personal data, i.e., information concerning a private individual, his or her personal characteristics and which information can be directly or indirectly identified as concerning such individual. The Finnish Personal Data Act will be repealed by the EU General Data Protection Regulation (679/2016) on 25 May 2018 ("GDPR"), which sharpens the requirements on lawful processing of personal data. Personal data legislation applies to personal data of all individuals irrespective of their status as consumers, but it does not apply to company data.

The general obligations provided by the GDPR to personal data controllers include, among others, lawfulness, transparency, accuracy and data minimisation requirements, as well as purpose limitation and data security. In principle, during and after the transaction, personal data of obligors cannot be processed for purposes that conflict with the original purposes of processing. In addition, the data transfers out of EU/EEA are restricted as provided in the GDPR.

Furthermore, the data subjects (obligors) have certain rights that should be guaranteed. The data subjects should receive sufficient information on the processing of their data, including the identity of the data controller. In transactions this information requirement may require notifications or other information procedures towards obligors when the debt is transferred to another creditor becoming data controller. In addition, the data subjects have the right to access their data and request deletion or correction of erroneous or unnecessary data.

8.4 Consumer Protection. If the obligors are consumers, will the purchaser (including a bank acting as purchaser) be required to comply with any consumer protection law of your jurisdiction? Briefly, what is required?

The Finnish Consumer Protection Act (the "CPA") is applicable, *inter alia*, to the provision of consumer credit. The CPA includes regulation on, e.g., the conditions for accelerating a consumer loan, the information that has to be provided to a consumer regarding the loan and the consumer's right to set-off against both the seller and the purchaser.

8.5 Currency Restrictions. Does your jurisdiction have laws restricting the exchange of your jurisdiction's currency for other currencies or the making of payments in your jurisdiction's currency to persons outside the country?

No, Finland does not have any such laws.

8.6 Risk Retention. Does your jurisdiction have laws or regulations relating to "risk retention"? How are securitisation transactions in your jurisdiction usually structured to satisfy those risk retention requirements?

No, Finland does not have any such laws or regulations.

8.7 Regulatory Developments. Have there been any regulatory developments in your jurisdiction which are likely to have a material impact on securitisation transactions in your jurisdiction?

No, there have been no regulatory developments in Finland which would be likely to have a material impact on securitisation transactions.

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9 Taxation

9.1 Withholding Taxes. Will any part of payments on receivables by the obligors to the seller or the purchaser be subject to withholding taxes in your jurisdiction? Does the answer depend on the nature of the receivables, whether they bear interest, their term to maturity, or where the seller or the purchaser is located? In the case of a sale of trade receivables at a discount, is there a risk that the discount will be recharacterised in whole or in part as interest? In the case of a sale of trade receivables where a portion of the purchase price is payable upon collection of the receivable, is there a risk that the deferred purchase price will be recharacterised in whole or in part as interest? If withholding taxes might apply, what are the typical methods for eliminating or reducing withholding taxes?

Finnish withholding tax is generally not levied on payments on receivables to a non-resident purchaser. In a typical securitisation situation, i.e., where the securitised receivables qualify as, e.g., account receivables from foreign trade activities or loans taken abroad, this will apply to all forms of payments, including interest.

The location of the purchaser, the nature of the receivables, their term to maturity or the purchase price for the receivables should not affect the assessment of whether there is any withholding tax obligation.

9.2 Seller Tax Accounting. Does your jurisdiction require that a specific accounting policy is adopted for tax purposes by the seller or purchaser in the context of a securitisation?

A specific accounting policy does not need to be adopted in order to qualify for the withholding tax exemption described in question 9.1.

9.3 Stamp Duty, etc. Does your jurisdiction impose stamp duty or other transfer or documentary taxes on sales of receivables?

Finnish transfer tax is generally payable at a rate of 1.6% on the sale of receivables that qualify as securities for Finnish tax purposes, unless the transfer takes place through the Helsinki Stock Exchange or an equivalent exchange, or if both transaction parties are non-residents. Finnish branches of foreign credit institutions and certain foreign investment service companies are considered as residents for transfer tax purposes. Different rules apply also to, e.g., shares in real estate companies.

However, the only debt instruments that qualify as securities for Finnish transfer tax purposes are bonds whose interest is determined based on the operating result or dividend distribution of the issuer, or that entitle a share of the annual profit of the issuer.

The transfer tax, if any, is payable by the transferee. If the transferee is a non-resident or a foreign credit institution, or certain foreign investment service company having no permanent establishment in Finland, the transferor is liable for the payment of the tax by the transferee.

9.4 Value Added Taxes. Does your jurisdiction impose value added tax, sales tax or other similar taxes on sales of goods or services, on sales of receivables or on fees for collection agent services?

Value added tax ("VAT") is a general tax on consumption levied on goods and services supplied in Finland by businesses, on the import of goods into Finland, and on intra-Community acquisitions. As a rule all commercial selling of goods and services in Finland is subject to VAT.

The standard rate of VAT is currently 24%. Certain types of goods and services are excluded from VAT. Among the excluded services are financial and insurance services such as securities trading and the sale of receivables.

However, collection and factoring services are not tax-exempt financial services and, thus, VAT at 24% is imposed on any compensation paid for such services. Furthermore, if the services are rendered for a foreign entity having no permanent establishment in Finland, the fees are charged without Finnish VAT if the reverse charge mechanism applies.

In securitisation of receivables the VAT treatment of the different services as tax-exempt financial services and/or VAT-taxable factoring or collecting services depends on the individual circumstances of the transaction and may be subject to interpretation.

9.5 Purchaser Liability. If the seller is required to pay value-added tax, stamp duty or other taxes upon the sale of receivables (or on the sale of goods or services that give rise to the receivables) and the seller does not pay, then will the taxing authority be able to make claims for the unpaid tax against the purchaser or against the sold receivables or collections?

Claims will not be made against the purchaser merely because the seller fails to pay its own VAT, asset transfer tax or similar tax. However, the purchaser can be liable to pay VAT if a so-called reverse charge mechanism is applicable.

9.6 Doing Business. Assuming that the purchaser conducts no other business in your jurisdiction, would the purchaser's purchase of the receivables, its appointment of the seller as its servicer and collection agent, or its enforcement of the receivables against the obligors, make it liable to tax in your jurisdiction?

Non-residents are liable to pay Finnish tax only on income derived from Finland. Income derived from Finland is, e.g., income from business or professional activities carried out in Finland, or dividends or interest paid by a Finnish entity.

Furthermore, tax on income deriving from Finland is subject to mitigation based on double tax treaties. Generally, Finland's double tax treaties follow the OECD model convention.

The mere purchase and enforcement of the receivables should not, as such, create a permanent establishment or make the purchaser liable to pay tax in Finland. However, should the seller be appointed as a service and collection agent of the purchaser, a permanent establishment could be held to exist for Finnish tax purposes

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provided that such an agent would also be authorised to conclude contracts in the name of the purchaser, and if it would habitually exercise this authority. Should this be the case and the seller were regarded as the dependent agent of the purchaser, a permanent establishment would generally exist for Finnish tax purposes. If the seller were construed as the independent agent of the purchaser, a permanent establishment would generally exist for Finnish tax purposes if the service and collection services carried out by the seller would be held to go beyond the ordinary course of its business.

9.7 Taxable Income. If a purchaser located in your jurisdiction receives debt relief as the result of a limited recourse clause (see question 7.3 above), is that debt relief liable to tax in your jurisdiction?

A waiver of a receivable which is considered to have no value for the creditor should, as a rule, not be considered as taxable income for the debtor. As a receivable which cannot be collected from the debtor should generally be considered to have no value from the creditor's perspective, debt relief related to such debt should thus not be considered as taxable income in Finland for a Finnish debtor. However, if the limited recourse clause would not be considered valid, and the receivable therefore not entirely worthless for the creditor, the waiver of such receivable may be considered as taxable income for the Finnish debtor.

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1 Receivables Contracts

1.1 Formalities. In order to create an enforceable debt obligation of the obligor to the seller: (a) is it necessary that the sales of goods or services are evidenced by a formal receivables contract; (b) are invoices alone sufficient; and (c) can a binding contract arise as a result of the behaviour of the parties?

As a general principle of French law, it is not necessary that the seller and the debtor enter into a formal receivables contract to evidence the sale of goods or services. Therefore, invoices, a historic relationship or any other type of exchange of consent between the seller and the debtor, including oral agreement, are sufficient to evidence a valid debt obligation.

Notwithstanding the foregoing, the enforceability of the debt obligation of the debtor to the seller is a question of evidence. Under French law, rules of evidence are different depending on the status of the parties and of their relationship.

In summary, evidence of a relationship between commercial parties (i.e. business entities) can be brought by any means. In this respect, invoices or durable business relationships can be regarded as perfectly relevant presumptions of the existence of a contract and therefore of a perfected debt obligation. Between non-commercial parties (i.e. individuals), a written document is necessary to prove the existence of a contract of an amount greater than EUR 1,500. Finally, if the relationship is entered into between a commercial party and a non-commercial party, the non-commercial party shall have the right to produce evidence of a contract and therefore of a perfected debt obligation by any means, whereas the commercial party may only use the rules of the French Civil Code.

In theory, a binding contract may result from the behaviour of the parties. However, it is unlikely that a receivable suitable for a securitisation can be created by the mere behaviour of the parties.

1.2 Consumer Protections. Do your jurisdiction's laws: (a) limit rates of interest on consumer credit, loans or other kinds of receivables; (b) provide a statutory right to interest on late payments; (c) permit consumers to cancel receivables for a specified period of time; or (d) provide other noteworthy rights to consumers with respect to receivables owing by them?

Under the French Monetary and Financial Code, a loan granted to a consumer shall not carry an interest rate higher than a specified interest rate (*taux d'usure*). If the interest rate does exceed such a limit, the bank, having granted the loan, is liable for a penalty of up to two years' imprisonment or a fine of up to EUR 300,000. However, such a limit does not apply to corporate loans or loans granted to professionals under certain conditions.

As regards interest on late payments, the French Civil Code provides a statutory right to interest on late payment at a minimum interest rate fixed by governmental decree on an annual basis.

A loan granted to a consumer involves certain risks for the lenders, in particular under the provisions of the French Consumer Code. Pursuant to those provisions (*procédures de surendettement et de rétablissement personnel*), a consumer may request and obtain, from a competent court, a moratorium and/or reduction of its debt and related interest. Moreover, under certain circumstances and conditions, the consumer having borrowed money from a credit institution may obtain the outright cancellation of its entire debts owed to such credit institution.

1.3 Government Receivables. Where the receivables contract has been entered into with the government or a government agency, are there different requirements and laws that apply to the sale or collection of those receivables?

French law authorises the sale of receivables to a debtor which is a public body, including the government or a government agency.

A sale of receivables to a public entity is not subject to specific principles. However, it is worth noting that the provisions relating to the sale of receivables shall be combined with the specific rules applicable to such public entities.

As regards the enforceability of a sale of receivables itself, such sale must be notified to the public accountant (*comptable public*) of the public entity to which the receivable contract refers, and must be accompanied with the single original (*exemplaire unique*) of the receivable contract or a certificate of transferability (*certificat de cessibilité*), where such a contract is a public procurement.

Furthermore, the French Dailly Law expressly refers to public bodies. Under the French Dailly Law, the debtor may officially accept the sale of its debt to a third party. Such an acceptance creates a direct relationship between the debtor and the purchaser and must be duly authorised by the debtor's deliberative assembly where the debtor is a public body. In the specific context of public-private partnership agreements, the French Monetary and Financial Code provides that such an agreement may stipulate that certain receivables relating to the investment costs of a project are irrevocable once the public debtor has stated that such investments have been made. As a

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consequence, after the transfer of such receivables to the purchaser, the debtor is prohibited from setting off the fraction of receivable which relates to the investment costs against any other debt.

The above-mentioned "acceptance" procedure provided by the French Dailly Law historically benefitted to credit institutions only. Such benefit has been extended to French financing vehicles (comprising securitisation vehicles and specialised financing vehicles) thanks to *Ordonnance* n°2017-1432 of 4 October 2017 (see questions 4.1(iv), 6.3, 7.2 and 8.2 for further developments on these vehicles).

It is a longstanding principle that enforcement procedures provided by the French Code of Civil Procedure cannot be implemented against any public entity. Therefore, the enforcement of a sale of receivables against any public debtor will be subject to specific administrative proceedings (the Purchaser shall ask Administrative Courts to order an injunction, a periodic penalty payment or a fine).

2 Choice of Law – Receivables Contracts

2.1 No Law Specified. If the seller and the obligor do not specify a choice of law in their receivables contract, what are the main principles in your jurisdiction that will determine the governing law of the contract?

France has ratified the Rome Convention, dated 19 June 980 on the law applicable to contractual obligations (the *Rome Convention*), which has been implemented in Regulation (EC) No 593/2008 of the European Parliament and of the Council of 17 June 2008 on the law applicable to contractual obligations (the *Rome I Regulation*). According to the Rome I Regulation, when the parties do not specify a choice of law: (a) a contract for the sale of goods shall be governed by the law of the country where the seller has his habitual residence; (b) a contract for the provision of services shall be governed by the law of the country where the service provider has his habitual residence; (c) a contract relating to a right *in rem* in immovable property or to a tenancy of immovable property shall be governed by the law of the country where the property is situated; (d) notwithstanding point (c), a tenancy of immovable property concluded for temporary private use for a period of no more than six consecutive months shall be governed by the law of the country where the landlord has his habitual residence, provided that the tenant is a natural person and has his habitual residence in the same country; (e) a franchise contract shall be governed by the law of the country where the franchisee has his habitual residence; (f) a distribution contract shall be governed by the law of the country where the distributor has his habitual residence; (g) a contract for the sale of goods by auction shall be governed by the law of the country where the auction takes place, if such a place can be determined; and (h) a contract concluded within a multilateral system which brings together or facilitates the bringing together of multiple third-party buying and selling interests in financial instruments, as defined by article 4(1), point (17) of Directive 2004/39/EC, in accordance with non-discretionary rules and governed by a single law, shall be governed by that law.

Where the contract is not covered by the above categories or where the elements of the contract would be covered by more than one of points (a) to (h), the contract shall be governed by the law of the country where the party required to effect the characteristic performance of the contract has his habitual residence. In addition, where it is clear from all the circumstances of the case that the contract is manifestly more closely connected with a country other than that indicated above, the law of that other country shall apply. Where the law applicable cannot be determined pursuant to the above, the contract shall be governed by the law of the country with which it is most closely connected. Specific rules apply for contract of carriage, contract with consumers, insurances contracts and individual employment contracts.

2.2 Base Case. If the seller and the obligor are both resident in your jurisdiction, and the transactions giving rise to the receivables and the payment of the receivables take place in your jurisdiction, and the seller and the obligor choose the law of your jurisdiction to govern the receivables contract, is there any reason why a court in your jurisdiction would not give effect to their choice of law?

The Rome I Regulation applies, subject to certain exceptions, to commercial or civil contractual obligations in any situation involving a conflict between the laws of different countries. In relation to the base case above, there would be no conflict of laws in the absence of relevant elements of foreign law. Under the provisions of the French Civil Code, the French law chosen by the seller and the debtors in the receivable contracts will become the mandatory law applying to their relations and such choice will be recognised as a valid choice of law by a French court.

2.3 Freedom to Choose Foreign Law of Non-Resident Seller or Obligor. If the seller is resident in your jurisdiction but the obligor is not, or if the obligor is resident in your jurisdiction but the seller is not, and the seller and the obligor choose the foreign law of the obligor/seller to govern their receivables contract, will a court in your jurisdiction give effect to the choice of foreign law? Are there any limitations to the recognition of foreign law (such as public policy or mandatory principles of law) that would typically apply in commercial relationships such as that between the seller and the obligor under the receivables contract?

According to the Rome I Regulation, a contract shall be governed by the law chosen by the parties. Thus, the seller and the debtor are free to choose a law other than French law to govern the receivable contract and the receivables. However, this is with the proviso that, where all the other elements relevant to the situation at the time of the choice are connected with France only, such choice of law will not prejudice the application of mandatory rules (*ordre public*) in France.

Subject to that proviso, the choice of a foreign law to govern the receivables contract will be recognised as a valid choice of law by a French court.

This is also subject to specific rules that apply to contract of carriage, consumers' contracts, insurance contracts and individual employment contracts.

In particular, in relation to consumers' contracts, as a general principle a contract concluded by a natural person for a purpose which can be regarded as being outside his trade or profession (the "consumer") with another person acting in the exercise of his trade or profession (the "professional"), shall be governed by the law of the country where the consumer has his habitual residence, provided that the professional: (a) pursues his commercial or professional activities in the country where the consumer has his habitual residence; or (b) by any means, directs such activities to that country or to several countries including that country, and the contract falls within the scope of such activities. Notwithstanding this general principle, the parties may choose the law applicable to a contract, subject to the same proviso as above and provided further

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that such a choice may not, however, have the result of depriving the consumer of the protection afforded to him by provisions that cannot be derogated from by agreement by virtue of the law which, in the absence of choice, would have been applicable on the basis of that general principle.

3 Choice of Law – Receivables Purchase Agreement

3.1 Base Case. Does your jurisdiction's law generally require the sale of receivables to be governed by the same law as the law governing the receivables themselves? If so, does that general rule apply irrespective of which law governs the receivables (i.e., your jurisdiction's laws or foreign laws)?

French law does not require the sale of receivables to be governed by the same law governing the receivables. Pursuant to article 14 of the Rome I Regulation, the law applicable to the sale of receivables can be freely chosen by the seller and the purchaser of the receivables. However, article 14 provides that the law governing the receivables will determine a certain number of important elements such as the possibility to assign the receivable, the relationship between the assignor and the debtor, the requirements for the assignment to be enforceable and the characteristics of a satisfactory payment by the debtor.

3.2 Example 1: If (a) the seller and the obligor are located in your jurisdiction, (b) the receivable is governed by the law of your jurisdiction, (c) the seller sells the receivable to a purchaser located in a third country, (d) the seller and the purchaser choose the law of your jurisdiction to govern the receivables purchase agreement, and (e) the sale complies with the requirements of your jurisdiction, will a court in your jurisdiction recognise that sale as being effective against the seller, the obligor and other third parties (such as creditors or insolvency administrators of the seller and the obligor)?

A French court will recognise such a sale as effective against the seller, the obligor and other third parties from a French law perspective, to the extent the formalities, if any, that apply to the mode of transfer chosen, are complied with (see question 4.1). This, however, assumes that the purchaser is duly authorised to acquire receivables in France (see question 8.1) and that the law applicable to it would not conflict with French law. Assuming that an insolvency proceeding would be opened in France, an insolvency administrator would not normally be considered a third party. It may have some grounds to invalidate an assignment of receivables in certain circumstances (see section 6) but it is a continuation of the seller and, therefore, bound by the assignment to the same extent as the seller.

3.3 Example 2: Assuming that the facts are the same as Example 1, but either the obligor or the purchaser or both are located outside your jurisdiction, will a court in your jurisdiction recognise that sale as being effective against the seller and other third parties (such as creditors or insolvency administrators of the seller), or must the foreign law requirements of the obligor's country or the purchaser's country (or both) be taken into account?

From a French law perspective, the same analysis as set out in respect of question 3.2 would apply, except that if the seller is located in a country other than France, and if insolvency proceedings against the seller are likely to be opened in that country, a specific analysis would be required to assess the enforceability of the sale in that context and in line with the law applicable to such insolvency proceeding.

3.4 Example 3: If (a) the seller is located in your jurisdiction but the obligor is located in another country, (b) the receivable is governed by the law of the obligor's country, (c) the seller sells the receivable to a purchaser located in a third country, (d) the seller and the purchaser choose the law of the obligor's country to govern the receivables purchase agreement, and (e) the sale complies with the requirements of the obligor's country, will a court in your jurisdiction recognise that sale as being effective against the seller and other third parties (such as creditors or insolvency administrators of the seller) without the need to comply with your jurisdiction's own sale requirements?

A French court will recognise such a sale as effective against the seller and the obligor to the extent that it is so effective under the law governing the receivable and the sale. In contrast, the enforceability against third parties is not dealt with by the Rome I Regulation; French international private law rules on this topic are not straightforward, and it is difficult to predict what the position of a French court would be in this specific situation.

3.5 Example 4: If (a) the obligor is located in your jurisdiction but the seller is located in another country, (b) the receivable is governed by the law of the seller's country, (c) the seller and the purchaser choose the law of the seller's country to govern the receivables purchase agreement, and (d) the sale complies with the requirements of the seller's country, will a court in your jurisdiction recognise that sale as being effective against the obligor and other third parties (such as creditors or insolvency administrators of the obligor) without the need to comply with your jurisdiction's own sale requirements?

The answer would be the same as for question 3.4. In addition, as is the case for question 3.3, if the seller is located in a country other than France, and if insolvency proceedings against the seller are likely to be opened in that country, a specific analysis would be required to assess the enforceability of the sale in that context and in line with the law applicable to such insolvency proceeding. Note that the same assumptions as referred to in question 3.2 will apply.

3.6 Example 5: If (a) the seller is located in your jurisdiction (irrespective of the obligor's location), (b) the receivable is governed by the law of your jurisdiction, (c) the seller sells the receivable to a purchaser located in a third country, (d) the seller and the purchaser choose the law of the purchaser's country to govern the receivables purchase agreement, and (e) the sale complies with the requirements of the purchaser's country, will a court in your jurisdiction recognise that sale as being effective against the seller and other third parties (such as creditors or insolvency administrators of the seller, any obligor located in your jurisdiction and any third party creditor or insolvency administrator of any such obligor)?

A French court will recognise such a sale as effective against the seller. Insofar as regards enforceability against the obligor, French

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law would apply and, therefore, should the requirements for the sale being enforceable against the obligor under the law of the purchaser's country and under French law differ, such a sale might not be enforceable against said obligor from a French law perspective and it may be advisable to proceed with the formalities required by French law (see question 4.1 (i)) to ensure such enforceability. Enforceability against third parties would not be straightforward to analyse, for the reason mentioned already in relation to question 3.4. Note that the same assumptions as those referred to in question 3.2 will apply.

4 Asset Sales

4.1 Sale Methods Generally. In your jurisdiction what are the customary methods for a seller to sell receivables to a purchaser? What is the customary terminology – is it called a sale, transfer, assignment or something else?

Firstly, several conditions must be complied with in respect of the receivables that are intended to be sold by a seller to a purchaser:

(a) the receivables must exist now or in the future;

(b) the receivables must belong to the seller; and

(c) the receivables must be identified and individualised or be capable of being identified and individualised.

Secondly, to a significant extent, the status of the purchaser determines the method of sale and the conditions for the sale of the receivables. In this respect, the sale of the receivables must take the form of:

(i) an assignment under the common regime of articles 1321 *et seq.* of the French Civil Code. The sale is valid between the seller and the purchaser and enforceable against third parties (other than the debtors) upon the date of execution of the sale agreement. It is enforceable against the debtors only when and if it has consented to the sale, it has been notified to it or it has acknowledged it. Assuming that the debtor is identified, there are no restrictions in respect of the type of receivables that can be assigned pursuant to the relevant provisions of the French Civil Code or in respect of the status of the purchaser;

(ii) an assignment by way of subrogation pursuant to articles 1346-1 *et seq.* of the French Civil Code. Under this method, a third party (the *subrogé*) pays the initial creditor (the *subrogeant*) and takes over the initial creditor's rights against the debtor. The subrogation must be express and, subject to limited exceptions, must occur at the time of the payment. As from the date of the subrogation, which shall coincide with the delivery of a formal receipt by the initial creditor to the third party (*quittance subrogative*), the transfer of the initial creditor's rights against the debtor to the third party shall be effective and enforceable against the debtor without any further formalities. Assuming that the debtor is identified, there are no restrictions in respect of the type of receivables that can be assigned by way of subrogation or in respect of the status of the purchaser. However, the initial creditor's rights against the debtor shall be transferred to the new creditor only up to the amount paid by it. In the context of a securitisation transaction, the constraints of the date of the subrogation and of the amount paid at the time of the subrogation may raise issues in connection with the sale of receivables with a discount purchase price or a deferred purchase price;

(iii) an assignment under the French Dailly Law pursuant to articles L. 313-23 to L. 313-34 of the French Monetary and Financial Code. The assignment of the receivables is performed by way of a single transfer document (*acte de cession*) exchanged between the seller and the purchaser. The assignment is effective between the parties and enforceable against third parties as from the date affixed by the purchaser on such transfer document without any further formalities. The provisions of the French Monetary and Financial Code have been amended in connection with the Dailly Law to secure the sale of future receivables and to develop the sale of receivables in the context of international financing transactions. Despite these recent evolutions, there are still some restrictions as to the type of receivables that can be sold under this method and as to the status of the purchaser. The receivables must arise from a "professional" relationship between the seller and the debtor, and the purchaser must be a credit institution duly licensed in France (or an EU-passported credit institution) or, since the recent *Ordonnance* n°2017-1432 of 4 October 2017, a French financing vehicle (see paragraph (iv) below).

(iv) an assignment under the French Securitisation Law pursuant to articles L. 214 – 166 – 1 to L. 214 – 190 of the French Monetary and Financial Code. The assignment of the receivables is performed by way of a single transfer document (*bordereau*) exchanged between the seller and the purchaser. The assignment is effective between the parties and enforceable against third parties (including the debtors) as from the date affixed on such transfer document without any further formalities. As for the method of assignment referred to in (iii) above, the provisions of the French Monetary and Financial Code allow the sale of future receivables and the sale of receivables in the context of international securitisation transactions. There are no restrictions as to the type of receivables that can be sold under this method. However, the purchaser must be a French *fonds commun de titrisation* or *FCT*, which is a co-ownership entity without legal personality jointly created by a management company and a custodian. There are many advantages in using this method, including the fact that all related security interests in connection with the purchased receivables are automatically transferred to the FCT without any further formalities, that upon the seller being subject to any insolvency proceeding, the assignment of the receivables will remain valid and enforceable, and that the FCT is the only French entity qualifying as a bankruptcy-remote vehicle for rating purposes. Alternatively, the purchaser may be set up under the form of a securitisation company (*société de titrisation* or *SDT*). In this case, the SDT is a commercial company benefitting from the same rules as for a FCT but being subject to a different tax treatment. From experience, an FCT or an SDT is the ideal tool for international securitisation transactions. The legal regime applicable to FCTs and SDTs has been significantly revised and improved recently thanks to *Ordonnance* n°2017-1432 of 4 October 2017. This *Ordonnance* also created new types of vehicles, namely the French *fonds de financement spécialisé* or *FFS* and the French *société de financement spécialisé* or *SFS*, which are close to FCTs and SDTs', respectively, and which together form a new legal category of investment vehicles called *organismes de financement* (financing vehicles). However, FFSs and SFSs are not strictly speaking "securitisation vehicles" to the extent that they are not allowed to issue different tranches of notes, bonds or shares representing different tranches of credit risk. Please see, however, more developments on these vehicles in questions 1.3, 4.8, 6.5, 6.7, 7.2 and 8.7; or

(v) in the case of mortgage loan receivables or receivables on public entities, it should be noted that another method of assignment is provided by articles L. 515-13 *et seq.* or in the case of mortgage loans receivables only, articles L. 515-34 *et seq.* of the French Monetary and Financial Code. Basically, the conditions and procedures of the assignment are the same as the assignment under the French Dailly Law or the French Securitisation Law. However, the Purchaser must be a mortgage company (*société de crédit foncier (SCF)* or a *société de financement de l'habitat (SFH)*), which

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are French financial institutions licensed by the French banking authorities with a limited purpose and structured as bankruptcy-remote entities.

The terminology varies; transfer, sale or assignment are terms that are frequently used. From a legal perspective, these are equal.

4.2 Perfection Generally. What formalities are required generally for perfecting a sale of receivables? Are there any additional or other formalities required for the sale of receivables to be perfected against any subsequent good faith purchasers for value of the same receivables from the seller?

Under the common regimes of the French Civil Code, the French Dailly Law or the French Securitisation Law, in order for the sale of receivables to be perfected against third parties, including any later purchaser, no additional formalities (other than those described in question 4.1) must be complied with.

4.3 Perfection for Promissory Notes, etc. What additional or different requirements for sale and perfection apply to sales of promissory notes, mortgage loans, consumer loans or marketable debt securities?

Generally speaking, the requirements for the sale and perfection of mortgage loans, consumer loans, promissory notes or debt securities are the following:

(i) promissory notes are transferred by way of endorsement for the benefit of a credit institution; the endorsement transfers the underlying debt to the new holder of such promissory notes;

(ii) marketable debt securities are transferred (A) if they are not registered in the books of Euroclear France or in that of any other clearing system, by way of a transfer order (*ordre de mouvement*), or (B) if they are registered in the books of Euroclear France or in that of any other clearing system, by way of a transfer from the relevant seller's account to the transferee's account in accordance with the rules applicable to Euroclear France or to any such other clearing system; and

(iii) mortgage loans and consumer loans are transferred in accordance with question 4.1 without the debtor's consent depending on the method of assignment, and the transfer of the mortgage securing the loans must be registered in the name of the purchaser (except under certain circumstances if the mortgage loans are materialised by specific instruments such as *copie exécutoire à ordre*).

However, if the sale of the instruments referred to in (iii) above is performed under the provisions of the French Dailly Law, the French SCF Law, the French SFH Law or the French Securitisation Law to a credit institution, a SCF, a SFH, a FCT or a SDT, then there are no formalities required in order to transfer the mortgage or other security interests securing the loans.

4.4 Obligor Notification or Consent. Must the seller or the purchaser notify obligors of the sale of receivables in order for the sale to be effective against the obligors and/or creditors of the seller? Must the seller or the purchaser obtain the obligors' consent to the sale of receivables in order for the sale to be an effective sale against the obligors? Whether or not notice is required to perfect a sale, are there any benefits to giving notice – such as cutting off obligor set-off rights and other obligor defences?

Whether or not the notification of the debtors is required for the sale to be enforceable against the debtors will depend on the method of the assignment. Under the common regime of the French Civil Code, the sale will be enforceable against the debtors upon their consent to the sale, being notified of it, or their acknowledgment of it. Under the French Dailly Law or the French Securitisation Law, the sale will be enforceable against the debtors as from the date of the sale without any requirement to notify them. In all situations, notification of the assignment to the debtor freezes the right of set-off (if any) of the debtor against the purchaser, save in respect of claims which are connected (*connexes*).

Even when the assignment of receivables is governed by the French Dailly Law or the French Securitisation Law, notifying the obligors will allow the assignee to instruct the obligors to pay the amounts due under the assigned receivables directly into its hands, especially in a situation where the seller is defaulting.

In relation to consent, please see the answers to questions 4.6 and 4.7.

4.5 Notice Mechanics. If notice is to be delivered to obligors, whether at the time of sale or later, are there any requirements regarding the form the notice must take or how it must be delivered? Is there any time limit beyond which notice is ineffective – for example, can a notice of sale be delivered after the sale, and can notice be delivered after insolvency proceedings have commenced against the obligor or the seller? Does the notice apply only to specific receivables or can it apply to any and all (including future) receivables? Are there any other limitations or considerations?

Apart from the French Dailly Law which provides for a specific notification form, the form of notice is not regulated. In all cases, it must be in writing and detailed enough to make it clear which receivables have been sold, especially in relation to future receivables. It is generally agreed that the notification of the debtor after the opening of insolvency proceedings against the seller is ineffective if the assignment took the form of the common regime of articles 1321 *et seq.* of the French Civil Code. When other legal means of assignment (see question 4.1) are used, notification of the debtors can validly be made after the bankruptcy of the seller.

4.6 Restrictions on Assignment – General Interpretation. Will a restriction in a receivables contract to the effect that "None of the [seller's] rights or obligations under this Agreement may be transferred or assigned without the consent of the [obligor]" be interpreted as prohibiting a transfer of receivables by the seller to the purchaser? Is the result the same if the restriction says "This Agreement may not be transferred or assigned by the [seller] without the consent of the [obligor]" (i.e., the restriction does not refer to rights or obligations)? Is the result the same if the restriction says "The obligations of the [seller] under this Agreement may not be transferred or assigned by the [seller] without the consent of the [obligor]" (i.e., the restriction does not refer to rights)?

The presence of a provision contract to the effect that "*[n]one of the [seller]'s rights or obligations under this Agreement may be transferred or assigned without the consent of the [obligor]*" in a receivables contract may restrict the assignment of the relevant receivables. The consent from the other party to the receivables contract will be necessary in order to assign the receivables deriving from the execution of the receivables contract.

However, if the provision of the receivables contract only prohibits the assignment of the agreement itself or the assignment of the

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obligations under the agreement, it might be considered that such prohibition is limited to the assignment of the agreement itself and not to the assignment of the receivable arising thereunder.

In any case, and beyond the wording, the parties' intention must be taken into consideration in the construction of the clause. In particular, key questions to be considered will concern the purpose of the clause: who is protected by this clause and what confidential information is at stake?

This is subject, in all cases, to the provision in our answer to question 4.7.

4.7 Restrictions on Assignment; Liability to Obligor. If any of the restrictions in question 4.6 are binding, or if the receivables contract explicitly prohibits an assignment of receivables or "seller's rights" under the receivables contract, are such restrictions generally enforceable in your jurisdiction? Are there exceptions to this rule (e.g., for contracts between commercial entities)? If your jurisdiction recognises restrictions on sale or assignment of receivables and the seller nevertheless sells receivables to the purchaser, will either the seller or the purchaser be liable to the obligor for breach of contract or tort, or on any other basis?

The French Commercial Code (article L.442-6-II-c) provides that any clause of the receivables contract prohibiting the assignment to any third party of the receivables arising from such contract is null and void if such receivables contract is entered into between commercial parties (meaning that this rule will not apply to a receivables contract entered into with consumers). However, the parties may still contractually limit the assignability of the receivables arising from the receivables contract, for instance, by stating that a party will only be allowed to assign the said receivables after having obtained the consent of the other party as to the identity of the assignee. Such provisions are valid but will not be enforceable against the purchaser if it cannot be proven that the latter was aware of the existence of such a restriction.

If (i) the receivables contract is entered into between the seller and a non-commercial party (i.e. customer) or if the receivables contract contains provisions limiting the assignability of the receivables, for instance by stating that a party will only be allowed to assign the said receivables after having obtained the consent of the other party as to the identity of the assignee, and (ii) the purchaser is aware, as at the date it purchased the receivables, of the existing restrictions as to the assignment of the receivables, it might, pursuant to the provisions of the French Civil Code and according to certain French court decisions, be liable for any damage caused to the debtors for having knowingly contributed to the violation of the provisions agreed to between the seller and debtors.

Moreover, in such a case, the fact of having assigned the receivables without the prior consent of the debtors would constitute a breach of contract by the seller. Such a contractual breach could give rise to a claim for damages of the debtors against the seller pursuant to the provisions of the French Civil Code. The debtors having a claim against the seller, together with any consequent set-off right, may cause the debtors to be or become non-eligible for the assignment.

4.8 Identification. Must the sale document specifically identify each of the receivables to be sold? If so, what specific information is required (e.g., obligor name, invoice number, invoice date, payment date, etc.)? Do the receivables being sold have to share objective characteristics? Alternatively, if the seller sells *all* of its receivables to the purchaser, is this sufficient identification of receivables? Finally, if the seller sells *all* of its receivables *other than* receivables owing by one or more specifically identified obligors, is this sufficient identification of receivables?

Assuming that the sale of the receivables is performed in accordance with the provisions of the French Dailly Law, the French SCF Law, the French SFH Law or the French Securitisation Law to a credit institution, a SCF, a SFH, a FCT, a SDT, a FFS or a SFS, the sale document (*acte de cession*) must contain the following mandatory information:

(a) references to the relevant provisions of the law that governs the sale document;

(b) identification of the purchaser; and

(c) identification of each receivable subject to the sale document; each receivable must be sufficiently identified and individualised in precise detail, for instance the designation of the debtor, and the amount or the maturity of the receivable (this list being given as an example by the law). When the sale is made by a computerised process (*procédé informatique*) that allows the identification of receivables, then the sale document shall only mention the means by which the receivables are transferred, identified and individualised and an estimate of their number and total amount.

4.9 Recharacterisation Risk. If the parties describe their transaction in the relevant documents as an outright sale and explicitly state their intention that it be treated as an outright sale, will this description and statement of intent automatically be respected or is there a risk that the transaction could be characterised by a court as a loan with (or without) security? If recharacterisation risk exists, what characteristics of the transaction might prevent the transfer from being treated as an outright sale? Among other things, to what extent may the seller retain any of the following without jeopardising treatment as an outright sale: (a) credit risk; (b) interest rate risk; (c) control of collections of receivables; (d) a right of repurchase/redemption; (e) a right to the residual profits within the purchaser; or (f) any other term?

Under French law, the courts are not bound by the qualification given by the parties. Pursuant to article 12 of the French Civil Procedure Code, it is up to the judge to give or restore the qualification of an agreement, without taking into account the qualification given by the parties. In doing so, the judge will analyse the agreement and its core elements, and its "*économie*", i.e. the reciprocal obligations of the parties.

In relation to perfection, the sale of receivables is perfected under the various methods of assignment described in question 4.1, subject to the completion of the relevant formalities. Upon such formalities

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(e.g. execution of the transfer document under the French Dailly law, the French SCF, the French SFH or the French Securitisation Law), the receivables cease to belong to the seller and are legally transferred to the purchaser. The fact that the seller retains certain risks (credit, interest rate, dilutions, etc.) and may, to a certain extent, (i) control the collections received in its capacity as servicer on behalf of the purchaser, and (ii) have a right to repurchase some of the receivables, has no impact on the perfection of the sale.

4.10 Continuous Sales of Receivables. Can the seller agree in an enforceable manner to continuous sales of receivables (i.e., sales of receivables as and when they arise)? Would such an agreement survive and continue to transfer receivables to the purchaser following the seller's insolvency?

French securitisation transactions are generally structured to provide a commitment from the seller to assign over a certain period of time (revolving period) all or part of the receivables it owns. Such commitment is enforceable against the seller until its insolvency. Upon insolvency of the seller, the insolvency official will have the option either to continue or terminate such commitment depending on the circumstances. The option of the insolvency official is, however, subject to a formal procedure set out by the French Commercial Code.

4.11 Future Receivables. Can the seller commit in an enforceable manner to sell receivables to the purchaser that come into existence after the date of the receivables purchase agreement (e.g., "future flow" securitisation)? If so, how must the sale of future receivables be structured to be valid and enforceable? Is there a distinction between future receivables that arise prior to *versus* after the seller's insolvency?

The French Securitisation Law specifically provides that the sale of the receivables that come into existence after the date of the sale contract is not affected by the commencement of insolvency proceedings against the seller. According to the French Securitisation Law, the sale is perfected on the date of execution of the transfer document irrespective of the date on which the receivables come into existence (*date de naissance*), the date on which they become due (*date d'échéance*) or the date on which they become due and payable (*date d'exigibilité*), including upon an insolvency proceeding of the seller.

The French Securitisation Law has been amended a number of times over the years, in particular to ease the assignment of future receivables and to ensure enforceability, even in relation to future receivables which are sold before, but come into existence after, bankruptcy of the seller. Thus, the law includes crystal-clear provisions to that effect and no specific legal structuring is necessary.

4.12 Related Security. Must any additional formalities be fulfilled in order for the related security to be transferred concurrently with the sale of receivables? If not all related security can be enforceably transferred, what methods are customarily adopted to provide the purchaser the benefits of such related security?

Assuming that the sale of receivables is performed under the French Dailly law, the French Securitisation Law, the French SCF Law or the French SFH Law, all related security and ancillary rights will be automatically, and without formality (*de plein droit*), transferred to the purchaser, including in respect of mortgages or other registered security interest. Such transfer will be enforceable as from the date of the sale of the receivables.

4.13 Set-Off; Liability to Obligor. Assuming that a receivables contract does not contain a provision whereby the obligor waives its right to set-off against amounts it owes to the seller, do the obligor's set-off rights terminate upon its receipt of notice of a sale? At any other time? If a receivables contract does not waive set-off but the obligor's set-off rights are terminated due to notice or some other action, will either the seller or the purchaser be liable to the obligor for damages caused by such termination?

In case of an assignment of receivables governed by articles 1321 *et seq.* of the French Civil Code (as described in question 4.1), the obligor will, as a matter of principle, be entitled to use its set-off rights if the legal conditions of set-off between the obligor and the seller were complied with before the notice of sale made to the obligor or if the relevant claims are connected claims (*créances connexes*).

A similar solution will prevail in the context of a Dailly Law assignment or a Securitisation Law assignment (as described in question 4.1). Indeed, after the obligor has received a notice of assignment (*notification*), the set-off rights may no longer be opposed to the purchaser by such obligor, except in relation to connected claims (*créances connexes*). In any case, if such obligor has accepted the assignment through a formal acceptance (*acceptation*) (pursuant to article L. 313-29 of the French Monetary and Financial Code), he will not be entitled to oppose to the purchaser any defence (including set-off) deriving from its personal relationship with the seller.

4.14 Profit Extraction. What methods are typically used in your jurisdiction to extract residual profits from the purchaser?

Various methods are available, including a differed purchase price mechanism or a special servicing fee (to the extent the seller and the servicer are the same entities). However, when a FCT or a SDT are used, the typical profits extraction mechanism takes the form of the issuance of residual notes or units subscribed by the seller for a nominal amount and giving right to the excess cash available.

5 Security Issues

5.1 Back-up Security. Is it customary in your jurisdiction to take a "back-up" security interest over the seller's ownership interest in the receivables and the related security, in the event that an outright sale is deemed by a court (for whatever reason) not to have occurred and have been perfected (see question 4.9 above)?

It is not customary in France to take a "back-up" security interest over the seller's ownership interest in the receivables and the related security. To our knowledge, subject to "covered bond"-type structures, no securitisation transaction implemented in France has used such mechanism to secure the risk that a sale of receivables is deemed by a court not to have been perfected.

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5.2 Seller Security. If it is customary to take back-up security, what are the formalities for the seller granting a security interest in receivables and related security under the laws of your jurisdiction, and for such security interest to be perfected?

Please see the answer to question 5.1.

5.3 Purchaser Security. If the purchaser grants security over all of its assets (including purchased receivables) in favour of the providers of its funding, what formalities must the purchaser comply with in your jurisdiction to grant and perfect a security interest in purchased receivables governed by the laws of your jurisdiction and the related security?

The French Civil Code provides for a simple procedure to pledge receivables. Such pledge must take the form of a written agreement which identifies the pledged receivables (or which includes the means of identification of the receivables in case of future receivables). Such pledge is valid between the pledgor and the pledgee and enforceable against third parties upon signing. It is enforceable against the debtors only upon notification.

The so-called "financial guarantee regime", resulting from the European Directive on financial collateral, provides for an even more simplified regime which resists bankruptcy of the pledgor but which is only available to financial institutions (which include, for the purpose of this specific regime, French securitisation vehicles).

5.4 Recognition. If the purchaser grants a security interest in receivables governed by the laws of your jurisdiction, and that security interest is valid and perfected under the laws of the purchaser's jurisdiction, will the security be treated as valid and perfected in your jurisdiction or must additional steps be taken in your jurisdiction?

It is generally agreed that a pledge over French assets should be governed by French law. Accordingly, the situation described in this question is to be avoided.

5.5 Additional Formalities. What additional or different requirements apply to security interests in or connected to insurance policies, promissory notes, mortgage loans, consumer loans or marketable debt securities?

Under French law, depending on the type of assets and the legal status of the pledgor and the pledgee, additional or specific formalities might be required on a case-by-case basis.

5.6 Trusts. Does your jurisdiction recognise trusts? If not, is there a mechanism whereby collections received by the seller in respect of sold receivables can be held or be deemed to be held separate and apart from the seller's own assets (so that they are not part of the seller's insolvency estate) until turned over to the purchaser?

France has not yet ratified the 1985 International Convention relating to the law applicable to trusts and their recognition. Accordingly, trusts are generally not recognised under French law, bearing in mind that the situation evolves slowly; in particular, trusts have been expressly mentioned in recent tax laws, and a court decision known as the "Belvédère" case recently recognised the capacity of a trust to represent creditors in the context of a parallel debt. In addition, a similar concept has been introduced into the French Civil Code. The *fiducie* is an agreement which allows a party (*constituant*) to isolate assets into a special-purpose fund (the *fiducie*) which is managed by a fiduciary (*fiduciaire*) to the benefit of the *constituant* or a third-party beneficiary. This mechanism is generally not used in connection with securitisation transactions although it has already been used in the context of securitisation of equipment lease receivables. A *fiducie* is either set up for assets management purposes or as a security.

The French Securitisation Law has introduced a mechanism to secure the collections received by the seller in connection with the sold receivables. Pursuant to articles L. 214-173 and D. 214-228 of the French Monetary and Financial Code, specially dedicated bank accounts are set up in the books of the collection account banks of the seller to receive the collections in respect of the sold receivables and whereby the seller agrees to specially dedicate the collection accounts to the FCT or the SDT. Consequently, the management company will have the right, subject to the terms of the agreement, to use the amounts credited into such account, as from the date of such agreement. Creditors of the seller will not be able to claim any of the sums collected into this account, under any circumstances including the opening of insolvency proceedings against the seller.

5.7 Bank Accounts. Does your jurisdiction recognise escrow accounts? Can security be taken over a bank account located in your jurisdiction? If so, what is the typical method? Would courts in your jurisdiction recognise a foreign law grant of security (for example, an English law debenture) taken over a bank account located in your jurisdiction?

Under French law, a security interest may be taken over a bank account. Pursuant to articles 2355 *et seq.* of the French Civil Code, the seller may grant a security interest on the balance of a bank account (*nantissement de compte bancaire*) in accordance with the principles applicable to pledges over receivables (*nantissement de créances*).

The French Monetary and Financial Code also provides for specific forms of pledge over bank accounts known as *garanties financières* which provide, in certain circumstances, a better protection in case of bankruptcy of the debtor.

The most natural law applicable to charges (*sûretés réelles*) under French law is, as a matter of principle, and although this may be subject to academic debates, the law of location (*lex rei sitae*) of the asset (either movable or immovable). Similarly, financial guarantees under Directive 2002/47/CE are governed by the law of the Member State in which the financial instruments account is located. Therefore, in case a French bank account is subject to a security interest, the law determining the effects of such pledge shall be French law, according to the *lex rei sitae* and by analogy to the provisions on financial guarantees. French courts are generally reluctant to recognise foreign security interests over assets located in France. They set up a series of requirements based on the principle that charges (*sûretés réelles*) are enumerated to a limited extent under French law (*numerus clausus*). Hence, the foreign security interest shall correspond to a type of security interest recognised in France and its validity and enforceability requirements shall be similar to those requested under French law.

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5.8 Enforcement over Bank Accounts. If security over a bank account is possible and the secured party enforces that security, does the secured party control all cash flowing into the bank account from enforcement forward until the secured party is repaid in full, or are there limitations? If there are limitations, what are they?

In case of a security over a bank account governed by articles 2355 *et seq.* of the French Civil Code, the scope of the pledge is the credit balance of the bank account on the date the security is enforced. As from the enforcement of the security over the bank account, such account will be blocked and the secured party will be able to control the cash flowing into the relevant account until the release of the pledge over the bank account i.e. until full repayment.

In the context of *garanties financières*, the beneficiary will be entitled, subject to the terms of the agreement and the way the *garantie financière* is structured, to control all cash flowing to the relevant account as from enforcement and until the secured obligations are repaid in full.

In addition, and although this is not considered as a security as such under French law, it must be remembered that, as seen in the answer to question 5.6, the French Securitisation Law provides for specially dedicated bank accounts that are set up in the books of the collection bank and that will allow the management company to control the cash flowing into the collection account, subject to the terms of the agreement.

5.9 Use of Cash Bank Accounts. If security over a bank account is possible, can the owner of the account have access to the funds in the account prior to enforcement without affecting the security?

In the case of the French Civil Code regime (as described above), the owner of the bank account may have access to the funds standing to the credit of the bank account subject to the pledge, without affecting the security.

In the context of *garanties financières*, the right of the guarantor to use the money will depend on the type of financial guarantee chosen by the parties. The preferred route, i.e. remittance of cash by the guarantor to the credit of a bank account owned by the beneficiary, does not allow the guarantor to use the collateralised amount of cash, since the guarantor is not the owner of the bank account on which the sums are standing.

6 Insolvency Laws

6.1 Stay of Action. If, after a sale of receivables that is otherwise perfected, the seller becomes subject to an insolvency proceeding, will your jurisdiction's insolvency laws automatically prohibit the purchaser from collecting, transferring or otherwise exercising ownership rights over the purchased receivables (a "stay of action")? If so, what generally is the length of that stay of action? Does the insolvency official have the ability to stay collection and enforcement actions until he determines that the sale is perfected? Would the answer be different if the purchaser is deemed to only be a secured party rather than the owner of the receivables?

The commencement of French insolvency proceedings (i.e. safeguard, reorganisation or liquidation proceedings) against the seller after the sale of receivables should not prohibit the purchaser from collecting, transferring or otherwise exercising ownership rights over the receivables, provided that the sale is performed under the French Dailly Law, the French SCF Law, the French SFH Law or the French Securitisation Law to a credit institution, a SCF, a SFH, a FCT, or a SDT. From an insolvency law point of view, the sale is valid and enforceable against third parties (including an insolvency official) as from the date of the sale document, and qualifies as a true sale by virtue of law.

In respect of the sale of future receivables (i.e. receivables that arise after the seller becomes subject to an insolvency proceeding), the sale of such receivables by way of a Dailly, SCF, SFH, FCT or SDT sale document (*acte de cession*) should not be affected by the commencement of French insolvency proceedings against the seller as such principle is clearly stated in the law.

6.2 Insolvency Official's Powers. If there is no stay of action, under what circumstances, if any, does the insolvency official have the power to prohibit the purchaser's exercise of its ownership rights over the receivables (by means of injunction, stay order or other action)?

The insolvency official could not prohibit the exercise of rights by the purchaser of the receivables by means of injunction, stay order or other action (however, see question 6.1).

6.3 Suspect Period (Clawback). Under what facts or circumstances could the insolvency official rescind or reverse transactions that took place during a "suspect" or "preference" period before the commencement of the seller's insolvency proceedings? What are the lengths of the "suspect" or "preference" periods in your jurisdiction for (a) transactions between unrelated parties, and (b) transactions between related parties? If the purchaser is majority-owned or controlled by the seller or an affiliate of the seller, does that render sales by the seller to the purchaser "related party transactions" for purposes of determining the length of the suspect period? If a parent company of the seller guarantee's the performance by the seller of its obligations under contracts with the purchaser, does that render sales by the seller to the purchaser "related party transactions" for purposes of determining the length of the suspect period?

In the context of reorganisation or liquidation proceedings (but not safeguard proceedings), as a general principle, a sale of receivables may be challenged by the receiver during a so-called "suspect" period (*période suspecte*) of up to 18 months prior to the opening of insolvency proceedings if the insolvency official can establish that the sale was made for inadequate value, or if the purchaser was aware of the seller's insolvency at the time of the purchase. The same principles apply, whether the parties concerned are related or unrelated. However, this "suspect period" does not apply to assignments of receivables made to the benefit of a SCF, a SFH, a FCT, a SDT, a FFS or a SFS.

6.4 Substantive Consolidation. Under what facts or circumstances, if any, could the insolvency official consolidate the assets and liabilities of the purchaser with those of the seller or its affiliates in the insolvency proceeding? If the purchaser is owned by the seller or by an affiliate of the seller, does that affect the consolidation analysis?

Generally, the insolvency official of the seller cannot request the

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court to order consolidation of the assets and liabilities of the purchaser with those of the seller or its affiliates unless the court finds that there is abnormal commingling of assets between the purchaser and the seller (*confusion de patrimoines*) or the purchaser is considered to be a sham or a mere fiction (*fictivité*). In these circumstances, the insolvency proceedings would be extended to the purchaser and would affect its assets, in that the assets of the seller and that of the purchaser would be consolidated. This analysis applies irrespective of the fact that the purchaser and the seller may be part of the same group of companies.

6.5 Effect of Insolvency on Receivables Sales. If insolvency proceedings are commenced against the seller in your jurisdiction, what effect do those proceedings have on (a) sales of receivables that would otherwise occur after the commencement of such proceedings, or (b) on sales of receivables that only come into existence after the commencement of such proceedings?

Please see question 6.1.

6.6 Effect of Limited Recourse Provisions. If a debtor's contract contains a limited recourse provision (see question 7.3 below), can the debtor nevertheless be declared insolvent on the grounds that it cannot pay its debts as they become due?

Whether or not the debtor may be considered insolvent in such a situation depends on the definition and interpretation of the concept of *cessation des paiements* (cessation of payments) used by French courts to decide if insolvency proceedings must be opened against a debtor.

The concept of *cessation des paiements* is defined by article L. 631-1 of the French Commercial Code as the impossibility of the debtor to pay its liabilities when due, (*passif exigible*) out of its available assets (*actif disponible*). French law has limited the scope of the concept of *passif exigible*, which is clearly limited to *passif échu* (liabilities which have reached their maturity date or receivables which are accelerated). However, where the debtor can establish that the creditor has granted a moratorium on payment of the relevant debts and that consequently the debtor is able to pay its debts, such debtor will not be considered as insolvent.

In addition, it must be mentioned that non-petition clauses are not given effect under French law (see question 7.5).

7 Special Rules

7.1 Securitisation Law. Is there a special securitisation law (and/or special provisions in other laws) in your jurisdiction establishing a legal framework for securitisation transactions? If so, what are the basics? Is there a regulatory authority responsible for regulating securitisation transactions in your jurisdiction?

The French Securitisation Law dated 23 December 1988, as lastly amended by *Ordonnance* n°2017-1432 of 4 October 2017, codified in articles L. 214-166-1 to L. 214-190-3 of the French Monetary and Financial Code, implemented a legal framework for securitisation transactions in France. Please see question 7.2 for the basics.

Securitisation transactions are not regulated as such. However, depending on the sale method (see question 4.1), the purchaser, its management company and/or its custodian might be regulated by the *Autorité des marchés financiers* (AMF) or the *Autorité de contrôle prudentiel et de résolution* (ACPR). In addition, a securitisation transaction that results in the issuance of transferable securities, such as bonds, notes or shares, to be offered to the public in France or to be admitted for trading on the French stock exchange markets, requires a prospectus to be cleared in advance by the AMF.

7.2 Securitisation Entities. Does your jurisdiction have laws specifically providing for establishment of special purpose entities for securitisation? If so, what does the law provide as to: (a) requirements for establishment and management of such an entity; (b) legal attributes and benefits of the entity; and (c) any specific requirements as to the status of directors or shareholders?

The French Securitisation Law created the *fonds communs de titrisation* (literally, a "common pool of securitisation", although a better translation would be "mutual debt fund"). The FCT is a co-ownership vehicle whose purpose is the acquisition of receivables and debt instruments. Since *Ordonnance* n°2017-1432 of 4 October 2017, it can also lend, enter into sub-participation agreements and issue financial guarantees. The FCT does not have separate legal personality. It may consist of several ring-fenced "compartments".

The FCT must be constituted jointly by a management company and a custodian. The management company is a portfolio management company (*société de gestion de portefeuille*) governed by articles L. 532-9 of the French Monetary and Financial Code.

The custodian is a credit institution incorporated in the European Economic Area or any institution approved by the French government. The management company and the custodian play an important role in the creation and the life of the FCT, the former as manager of its business and the latter as custodian of the FCT's assets and as supervisor of the management company.

The French legal provisions on securitisation provide that the FCT is entitled to acquire all types of debts, including existing or future receivables, non-performing receivables or any type of debt instrument governed by French law or any foreign law. The law also provides for the possibility of multiple issues by the FCT of units or any type of debt instruments, including bonds, governed by French law or by any foreign law. Finally, the FCT is entitled to enter into synthetic transactions either as a protection buyer or protection provider, and to enter into credit transactions (loans, leases, sub-participations, etc.) and is the only French entity qualifying as a bankruptcy-remote vehicle for rating purposes. From past experience, it seems that the use of a FCT is the ideal tool for international securitisation transactions (see question 4.1).

FCTs may also be used in order to securitise insurance risks.

French law introduced the possibility for a FCT to qualify as a *fonds de prêts à l'économie* (*FPE*), pursuant to article R.332-14-2 of the French Insurance Code. The FPE is designed to mainly target French insurance companies, French security bodies and French mutual insurance companies as investors, since they are benefitting from a favourable regulatory treatment when subscribing for the securities issued by a FPE.

The FCT should be outside the scope of French corporate income tax.

Securitisation vehicles can also be set up under the form of a SDT. In this case, the SDT is a commercial company benefitting from the same rules as for a FCT but it is subject to tax under ordinary rules.

As stated above, since *Ordonnance* n°2017-1432 of 4 October 2017, a FCT can also enter into credit transactions and in particular

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loans, sub-participations and lease activities. A SDT benefits from the same new regime which allows direct lending activities and involves a major exemption from the longstanding so-called "French banking monopoly", which constitutes a cornerstone of the French banking system and prevents entities other than duly licensed credit institutions from lending in France.

This *Ordonnance* also created new types of vehicles, namely the FFS and the SFS, as referred to at point (iv) of question 4.1. A FFS and a SFS are close to a FCT and SDT, respectively. In particular, they can enter into direct lending activities although, strictly speaking, they are not "securitisation vehicles" to the extent that they are not allowed to issue different tranches of notes, bonds or shares representing different tranches of credit risk (see point (iv) of question 4.1). This being said, the scope of authorised investments of a FFS or a SFF is slightly wider and includes, in particular, shares or equity instruments in general.

7.3 Location and form of Securitisation Entities. Is it typical to establish the special purpose entity in your jurisdiction or offshore? If in your jurisdiction, what are the advantages to locating the special purpose entity in your jurisdiction? If offshore, where are special purpose entities typically located for securitisations in your jurisdiction? What are the forms that the special purpose entity would normally take in your jurisdiction and how would such entity usually be owned?

Special purpose entities set-up for a securitisation transaction in France are normally established in France as such special purpose entities are governed by the French Securitisation Law which, by essence, governs only French special purpose entities. Any offshore special purpose entity set-up for a securitisation transaction which would not benefit from a European banking passport authorising it to carry out banking activities in France would, subject to limited and specific exemptions, act in breach of the so-called "French banking monopoly" because purchasing non-matured receivables on a regular basis for a consideration is a regulated credit activity in France. In any case, such an offshore special purpose entity would not be able to take advantage of certain legal features provided for by the French Securitisation Law – and benefitting French special purpose entities only.

Typically, the French special purpose entity used for securitisation transactions in France is the FCT (see question 7.2). A FCT has to issue at least two *parts* (ownership interest) of a minimal nominal value of EUR 150 each and the FCT would typically issue bonds to finance the purchase price of its assets. FCTs do not have share capital and they are therefore not "owned" by anyone. SDTs have a proper share capital but are very rarely used in securitisation transactions.

7.4 Limited-Recourse Clause. Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) limiting the recourse of parties to that agreement to the available assets of the relevant debtor, and providing that to the extent of any shortfall the debt of the relevant debtor is extinguished?

The question as to whether contractual limitations on the *droit de gage général* (commonly referred as to "limited recourse clause") are valid has given rise to differing doctrinal views and is *the* subject of very little jurisprudence. However, it is now generally admitted that a court will give effect to a limited recourse clause provided that (i) the limited recourse clause has been freely and knowingly agreed to by the creditor for the benefit of its debtors (and has not been imposed on the creditor by the debtors), and (ii) is the fair consideration for the obligations set out in the agreement such as those pursuant to which the debtors agree to do or not to do certain specific things, or to allocate to the creditor certain cash flows in accordance with a specific priority of payment.

It is common practice to include in agreements relating to a securitisation transaction a provision whereby the parties acknowledge and agree that the assets of the FCT are limited to the receivables it acquires and the cash collected on its accounts. Moreover, it is also common practice to provide that, past a certain date after the maturity date of the last receivable acquired by the FCT, the parties to the transaction agreement waive their rights to any residual amount the FCT might owe them (*abandon de créances*).

7.5 Non-Petition Clause. Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) prohibiting the parties from: (a) taking legal action against the purchaser or another person; or (b) commencing an insolvency proceeding against the purchaser or another person?

The validity of a non-petition provision has been highly discussed under French law as such provision is part of other standard provisions contained in the legal documentation of securitisation transactions. However, it is generally admitted under French law that a court will not give effect to such provision.

7.6 Priority of Payments "Waterfall". Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) distributing payments to parties in a certain order specified in the contract?

The French Securitisation Law states that the constitutional documents of the securitisation vehicle may provide for a subordination of the rights of certain creditors to the rights of other creditors. The allocation rules of the cash received by the securitisation vehicle are binding upon the unitholders, the shareholders (as the case may be), the holders of debt instruments issued by the securitisation vehicle and any creditors that have agreed to such allocation rules and subordination rights – even when those entities are subject to bankruptcy proceedings. The French judge will therefore have to give effect to these contractual provisions, deriving from the French Securitisation Law. In the case of foreign law-governed documentation, the judge will give effect to foreign law-governed provisions, subject to the French public policy rules (see the answer to question 2.3).

7.7 Independent Director. Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) or a provision in a party's organisational documents prohibiting the directors from taking specified actions (including commencing an insolvency proceeding) without the affirmative vote of an independent director?

Under French law, organisational documents and/or any other contract may prohibit directors to take certain specified actions without the vote or consultation of another director appointed as independent director. However, depending on the legal form of the

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company (e.g. *société par actions simplifiée*) and the title of the person acting on behalf of the company, such provisions may not be enforceable against third parties.

7.8 Location of Purchaser. Is it typical to establish the purchaser in your jurisdiction or offshore? If in your jurisdiction, what are the advantages to locating the purchaser in your jurisdiction? If offshore, where are purchasers typically located for securitisations in your jurisdiction?

Please see question 7.3.

8 Regulatory Issues

8.1 Required Authorisations, etc. Assuming that the purchaser does no other business in your jurisdiction, will its purchase and ownership or its collection and enforcement of receivables result in its being required to qualify to do business or to obtain any licence or its being subject to regulation as a financial institution in your jurisdiction? Does the answer to the preceding question change if the purchaser does business with more than one seller in your jurisdiction?

Any purchaser other than a FCT, SDT, FFS or SFS must be licensed in France as a credit institution in order to purchase non-matured receivables on a regular basis for consideration.

The fact that the purchaser does business in France with other sellers has no impact on the above requirement which relates to the nature of the contemplated operation (i.e. the purchase of non-matured receivables).

Note, however, that alongside the regulatory changes that allow the FCTs, SDTs, FFSs and SFSs to make direct lending activities in France (see question 7.2), a limited number of French entities established under the form of funds and non-bank foreign entities can now benefit from the same relaxation of the French banking monopoly.

8.2 Servicing. Does the seller require any licences, etc., in order to continue to enforce and collect receivables following their sale to the purchaser, including to appear before a court? Does a third-party replacement servicer require any licences, etc., in order to enforce and collect sold receivables?

Servicing and collection activities for the benefit of third parties are also regulated activities in France. In practice, when the seller acts as servicer or collection agent of its own receivables for the account of the purchaser and no action is brought before the courts, it is not required to comply strictly with French regulations applying to servicing activities. It should be noted that under the French Securitisation Law, such regulatory constraints do not apply but that the transfer of servicing from the seller to any third party must be notified to the debtors.

8.3 Data Protection. Does your jurisdiction have laws restricting the use or dissemination of data about or provided by obligors? If so, do these laws apply only to consumer obligors or also to enterprises?

French law regulates the transfer of personal data. The aim of such regulation is to protect the rights of individuals, including consumer debtors. However, it does not apply to debtors that are incorporated as enterprises.

The applicable regulation is known as the "*Loi Informatique et Liberté*" dated 6 January 1978 (as amended). Under such regulation, the transferor of personal data must, except under certain circumstances, inform each individual of any data transfer that directly identifies such individual or could allow his identification. The application of such regulation is placed under the control of the *Commission Nationale Informatique et Liberté* (*CNIL*).

In practice, there have been a number of solutions implemented in order to accommodate the application of the relevant regulation within the context of securitisation transactions, such as transferring only partial information or codified information.

Note, however, that the Regulation (EU) 2016/679 of the European Parliament and of the Council of 27 April 2016 on the protection of natural persons with regard to the processing of personal data and on the free movement of such data, will be applicable in France as from 25 May 2018 and that this will lead to current practices being reconsidered.

8.4 Consumer Protection. If the obligors are consumers, will the purchaser (including a bank acting as purchaser) be required to comply with any consumer protection law of your jurisdiction? Briefly, what is required?

The purchaser will not be required to comply with any additional consumer protection law except as stated in question 1.2. Consumer protection law, such as enforcement rules against consumer debtors, will continue to apply to the extent that the seller acts as servicer.

8.5 Currency Restrictions. Does your jurisdiction have laws restricting the exchange of your jurisdiction's currency for other currencies or the making of payments in your jurisdiction's currency to persons outside the country?

Under French law, it is a general principle that international payments are free of any administrative or governmental control. However, recent anti-money laundering rules impose an obligation on credit institutions to declare any suspect payments or transactions.

8.6 Risk Retention. Does your jurisdiction have laws or regulations relating to "risk retention"? How are securitisation transactions in your jurisdiction usually structured to satisfy those risk retention requirements?

EU risk retention rules set out in article 405 paragraph (1) sub-paragraph (c) of the Capital Requirements Regulation, article 51 paragraph (1) sub-paragraph (c) of the AIFM Regulation and article 254 paragraph (2) sub-paragraph (c) of the Solvency II Regulation apply to securitisation transactions in France. Pursuant to those risk retention rules, investors must ensure that the originator, sponsor or original lender undertakes to retain, on an ongoing basis during the entire life of the securitisation transaction, a material net economic interest in the securitisation of not less than 5 per cent of the nominal value of the securitised exposures (i.e. the purchased receivables).

Typically, to that purpose, receivables which would have otherwise been securitised are randomly selected and retained by the seller, or the seller subscribes for first loss tranche in the securitisation, and the seller undertakes not to enter into transactions aiming at hedging or mitigating its risk under such retained exposure.

In addition, it should be noted that the so-called STS Regulation was adopted on 26 October 2017. The STS Regulation aims in

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particular at harmonising the above mentioned retention obligations and creating direct retention obligations. Based on grandfathering provisions, most of the provisions introduced by the STS Regulation should only be applicable to securitisations the securities of which are issued on or after 1 January 2019.

8.7 Regulatory Developments. Have there been any regulatory developments in your jurisdiction which are likely to have a material impact on securitisation transactions in your jurisdiction?

Ordonnance n°2017-1432 of 4 October 2017 has significantly improved the French Securitisation Law in two ways: it constitutes a new major exemption from the so-called "French banking monopoly"; and it gives the French FCTs, SDTs, FFSs and SFSs a number of competitive advantages. Certain aspects of this reform are addressed above (see questions 1.3, 4.1(iv), 4.8, 6.3 and 7.2). Other practical changes are set out below.

With this reform, the new FCTs, SDTs, FFSs and SFSs share a common regime based on the prior features of the French securitisation vehicles regime including comprehensive bankruptcy remoteness provisions and the possibility to opt for a tax transparent fund structure or a corporate structure subject to corporate tax. All types of vehicles further benefit from an unrivalled creditor-friendly legal regime, such as extended protections against the insolvency of the vehicle's counterparties, lock-box mechanism and protection of future flows. They are also allowed, depending on their form and specificities, to:

- directly grant and make available loans to corporate borrowers in France and abroad, without the intermediation of a credit institution and without being subject to regulatory capital requirements;
- enter into lease transactions;
- enter into sub-participations;
- own a number of different types of assets, including shares and equity-like instruments;
- benefit from all kind of guarantees and security interest, including the so-called "Dailly" assignment (being the most commonly used and bankruptcy-proof security interest in the French lending market and which, up until now, could only be granted to the benefit of credit institutions);
- benefit from the "European Long Term Investment Fund" EU label; and
- be managed by a company incorporated outside of France, if licensed in a EU Member State to manage alternative investment funds.

This reform opens a large range of new possibilities for a variety of French and foreign actors, such as insurers, asset managers, investment funds, private equity funds, debt funds, special situations funds or direct lending platforms, in fields as diverse as:

- corporate financing (via direct lending to corporate, including SMEs);
- lease financing;
- real estate financing;
- infrastructure financing (with the new funds taking direct part in the origination, structuration and lending process alongside other financers);
- distressed assets management and restructuring (noting that the new funds will be allowed to grant new money and to hold equity in the restructured entity);
- regulatory capital transactions (as the new funds will be allowed to enter into a variety of risk transfer instruments, no longer limited to credit default swaps, as was the case until now);
- tech and fintech financings (by way of direct lending and market refinancing); and
- classic securitisations for all types of assets, including leasing receivables, non-performing loans, whole business, project bonds or sovereign exposures.

As a separate important point, this reform also includes some long-awaited provisions aiming at enlarging the legal tools available to French banks for refinancing their loan exposures. Refinancing techniques were limited until now by the French banking monopoly, as the purchasing of outstanding loans is, subject to limited exceptions, viewed as a regulated banking activity in France. The reform will extend considerably these exceptions and in particular will allow certain types of non-bank foreign entities to freely acquire such loans on the secondary market.

9 Taxation

9.1 Withholding Taxes. Will any part of payments on receivables by the obligors to the seller or the purchaser be subject to withholding taxes in your jurisdiction? Does the answer depend on the nature of the receivables, whether they bear interest, their term to maturity, or where the seller or the purchaser is located? In the case of a sale of trade receivables at a discount, is there a risk that the discount will be recharacterised in whole or in part as interest? In the case of a sale of trade receivables where a portion of the purchase price is payable upon collection of the receivable, is there a risk that the deferred purchase price will be recharacterised in whole or in part as interest? If withholding taxes might apply, what are the typical methods for eliminating or reducing withholding taxes?

Since 1 March 2010, payments of interest and other income by debtors established or domiciled in France are not subject to any French withholding tax, unless they are made outside France in a non-cooperative State or territory (*NCST*) within the meaning of article 238-0 A of the French Tax Code (*FTC*), in which case they are subject to the 75 per cent withholding tax, set out under FTC, §125 A III, unless a tax treaty reduces or eliminates such withholding tax.

A jurisdiction is defined as an NCST if, cumulatively: (i) it is not a Member State of the European Union; (ii) it is under scrutiny by the OECD Global Forum on Transparency and Exchange of Information; and (iii) it has not entered into with France, or with 12 other jurisdictions, a treaty providing for the exchange of information in relation to tax matters.

The latest list of NCST was published by the French government on 10 April 2016 (with retrospective effect as from 1 January 2016) and includes the following countries: Botswana; Brunei; Guatemala; Marshall Islands; Nauru; Niue; and Panama.

The list is updated every year by the French government, with a view to including jurisdictions which would qualify as NCSTs pursuant to the criteria referred to above or which would, in practice, not be sufficiently cooperative with the French tax authorities (*FTA*). In any case, if a State or territory is added to the list on year N, the new rules will only have effect on payments to this State or territory on 1 January of year N+1. Jurisdictions which agree to exchange information in relation to tax matters with France, or which are removed from the aforementioned OECD list of jurisdictions under scrutiny, would be removed from the NCST list with immediate effect.

Interest payments on debt instruments issued or entered into prior to 1 March 2010 or which are to be consolidated (*assimilables*) with

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debt instruments issued before 1 March 2010 continue to benefit from the exemption (where available) provided by FTC, §131 *quater*. (In particular, interest paid in respect of *obligations* or *titres de créances négociables*, or other debt securities considered by the FTA as falling into similar categories, are exempt from the withholding tax set forth in FTC, §125 A III under FTC, §131 *quater*.)

The 75 per cent withholding tax does not apply if the debtor can prove that the "*main purpose and effect*" of the transactions from which the payments originate is not that of allowing the payments of interest and other income to be made in a NCST. Pursuant to the official doctrine of the FTA (BOI-RPPM-RCM-30-10-20-40-20140211, ## 60 and 70), an issue of debt securities benefits from such exception without their issuer having to provide any proof of the purpose and effects of such issue, if such debt instruments are:

(i) offered by means of a public offer within the meaning of article L.411-1 of the French Monetary and Financial Code or pursuant to an equivalent offer in a state other than a NCST (i.e. any offer requiring the registration or submission of an offer document by or with a foreign securities market authority);

(ii) admitted to trading on a French or foreign regulated market or multilateral securities trading system, provided that such market or system is not located in a NCST and the operation of such market is carried out by a market operator, an investment services provider, or a similar foreign entity, provided further that such market operator, investment services provider or entity is not located in a NCST; or

(iii) admitted, at the time of their issue, to the clearing operations of a central depositary or securities clearing, delivery and payments systems operator within the meaning of article L.561-2 of the French Monetary and Financial Code, or of one or more similar foreign depositaries or operators, provided that such depositary or operator is not located in a NCST.

A sale, by a seller located in France, of trade receivables at a discount or where a portion of the purchase price is payable upon collection of the receivable, should constitute a financial expense deductible from the seller's taxable result.

9.2 Seller Tax Accounting. Does your jurisdiction require that a specific accounting policy is adopted for tax purposes by the seller or purchaser in the context of a securitisation?

No, it does not.

9.3 Stamp Duty, etc. Does your jurisdiction impose stamp duty or other transfer or documentary taxes on sales of receivables?

There is no transfer tax, stamp duty or other documentary tax on the assignment of receivables (unless the assignment is voluntarily registered with the FTA, in which case a nominal stamp duty of EUR 125 per registered document is payable).

9.4 Value Added Taxes. Does your jurisdiction impose value added tax, sales tax or other similar taxes on sales of goods or services, on sales of receivables or on fees for collection agent services?

The assignment of receivables should not attract VAT in France.

Pursuant to the official doctrine of the FTA as currently in force (BOI-TVA-SECT-50-10-10-20120912, #340), the servicing fee paid to a French seller should qualify for the VAT finance exemption, except as regards debt recovery services which are subject to French VAT.

9.5 Purchaser Liability. If the seller is required to pay value-added tax, stamp duty or other taxes upon the sale of receivables (or on the sale of goods or services that give rise to the receivables) and the seller does not pay, then will the taxing authority be able to make claims for the unpaid tax against the purchaser or against the sold receivables or collections?

No, it will not.

9.6 Doing Business. Assuming that the purchaser conducts no other business in your jurisdiction, would the purchaser's purchase of the receivables, its appointment of the seller as its servicer and collection agent, or its enforcement of the receivables against the obligors, make it liable to tax in your jurisdiction?

The purchaser would have a French corporate income tax liability if the place of effective management of the purchaser were in France or the purchaser had a permanent establishment (*PE*) in France. In relation to securitisations, the question is whether the fact that the collection of receivables is carried out by the French seller might result in the French seller being deemed to act as a dependent agent of the purchaser and thus in creating a French PE of the purchaser. In order to reduce that risk, the seller should have limited authority to bind the purchaser, and the servicing agreement should be carefully drafted.

9.7 Taxable Income. If a purchaser located in your jurisdiction receives debt relief as the result of a limited recourse clause (see question 7.3 above), is that debt relief liable to tax in your jurisdiction?

Under French domestic tax law, securitisation vehicles are not taxable. As a result, provided that a purchaser is located in France, it should not be taxed upon any debt relief.

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1 Receivables Contracts

1.1 Formalities. In order to create an enforceable debt obligation of the obligor to the seller: (a) is it necessary that the sales of goods or services are evidenced by a formal receivables contract; (b) are invoices alone sufficient; and (c) can a binding contract arise as a result of the behaviour of the parties?

As a matter of German law, a receivable arises from the underlying contract between the seller and the debtor. Certain types of contract and the conclusion of certain contracts with certain counterparties (such as consumers) are subject to a requirement of form, e.g., need to be in writing or comply with further requirements. However, German law does not stipulate a general form requirement on contracts. More particularly, for the sale of goods or the provision of services between merchants, there are normally no specific form requirements to comply with. Where no form requirements apply, a contract may be concluded orally or also by conclusive behaviour. In practice, however, written form is invariably used as evidence for enforcement purposes. An invoice evidences the payment obligation of the debtor, but is neither required, nor sufficient for the receivable to be originated.

1.2 Consumer Protections. Do your jurisdiction's laws: (a) limit rates of interest on consumer credit, loans or other kinds of receivables; (b) provide a statutory right to interest on late payments; (c) permit consumers to cancel receivables for a specified period of time; or (d) provide other noteworthy rights to consumers with respect to receivables owing by them?

German law does not specifically limit permissible interest rates on loans or other kinds of receivables. However, as a general principle of German law, transactions *contra bonos mores* (*sittenwidrig*) are void. Hence, a contract providing for interest rates which are considered unethically high may be invalidated. Pursuant to relevant case law, the limit is (as a general rule) twice the market interest rate or about 12% *per annum* above such market interest rate. This does also apply to consumer loans, but German courts would take the status of the borrower as a consumer particularly into account. Further, with respect to consumer loans the lender must meet certain information and documentation requirements in order for the specification of the interest rate to be effective.

In case of a payment default (*Verzug*), German law provides for a statutory default interest rate on unpaid principal equal to the base rate (*Basiszinssatz*) plus 5% *per annum*. The applicable base interest rate is published by the German Central Bank (*Deutsche Bundesbank*). In case of receivables (not loans) and if the obligor is not a consumer, a base rate of 9% *per annum* applies. Under German law, the parties can generally not agree in advance to pay compound interest (*Zinseszins*).

Consumer loans (and transactions closely connected to consumer loans) are subject to special consumer protection rules. In particular, the lender is obliged to disclose, in writing, important information about the loan directed to support the consumer to understand its future payment terms. Additional disclosure obligations apply with regard to consumer real estate loans, i.e., *inter alia*, a possible assignment of the loan without the borrower's consent. In case the lender does not fulfil such disclosure obligations, enforcement issues may arise. Further, such consumer protection rules entitle the borrowers to revoke the loan within 14 days from the day on which they entered into the loan.

Borrowers may generally terminate loans at the end of any fixed interest period, in case such interest period expires prior to the maturity of the loan and no new rate of interest has been agreed to by the parties. In addition, borrowers may terminate loans with six months' prior notice at the end of the tenth year of the disbursement date of the loan. Further, the borrower of a floating rate loan has a statutory termination right entitling it to, generally and depending on the type of floating rate loan, terminate either with one month's prior notice at the end of each interest period, or with three months' prior notice.

Additional consumer protection laws apply where loans and related transactions are entered into at the residence of the consumer, by means of long distance communication or on the basis of general business conditions.

1.3 Government Receivables. Where the receivables contract has been entered into with the government or a government agency, are there different requirements and laws that apply to the sale or collection of those receivables?

There are no special requirements and rules for the sale or collection of receivables under receivables contracts entered into with the government or a government agency. If the public-sector debtor is a legal person under public law, § 354a HGB (*see* question 4.4 below) will always apply so that a contractual prohibition on assignments for the benefit of such debtor is always overcome. Tax credit and similar claims are subject to specific assignment limitations and notice requirements, and the German tax authorities can enforce previously assessed taxes without first obtaining an enforceable court judgment. Enforcement against public law debtors follows certain special rules and is subject to certain limitations.

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2 Choice of Law – Receivables Contracts

2.1 No Law Specified. If the seller and the obligor do not specify a choice of law in their receivables contract, what are the main principles in your jurisdiction that will determine the governing law of the contract?

Unless the parties have made an (explicit or implicit) choice of law in the receivables contract, pursuant to Regulation (EC) No. 593/2008 on the law applicable to contractual obligations (Rome I Regulation), the contract is governed by the laws of the country to which it is most closely connected. Several presumptions are set out in the Rome I Regulation in order to identify such relevant country. If these presumptions do not apply or lead to ambiguous results, the contract shall generally be governed by the law of the country where the party required to effect the characteristic performance of the contract has his habitual residence. However, if the contract is manifestly more closely connected with another country, the law of that other country shall apply. In case of carriage contracts, consumer contracts, insurance contracts and individual employment contracts more specific provisions of the Rome I Regulation apply.

2.2 Base Case. If the seller and the obligor are both resident in your jurisdiction, and the transactions giving rise to the receivables and the payment of the receivables take place in your jurisdiction, and the seller and the obligor choose the law of your jurisdiction to govern the receivables contract, is there any reason why a court in your jurisdiction would not give effect to their choice of law?

No, there is no such reason preventing a German court from applying German law in such case.

2.3 Freedom to Choose Foreign Law of Non-Resident Seller or Obligor. If the seller is resident in your jurisdiction but the obligor is not, or if the obligor is resident in your jurisdiction but the seller is not, and the seller and the obligor choose the foreign law of the obligor/seller to govern their receivables contract, will a court in your jurisdiction give effect to the choice of foreign law? Are there any limitations to the recognition of foreign law (such as public policy or mandatory principles of law) that would typically apply in commercial relationships such as that between the seller and the obligor under the receivables contract?

In these circumstances, a German court will, on the basis of Art. 3(1) Rome I Regulation, typically give effect to the choice of the non-German law of the jurisdiction of the obligor or the seller, respectively.

This is subject to certain limitations, such as that the effect of a choice of law under Art. 3(1) Rome I Regulation is limited to contractual rights and obligations and has no effect with respect to other legal issues such as dispositions (e.g., transfers or pledges) of *in rem* rights (cf. Art. 43 of the Introductory Act to the German Civil Code (*EGBGB*)) and may not be upheld as a valid choice of law by the courts of Germany if any contractual obligation arising is outside the scope of the Rome I Regulation. Further, German courts may refuse the application of a provision of the law of the seller/obligor chosen if such application is manifestly incompatible with the public policy (*ordre public*) of Germany (Art. 21 Rome I Regulation) or if the law was chosen intentionally in order to avoid the application of mandatory German law provisions which is, however, unlikely to be the case if the law of the seller or the obligor is chosen due to the factual connection of the seller and the obligor to such jurisdiction. Moreover, giving effect to the choice of non-German law will not restrict German courts from applying overriding mandatory provisions of German law (Art. 9(2) Rome I Regulation) and overriding mandatory provisions of the law of the country where the obligations arising out of the receivables contract are to be performed.

3 Choice of Law – Receivables Purchase Agreement

3.1 Base Case. Does your jurisdiction's law generally require the sale of receivables to be governed by the same law as the law governing the receivables themselves? If so, does that general rule apply irrespective of which law governs the receivables (i.e., your jurisdiction's laws or foreign laws)?

No, German law does not require the sale of receivables to be governed by the same law which governs the receivables. Rather, the freedom of choice of law under the Rome I Regulation also applies to a contract on the sale of receivables. Hence, the seller and the purchaser may, subject to the general limitations applying to the choice of law (*see* question 2.3 above), freely choose the law governing the sale of receivables.

Moreover, as German law distinguishes between the (contractual) sale of the receivables and the *in rem* transfer (i.e., the property aspects) of the receivables, it is noteworthy to clarify that such freedom to choose the governing law extends, as explicitly provided for in Art. 14(1) Rome I Regulation (together with recital 38), to the *in rem* transfer.

However, in order to take into account the interests of the debtor, the choice of law is limited by Art. 14(2) Rome I Regulation, pursuant to which the law governing the receivables shall determine its assignability, the relationship between the assignee and the debtor and the conditions under which the assignment can be invoked against the debtor and whether the debtor's obligations have been discharged. Further, the freedom of choice of law under the Rome I Regulation may arguably not extend to the enforceability of the sale/assignment against third parties, the question of which is, as per the prevailing opinion under German law, not addressed in the Rome I Regulation. Consequently, it is disputed which laws are relevant for this question. In application of general German conflict of law rules and case-law, a prevailing opinion points to the law governing the receivables on this question. Other authors favour the law chosen in accordance with the Rome I Regulation or the law of the seller jurisdiction. A minority view points to the law of the debtor jurisdiction in this regard.

3.2 Example 1: If (a) the seller and the obligor are located in your jurisdiction, (b) the receivable is governed by the law of your jurisdiction, (c) the seller sells the receivable to a purchaser located in a third country, (d) the seller and the purchaser choose the law of your jurisdiction to govern the receivables purchase agreement, and (e) the sale complies with the requirements of your jurisdiction, will a court in your jurisdiction recognise that sale as being effective against the seller, the obligor and other third parties (such as creditors or insolvency administrators of the seller and the obligor)?

A court in Germany will, as a matter of German law, recognise such sale as being effective against the seller, the obligor and other third parties.

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3.3 Example 2: Assuming that the facts are the same as Example 1, but either the obligor or the purchaser or both are located outside your jurisdiction, will a court in your jurisdiction recognise that sale as being effective against the seller and other third parties (such as creditors or insolvency administrators of the seller), or must the foreign law requirements of the obligor's country or the purchaser's country (or both) be taken into account?

For the sale and transfer by a German seller under German law of a German law governed receivable, German courts will, as a rule, not have regard to foreign law requirements of the obligor's country or the purchaser's country (or both). Hence, a court in Germany will, as a matter of German law, generally recognise such sale as being effective against the seller, the obligor and other third parties. One limitation is that, under German conflict of law rules, it is disputed how the third party effect is to be determined and a minority opinion points to the debtor jurisdiction (*see* question 3.1 above).

3.4 Example 3: If (a) the seller is located in your jurisdiction but the obligor is located in another country, (b) the receivable is governed by the law of the obligor's country, (c) the seller sells the receivable to a purchaser located in a third country, (d) the seller and the purchaser choose the law of the obligor's country to govern the receivables purchase agreement, and (e) the sale complies with the requirements of the obligor's country, will a court in your jurisdiction recognise that sale as being effective against the seller and other third parties (such as creditors or insolvency administrators of the seller) without the need to comply with your jurisdiction's own sale requirements?

Subject to the limitations applicable to the choice of law (*see* question 2.3 above), a German court will generally uphold the choice of law of the obligor's country to govern the receivables purchase agreement (such choice also extending to the *in rem* aspects between the seller and the purchaser in accordance with Art. 14(1) Rome I Regulation) and, as the sale complies with the requirements of the law of the obligor's country, recognise the sale and transfer as being effective between the seller and the purchaser.

On the third party effect, if a German court applied the requirements of the law of the obligor's country to also govern this question – either by applying the traditional (i.e., before the enactment of the Rome I Regulation) German law view (which pointed to the law governing the receivable) or by extending the scope of the choice of law under Art. 14(1) Rome I Regulation to this question – there would be no need to comply with German law requirements. However, if the German court applied the law of the seller's jurisdiction to this issue (as suggested by certain authors, *see* question 3.1 above), it would only recognise the sale and transfer as being effective *vis-à-vis* third parties if German law requirements are also complied with.

3.5 Example 4: If (a) the obligor is located in your jurisdiction but the seller is located in another country, (b) the receivable is governed by the law of the seller's country, (c) the seller and the purchaser choose the law of the seller's country to govern the receivables purchase agreement, and (d) the sale complies with the requirements of the seller's country, will a court in your jurisdiction recognise that sale as being effective against the obligor and other third parties (such as creditors or insolvency administrators of the obligor) without the need to comply with your jurisdiction's own sale requirements?

A court in Germany would consider such sale as being effective against the seller, the obligor and other third parties, because, as described in question 3.1 above, the law of the seller's jurisdiction would apply to all such questions only provided that the minority view pointing to the law of the obligor's jurisdiction for determining the third party effect would require German law requirements to be complied with.

3.6 Example 5: If (a) the seller is located in your jurisdiction (irrespective of the obligor's location), (b) the receivable is governed by the law of your jurisdiction, (c) the seller sells the receivable to a purchaser located in a third country, (d) the seller and the purchaser choose the law of the purchaser's country to govern the receivables purchase agreement, and (e) the sale complies with the requirements of the purchaser's country, will a court in your jurisdiction recognise that sale as being effective against the seller and other third parties (such as creditors or insolvency administrators of the seller, any obligor located in your jurisdiction and any third party creditor or insolvency administrator of any such obligor)?

Assuming that German law requirements are complied with, a court in Germany will consider such sale as being effective against the seller, the obligor and other third parties. This is because the German court will, with respect to the relationship between the seller and the purchaser, apply the law chosen by the seller and the purchaser (pursuant to Art. 14(1) Rome I Regulation) and the requirements of such law are complied with. Further, the German court will, *vis-à-vis* the obligor, apply German law (in accordance with Art. 14(2) Rome I Regulation) and, with respect to the third-party effect, also apply German law (as the law governing the receivable or of the seller's jurisdiction) or the law chosen between the seller and the purchaser – all of which laws are complied with. With respect to the third-party effect, the minority view pointing to the obligor jurisdiction might again stipulate requirements of such jurisdiction here.

4 Asset Sales

4.1 Sale Methods Generally. In your jurisdiction what are the customary methods for a seller to sell receivables to a purchaser? What is the customary terminology – is it called a sale, transfer, assignment or something else?

German law distinguishes between the law of obligations (*Schuldrecht*) and property law (*Sachenrecht*). Further, pursuant to the so-called "abstraction principle" (*Abstraktionsprinzip*), which is

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a fundamental principle of German private law, the obligations of the parties under the law of obligations (such transaction referred to as the "underlying transaction" – *Verpflichtungsgeschäft*) and the title transfer effected by a party in order to fulfil its respective obligation (such transactions referred to as the "implementing transactions" – *Verfügungsgeschäfte*) form separate transactions which are to be considered independently. The Rome I Regulation describes such a concept in its recital 38, as the "separate treatment of property aspects from the aspects under the law of obligations". Consequently, a sale of receivables under German law involves, from a legal standpoint, the following transactions: first of all, the sales contract under which the seller undertakes to sell, and the purchaser undertakes to purchase, the receivables, the transfer of title to the receivables by the seller to the purchaser and, strictly speaking as a third transaction, the transfer of the purchase price by the purchaser to the seller. Under German legal terminology, a sales contract constitutes a *Kaufvertrag* within the meaning of § 433 of the German Civil Code (*Bürgerliches Gesetzbuch – BGB*) and the transfer of title to the receivables is effected by way of an assignment (*Abtretung*) within the meaning of § 398 BGB. Among many other possibilities, one wording reflecting these separate transactions (which is, however, not necessary in order to create binding obligations), would be: "the seller sells (*verkauft*) and assigns (*tritt ab*) the receivables".

4.2 Perfection Generally. What formalities are required generally for perfecting a sale of receivables? Are there any additional or other formalities required for the sale of receivables to be perfected against any subsequent good faith purchasers for value of the same receivables from the seller?

Strictly speaking, under German law no concept of a perfection of a sale exists, the closest equivalent being the effectiveness of the assignment (*see* question 4.1 above) and, in order for the assignment to be effective, the mere agreement between the seller and the purchaser on the assignment is generally sufficient. Giving notice of the assignment to the obligor is not legally required. However, if the obligor is not notified of the assignment, the obligor may continue to be entitled to raise certain objections (*see* question 4.4 below). German law generally does not recognise a good faith acquisition of receivables.

4.3 Perfection for Promissory Notes, etc. What additional or different requirements for sale and perfection apply to sales of promissory notes, mortgage loans, consumer loans or marketable debt securities?

Promissory notes in other jurisdictions are often compared to German law *Schuldscheine* (certificates of indebtedness). A *Schuldschein* evidences an underlying loan agreement but does not constitute a security (in a sense of a transferable debt instrument) as a matter of German law. *Schuldscheine* are transferred by assigning the underlying loan claim and, hence, no additional or different requirements apply to their assignment (unless provided otherwise in the instrument). As a practical matter, the purchaser requires delivery of the debt certificates with regard to the assignment of the underlying loan.

Security interest on German real property can be granted in the form of either (i) an "accessory" mortgage (*Hypothek*) (mortgage), or (ii) a "non-accessory" land charge (*Grundschuld*) (land charge). Both kinds of security interest can be granted either in certificated or in non-certificated form. Mortgages have no practical significance.

A land charge can be transferred by written assignment of the land charge and, as applicable, (i) in the case of a certificated land charge, delivery of the land charge certificate, or (ii), in case of a non-certificated land charge, registration of the transfer with the competent land register. According to § 1192(1a) BGB, defences to which the owner is entitled with regard to the land charge on the basis of the security purpose agreement with the previous creditor, or which emerge from the security purpose agreement, may also be imposed on any assignee of the land charge.

Most land charges in Germany nowadays, are in non-certificated form. The required registration of the transfer with the land register may trigger significant costs. Further, a seller may want to avoid a registration with the land register in order to prevent the obligors from obtaining knowledge of the sale. Therefore, the seller sometimes holds the land charges as a trustee for the purchaser. However, whether such trust agreement will be recognised in case of insolvency of the seller is not clear. For that reason, the German Banking Act (*Kreditwesengesetz – KWG*) contains special provisions for refinancing register transactions which allow for the creation of insolvency remote trust arrangements.

Unless a seller shall continue to exclusively deal with the relevant consumer borrower, such seller is generally obliged to notify the consumer borrower of an assignment (providing certain details).

Bearer securities are transferred by way of an agreement between the seller and the purchaser to transfer ownership and the delivery of the securities to the purchaser. Registered securities are transferred by way of assignment of the rights evidenced by them. Instruments made out to order are transferred by an agreement between the seller and the purchaser to transfer ownership, endorsement and delivery of the instrument to the purchaser. To the extent that debt securities are certificated in global form and deposited with a clearing system, delivery of the securities is evidenced by a corresponding book-entry.

4.4 Obligor Notification or Consent. Must the seller or the purchaser notify obligors of the sale of receivables in order for the sale to be effective against the obligors and/or creditors of the seller? Must the seller or the purchaser obtain the obligors' consent to the sale of receivables in order for the sale to be an effective sale against the obligors? Whether or not notice is required to perfect a sale, are there any benefits to giving notice – such as cutting off obligor set-off rights and other obligor defences?

In order for the sale/assignment to be effective against the obligor and/or creditors of the seller, it is not legally required that the obligor is notified of the assignment (silent assignment). However, prior to a notification of the assignment to the debtor (and also, but generally speaking to a lesser degree, where the obligor was previously notified) statutory debtor protection provisions apply which give the debtor, *inter alia*, a set-off right in relation to claims it has against the assignor. In addition, the purchaser will be subject to any amendments of the underlying receivables contract or other transactions relating to the receivable, such as a waiver or deferral of payments entered into by the seller and the obligor. Furthermore, prior to a notification, the debtor may fully discharge its payment obligation by way of payment to the assignor. In practice these risks can be mitigated to a certain extent by introducing mandatory debtor notifications upon the occurrence of certain trigger events (such as an originator rating downgrade) and/or dilution reserves.

However, even where the obligor was previously notified, it may generally raise against the purchaser all the objections it had against the seller at the time of the sale. Where the sold receivable is a consumer loan, the seller generally has an obligation to notify the consumer of the assignment and to provide certain information

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about the purchaser; any violation of such obligations does not affect the effectiveness of the sale and assignment of the receivable, but may entitle the consumer to claim damages.

Where the obligor was not notified (and is not otherwise aware) of the assignment it may, in such a scenario, satisfy its obligations *vis-à-vis* the purchaser by making payment to the seller. Furthermore, under § 406 BGB, an obligor may set off against the assignee an existing claim which the obligor has against the assignor. An obligor cannot, however, effect such set-off where (a) the obligor knew of the assignment at the time of acquiring its claim against the assignor, *or* (b) where such claim of the obligor (i) did not become due until after the obligor had acquired such knowledge *and* (ii) matures after the claims of the assignee. On this basis, even where the obligor is aware of the assignment where either (a) it acquired its counterclaim against the seller before it obtained such knowledge, or (b) such counterclaim against the seller is due before the receivable owed by the obligor is due, it may continue to offset the assigned receivable against its counter-claim against the seller.

Accordingly, although the notification of the assignment of a receivable to the obligor is not required for an effective assignment of a receivable under German law, such notification has the benefit (from the purchaser's perspective) of preventing the obligor from being able to raise certain objections and exercising certain rights it may have against the seller *vis-à-vis* the purchaser.

Receivables governed by German law can generally be sold and assigned without the consent of the obligor, except where the underlying receivables contract contains a prohibition on assignments. Such a prohibition will usually be explicit, but can also be implied in the underlying receivables contract. According to a 2007 decision by the German Federal High Court (*Bundesgerichtshof – BGH*), neither German data protection laws nor general bank secrecy obligations constitute an implied prohibition on assignment. However, according to a 2013 decision of the German Federal High Court, an implied prohibition on assignments does exist where the confidentiality of the data to which the receivables in question relate is protected by criminal law (e.g., a doctor's patient data); accordingly, a valid assignment of any such receivables requires the obligor's consent.

Under certain circumstances and if the purchaser is prepared to assume a certain amount of additional risk, a securitisation of receivables containing a prohibition of assignment clause is also possible without consent if the requirements of § 354a of the German Commercial Code (*Handelsgesetzbuch – HGB*) are satisfied. Pursuant to § 354a(1) HGB, a receivable can be validly assigned despite any contractual prohibition of assignment if (i) the underlying agreement between the contracting parties constitutes a commercial transaction (*Handelsgeschäft*) for both parties, or (ii) the debtor is a public law entity (*juristische Person des öffentlichen Rechts*) or a separate estate governed by public law (*öffentlich-rechtliches Sondervermögen*). Please note that there are exceptions to this rule for (loan) receivables where a credit institution is the creditor, i.e., in such case any assignment without the contractually required consent would be void (§ 354a(2) HGB). Although an assignment of receivables with prohibition of assignment clauses can be valid pursuant to § 354a(1) HGB, some additional risks exist because the underlying debtor will always be entitled to effect a payment with discharging effect to the assignor, even in cases where the underlying debtor has been notified of the assignment.

4.5 Notice Mechanics. If notice is to be delivered to obligors, whether at the time of sale or later, are there any requirements regarding the form the notice must take or how it must be delivered? Is there any time limit beyond which notice is ineffective – for example, can a notice of sale be delivered after the sale, and can notice be delivered after insolvency proceedings have commenced against the obligor or the seller? Does the notice apply only to specific receivables or can it apply to any and all (including future) receivables? Are there any other limitations or considerations?

Pursuant to German law, as described in question 4.4 above, there is generally no need to notify the obligor of the assignment in order for the assignment to be effective, but a notification may exclude certain defences and counterclaims of the obligor. There are generally no specific form requirements regarding the notice. However, specific requirements may be contractually agreed or may apply, in specific circumstances, by statutory law.

4.6 Restrictions on Assignment – General Interpretation. Will a restriction in a receivables contract to the effect that "None of the [seller's] rights or obligations under this Agreement may be transferred or assigned without the consent of the [obligor]" be interpreted as prohibiting a transfer of receivables by the seller to the purchaser? Is the result the same if the restriction says "This Agreement may not be transferred or assigned by the [seller] without the consent of the [obligor]" (i.e., the restriction does not refer to rights or obligations)? Is the result the same if the restriction says "The obligations of the [seller] under this Agreement may not be transferred or assigned by the [seller] without the consent of the [obligor]" (i.e., the restriction does not refer to rights)?

The first alternative prohibits the transfer of receivables by the seller to the purchaser. In case of the second alternative, the term "agreement" might well be interpreted to include all "rights and claims under the agreement" which would, again, result in a prohibition of assignment. While less likely, the prohibition in the third alternative may also be interpreted (e.g., due to the use of the word "assigned") to extend to the assignment of rights and claims.

4.7 Restrictions on Assignment; Liability to Obligor. If any of the restrictions in question 4.6 are binding, or if the receivables contract explicitly prohibits an assignment of receivables or "seller's rights" under the receivables contract, are such restrictions generally enforceable in your jurisdiction? Are there exceptions to this rule (e.g., for contracts between commercial entities)? If your jurisdiction recognises restrictions on sale or assignment of receivables and the seller nevertheless sells receivables to the purchaser, will either the seller or the purchaser be liable to the obligor for breach of contract or tort, or on any other basis?

Contracting parties may enter into binding prohibitions on assignments under German law, with the exception that the parties are merchants in respect of commercial transactions (*see* question 4.4 above). Sellers, in general, will be liable to the obligor for any financial damages in case of any violation of such assignments.

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4.8 Identification. Must the sale document specifically identify each of the receivables to be sold? If so, what specific information is required (e.g., obligor name, invoice number, invoice date, payment date, etc.)? Do the receivables being sold have to share objective characteristics? Alternatively, if the seller sells *all* of its receivables to the purchaser, is this sufficient identification of receivables? Finally, if the seller sells *all* of its receivables *other than* receivables owing by one or more specifically identified obligors, is this sufficient identification of receivables?

According to German law, the receivables to be sold and assigned must be sufficiently identifiable (*bestimmbar*). This can be achieved by referring to each sold/assigned receivable specifically (by way of criteria allowing for an unequivocal identification of the relevant receivables, e.g., invoice number, invoice date, debtor, etc.) in a list or email attachment or other electronic submission.

The sale of "all of the seller's receivables" or the sale of all of the seller's receivables other than receivables owing by one or more specifically identified obligors would generally also be possible. However, referring to "all *eligible* receivables" will often be problematic due to the complexity (and, hence, uncertainty) involved in case of complex or extended eligibility criteria.

4.9 Recharacterisation Risk. If the parties describe their transaction in the relevant documents as an outright sale and explicitly state their intention that it be treated as an outright sale, will this description and statement of intent automatically be respected or is there a risk that the transaction could be characterised by a court as a loan with (or without) security? If recharacterisation risk exists, what characteristics of the transaction might prevent the transfer from being treated as an outright sale? Among other things, to what extent may the seller retain any of the following without jeopardising treatment as an outright sale: (a) credit risk; (b) interest rate risk; (c) control of collections of receivables; (d) a right of repurchase/redemption; (e) a right to the residual profits within the purchaser; or (f) any other term?

Generally, a sale and assignment will qualify as "true sale" and will not be recharacterised as a "secured loan" if it is a valid sale and does not contain the creation of a security interest in relation to the receivables which is granted to secure an underlying obligation of the seller *vis-à-vis* the purchaser.

The "true sale" analysis under German insolvency law requires a more substantive analysis than under English law since, under German law, there exists no specific judicial or statutory authority on the question as to the nature of a "legal true sale". The prevailing view is to apply the principles that have been established by German courts for distinguishing true or genuine factoring from untrue or non-genuine factoring. Pursuant to German case law, true sale factoring requires that the credit risk relating to the debtor of a receivable must be transferred to the purchaser who must not have the right to take recourse to the seller if such credit risk materialises. For this purpose, it is important that the transaction in substance (substance over form) is structured as a sale and is not recharacterised as a secured loan whereby it is decisive that the purchaser of the receivables can be considered the legal and economic owner of the receivables sold which requires that the purchaser assumes the risk of the underlying debtors defaulting on their payment obligations (transfer of credit risk/*del credere* risk).

A retention of the credit risk that might affect the true sale treatment can result, in particular, from corresponding repurchase obligations, automatic re-assignments, variable purchase price concepts (discounts), liquidity and/or credit enhancements granted by or on behalf of the seller or a first loss tranche position taken by the seller in the securitisation. However, as a general rule, a seller may retain some part of the credit risk corresponding to historical default rates and enforcement costs without triggering potential recharacterisation risks.

A discount and a deferred purchase price element can be incorporated into the purchase price paid for the relevant receivables without disturbing the true sale nature of the transaction, considering, however, that the discount and/or deferred element must be either reasonable (based on historical default rates plus a certain margin) or (according to a strong view in legal literature) fixed at the time of sale so as not to endanger the removal of the receivables from the transferor's balance sheet.

It is recognised that a certain limited level of credit enhancement may be provided by the seller but there is no definitive guidance as to what level of retention of credit risk is still acceptable.

4.10 Continuous Sales of Receivables. Can the seller agree in an enforceable manner to continuous sales of receivables (i.e., sales of receivables as and when they arise)? Would such an agreement survive and continue to transfer receivables to the purchaser following the seller's insolvency?

The seller can agree in an enforceable manner to a continuous sale/assignment of receivables. However, such agreements will not survive the insolvency of a seller. Hence, the transfer of receivables will not be continued.

4.11 Future Receivables. Can the seller commit in an enforceable manner to sell receivables to the purchaser that come into existence after the date of the receivables purchase agreement (e.g., "future flow" securitisation)? If so, how must the sale of future receivables be structured to be valid and enforceable? Is there a distinction between future receivables that arise prior to *versus* after the seller's insolvency?

Under German law it is possible to assign receivables prior to the time they come into existence (future receivables) by way of a corresponding sale and assignment agreement between the seller and the purchaser. Special care must be taken to ensure that an assignment of future receivables complies with the German principle of specificity (*Bestimmtheitsgrundsatz*). Pursuant to case-law, this requires for future receivables that, at the time a receivable comes into existence, it is sufficiently identifiable (*bestimmbar*), i.e., it can be ascertained whether such receivable at such time is covered by the assignment or not (*Bestimmbarkeit*). If a receivable comes into existence after the opening of insolvency proceedings against the seller, the seller is no longer entitled to dispose of its assets, including by way of a transfer of receivables. In practice, it can be difficult to determine whether or not a receivable actually constitutes a future receivable (e.g., a claim for future rental payments) to which the above rules are applicable, or rather an existing receivable that is not yet due (e.g., a repayment claim under a loan agreement).

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4.12 Related Security. Must any additional formalities be fulfilled in order for the related security to be transferred concurrently with the sale of receivables? If not all related security can be enforceably transferred, what methods are customarily adopted to provide the purchaser the benefits of such related security?

To the extent that related security can be transferred by way of mere agreement between the seller and the purchaser, there are generally no additional formalities to be complied with. However, e.g. insurance claims may require the notification to, and sometimes the prior consent of, the insurer in order to be transferred. If inventory or other movable objects are transferred as collateral by way of a security transfer (*Sicherungsübereignung*) the purchaser needs to obtain at least indirect possession. So-called accessory security interests (*akzessorische Sicherheiten*) – which are, as a matter of German statutory law, linked to the existence, extent and enforceability of the secured receivable – such as a pledge (*Pfandrecht*) or a surety (*Bürgschaft*), are automatically transferred together with the sold receivable.

4.13 Set-Off; Liability to Obligor. Assuming that a receivables contract does not contain a provision whereby the obligor waives its right to set-off against amounts it owes to the seller, do the obligor's set-off rights terminate upon its receipt of notice of a sale? At any other time? If a receivables contract does not waive set-off but the obligor's set-off rights are terminated due to notice or some other action, will either the seller or the purchaser be liable to the obligor for damages caused by such termination?

With respect to any waiver of set-off rights (and of other defences) by the obligor, the enforceability of such waiver needs to be considered. In practice, set-off waivers will often qualify as general business conditions (*Allgemeine Geschäftsbedingungen*) within the meaning of § 305 BGB in which case the waiver will be ineffective (in its entirety) if it does not contain carve-outs for undisputed claims of the obligor against the seller and such claims which have been determined by non-appealable judgment. The impact of an assignment on the obligor's defences is subject to protection rules of the BGB (*see* question 4.3 above). Without prejudice to such statutory protections which may entitle the obligor to set-off against the purchaser, the seller or the purchaser would generally not be liable to the obligor for the termination of the obligor's set-off rights as a result of the assignment.

4.14 Profit Extraction. What methods are typically used in your jurisdiction to extract residual profits from the purchaser?

Similar to other jurisdictions, *inter alia*, tax and true sale consequences (the latter generally being more problematic than in other jurisdictions – *see* question 4.9 above) of the profit extraction method need to be considered. Profit may be extracted, e.g., via equity, subordinated instruments or in the form of certain fees.

5 Security Issues

5.1 Back-up Security. Is it customary in your jurisdiction to take a "back-up" security interest over the seller's ownership interest in the receivables and the related security, in the event that an outright sale is deemed by a court (for whatever reason) not to have occurred and have been perfected (see question 4.9 above)?

It is not customary in Germany to create such back-up security.

5.2 Seller Security. If it is customary to take back-up security, what are the formalities for the seller granting a security interest in receivables and related security under the laws of your jurisdiction, and for such security interest to be perfected?

It is not customary in Germany to create such back-up security (*see* question 5.1 above).

5.3 Purchaser Security. If the purchaser grants security over all of its assets (including purchased receivables) in favour of the providers of its funding, what formalities must the purchaser comply with in your jurisdiction to grant and perfect a security interest in purchased receivables governed by the laws of your jurisdiction and the related security?

The general rules of the creation of security interests under German law also govern the security interests granted in the purchased receivables by a purchaser. Such granted security interests must be sufficiently identified or identifiable and can be granted in a form of a pledge or a security assignment.

The pledge of a receivable is created by an agreement between the pledgor and the pledgee. In addition, the underlying obligor must be notified. The security assignment is created by an agreement on the transfer of the receivable for security purposes between the assignor and the assignee. With the effect of such assignment, legal ownership to the receivables is transferred. Although there is no requirement for notification to the obligor, certain objections (such as rights of set-off or counterclaim arising from its relationship with the assignor) may be raised by the obligor prior to notification of the security assignment.

An assignment for security purposes is generally adopted in practice. This is because the requirement for a notification to the obligor can be avoided. However, inter-company receivables and bank accounts are the exceptions thereof since the notification to the obligor in this case does not cause any significant issues.

Security interests over inventory and other movable assets are usually granted by means of security transfer (as opposed to a pledge which is impracticable as it would require the transfer of actual possession of the assets to the secured party). *See* also question 4.3 above for additional requirements, as well as question 4.12 above.

5.4 Recognition. If the purchaser grants a security interest in receivables governed by the laws of your jurisdiction, and that security interest is valid and perfected under the laws of the purchaser's jurisdiction, will the security be treated as valid and perfected in your jurisdiction or must additional steps be taken in your jurisdiction?

The grant of security is generally subject to the same conflict of laws rules as the assignment of receivables (*see* question 3.1 above).

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According to these rules, *vis-à-vis* the purchaser and the secured party, a security interest would be treated as valid and perfected in Germany if the requirements under the chosen law were satisfied and the respective receivables are permitted to be assigned pursuant to the law governing such receivables. *Vis-à-vis* the obligor, the question whether a security interest is valid and perfected is determined by the law governing the receivables. Where the receivables are governed by German law, the purchaser and the secured party need to take any additional steps as may be required under German law to grant a valid and perfected security interest *vis-à-vis* the obligor. This also applies to the issue whether such a security interest is valid and perfected *vis-à-vis* third parties in case a German court, in line with prior case law, applies the law governing the receivables to this issue and not, as suggested by some legal commentators, the law of the seller's jurisdiction (*see* question 3.1 above).

5.5 Additional Formalities. What additional or different requirements apply to security interests in or connected to insurance policies, promissory notes, mortgage loans, consumer loans or marketable debt securities?

Security interests over such assets can also be granted by way of a formal pledge or a security assignment of receivables. Security interests over debt securities (which are treated as movable assets under German law) booked to a custody account are normally created by way of a pledge. The additional requirements described in question 4.3 above also apply to the grant of security over these types of assets. The specific terms of the underlying assets may stipulate additional transfer requirements, which will have to be satisfied regularly for the creation of security interests as well. For example, the creation of security interests over claims arising from insurance policies will often require the consent or at least the notification of the insurer.

5.6 Trusts. Does your jurisdiction recognise trusts? If not, is there a mechanism whereby collections received by the seller in respect of sold receivables can be held or be deemed to be held separate and apart from the seller's own assets (so that they are not part of the seller's insolvency estate) until turned over to the purchaser?

The English and U.S. law concepts of trusts differ substantially from the fiduciary instruments available under German law. The German Federal High Court (*Bundesgerichtshof – BGH*) has held in one instance that (foreign law) trusts over German law assets may not be compatible with German law. A mere trust agreement would also not be sufficient to separate the assets from the seller's insolvency estate and would likely not be recognised by German insolvency courts in the seller's insolvency. However, depending upon the law applicable to a trust, it is not inconceivable that German courts might recognise trusts over assets that are not governed by German law to segregate the assets from the seller's insolvency estate.

To achieve a separation of incoming collections from the seller's insolvency estate, it is accepted practice and the safest route under German law to ensure that collections are paid directly into an account over which a security interest has been created in favour of the purchaser. Typically, a pledge of the collection account will be used to create such security interest. Usually, the obligor will not be notified of the assignment and the seller is authorised to continue collecting the receivables. The seller should be required to ensure that all collections will be directly paid into such collection account pledged in favour of the purchaser. In cases of payments from such collection accounts being made to the purchaser, clawback rules will apply (*see* question 6.3 below).

Where it is not possible to use accounts separately to set up for the transaction, the seller should pledge its "general" collection account to the purchaser. However, often such a pledge will be junior to other security interests created over such account, as account pledges are customary in Germany. In such a scenario, a purchaser would need to ensure that cash transfers to the purchaser account occur as frequently as possible and the collection authority of the seller is revoked as early as possible (collections can then be redirected to an account of the purchaser after notification of the assignment and new account details to the underlying obligor).

5.7 Bank Accounts. Does your jurisdiction recognise escrow accounts? Can security be taken over a bank account located in your jurisdiction? If so, what is the typical method? Would courts in your jurisdiction recognise a foreign law grant of security (for example, an English law debenture) taken over a bank account located in your jurisdiction?

German law recognises escrow accounts. In order to create a security interest over a bank account located in Germany, the account is typically pledged in favour of the collateral taker. It is not recommended to establish a foreign law security interest over a German bank account as it is very uncommon and creates unnecessary difficulties from a conflicts of law perspective (especially where the foreign law security does not meet the requirements of a pledge under German law) and German account banks (which need to be notified of a pledge) will likely try to refuse to participate in any cash sweep mechanism in this context.

5.8 Enforcement over Bank Accounts. If security over a bank account is possible and the secured party enforces that security, does the secured party control all cash flowing into the bank account from enforcement forward until the secured party is repaid in full, or are there limitations? If there are limitations, what are they?

German account pledge agreements often contain arrangements pursuant to which a pledgee can take control of the account prior to actual enforcement of the pledge. Such arrangements are permissible under German law and can take the form of a mere account blockage (i.e., stopping the ability of the pledgor to continue disposing over the account) and/or an agreement pursuant to which the pledgee is granted a unilateral right to dispose over the account (including by way of (daily) cash sweep to a purchaser account). If insolvency proceedings have been opened with respect to the pledgor, the account agreement between the pledgor as account holder and the account bank will automatically terminate by statutory law. In order to gain access to the monies standing to the credit of the account, the pledgee will need to enforce the account pledge. In the insolvency of the pledgor, an account pledge will generally give the pledgee a right of separate satisfaction with respect to the monies standing to the credit of the account at the time of opening of insolvency proceedings.

5.9 Use of Cash Bank Accounts. If security over a bank account is possible, can the owner of the account have access to the funds in the account prior to enforcement without affecting the security?

The account pledge agreement may provide that the pledgor as account holder may continue to dispose over the funds in the account prior to the occurrence of a trigger event without affecting the pledge itself. However, any funds debited from the account by the pledgor will no longer be available to the pledgee.

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6 Insolvency Laws

6.1 Stay of Action. If, after a sale of receivables that is otherwise perfected, the seller becomes subject to an insolvency proceeding, will your jurisdiction's insolvency laws automatically prohibit the purchaser from collecting, transferring or otherwise exercising ownership rights over the purchased receivables (a "stay of action")? If so, what generally is the length of that stay of action? Does the insolvency official have the ability to stay collection and enforcement actions until he determines that the sale is perfected? Would the answer be different if the purchaser is deemed to only be a secured party rather than the owner of the receivables?

There is no general stay of action in relation to receivables effectively sold and transferred to the purchaser. However, during preliminary insolvency proceedings (*vorläufiges Insolvenzverfahren*) the insolvency court may, as a preliminary measure, order that assets in respect of which a segregation right (*Aussonderungsrecht*) or a right for preferential treatment (*Absonderungsrecht*) would exist if insolvency proceedings were opened, may not be realised or collected and may be utilised to continue the debtor's business provided that they are of material importance for its continuance. Although this is not reflected in the wording and there is no case law on point, it appears to be the prevailing view in legal literature that this provision should not apply in relation to receivables which had been effectively sold and transferred by the seller to the purchaser by means of a proper true sale.

Moreover, upon the opening of (final) insolvency proceedings, the purchaser of the receivables may only collect the receivables if the transaction is not recharacterised as a secured loan transaction. In case of a recharacterisation, the assignment of the receivables could be treated as a security assignment (secured loan). In such a case, the purchaser would not have a segregation right (*Aussonderungsrecht*) but only a right for preferential treatment (*Absonderungsrecht*) in which case the insolvency administrator would be entitled to collect the respective receivables and to deduct a certain haircut from the collection proceeds (*see* question 4.9 above and question 6.2 below).

6.2 Insolvency Official's Powers. If there is no stay of action, under what circumstances, if any, does the insolvency official have the power to prohibit the purchaser's exercise of its ownership rights over the receivables (by means of injunction, stay order or other action)?

In relation to a potential order a stay of action during preliminary insolvency proceedings *see* question 6.1 above. Moreover, German insolvency courts may have the right to issue an order entitling a preliminary insolvency administrator to collect receivables over which security was granted by way of a security assignment (which might also be relevant in case the transaction was recharacterised as secured loan).

After the opening of (final) insolvency proceedings, no stay of action is possible if the sale of receivables qualifies as a true sale. In case of recharacterisation of a transaction as a secured loan transaction, no formal stay of action is required as only the insolvency administrator would have the right to collect the respective receivables (*see* question 6.1 above).

6.3 Suspect Period (Clawback). Under what facts or circumstances could the insolvency official rescind or reverse transactions that took place during a "suspect" or "preference" period before the commencement of the seller's insolvency proceedings? What are the lengths of the "suspect" or "preference" periods in your jurisdiction for (a) transactions between unrelated parties, and (b) transactions between related parties? If the purchaser is majority-owned or controlled by the seller or an affiliate of the seller, does that render sales by the seller to the purchaser "related party transactions" for purposes of determining the length of the suspect period? If a parent company of the seller guarantee's the performance by the seller of its obligations under contracts with the purchaser, does that render sales by the seller to the purchaser "related party transactions" for purposes of determining the length of the suspect period?

Under the German Insolvency Code (*Insolvenzordnung – InsO*) an insolvency administrator of the seller (the originator) may rescind or reverse transactions (clawback) in relation to the assignment of rights of the receivables during the applicable suspect period – its length can be from one month to 10 years prior to the insolvency filing. Similar to many other jurisdictions, any clawback under these rules is not at the discretion of the insolvency court, but is governed by statutory rules.

Transactions voidable pursuant to these rules in particular (without limitation) include the following:

(i) Pursuant to § 130 InsO, a transaction shall be voidable which gave or made possible to an insolvency creditor, security or satisfaction if:
- it was effected in the last three months prior to the filing of a petition for the opening of insolvency proceedings, if the debtor was insolvent at the time of the transaction and if at such time the creditor had knowledge of such insolvency or of the relevant facts supporting a compelling conclusion with respect to such insolvency; or
- it was effected after the petition for the opening of insolvency proceedings and the creditor at the time of the transaction had knowledge of the insolvency or of the petition or of the relevant facts supporting a compelling conclusion with respect to such insolvency or petition.

(ii) Pursuant to § 131 InsO, a transaction shall be voidable that gave or made possible to an insolvency creditor, security or satisfaction to which such creditor had no right or no right in such manner or at such time if:
- the transaction was effected in the last month prior to the petition for the opening of the insolvency proceedings or after the filing of such petition;
- the transaction was effected during the second or third month prior to the petition for the opening of the insolvency proceedings and the debtor was insolvent as at the time of such transaction; or
- the transaction was effected during the second or third month prior to the petition for the opening of the insolvency proceedings and the creditor, as at the time of such transaction, had knowledge that it has adverse effects on the insolvency creditors or of the relevant facts supporting a compelling conclusion with respect to those adverse effects.

(iii) Pursuant to § 132 InsO, a transaction shall be voidable that had a direct adverse effect on the insolvency creditors, if:
- the transaction was effected during the last three months prior to the petition for the opening of the insolvency proceedings and, as at the time of such transaction, the

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debtor was insolvent and the creditor had knowledge of such insolvency or of the relevant facts supporting a compelling conclusion with respect to such insolvency; or

- the transaction was effected after the petition for the opening of the insolvency proceedings and, as at the time of such transaction, the creditor had knowledge of the insolvency or the petition or of the relevant facts supporting a compelling conclusion with respect to such insolvency or petition.

(iv) Pursuant to § 133(1) InsO, a transaction shall be voidable that was effected during the last up to 10 years prior to the petition for the opening of the insolvency proceedings or thereafter, if such transaction was entered into by the insolvent debtor with an intention to damage its (other) creditors, provided that the other party had actual knowledge of such intention, which knowledge is presumed to exist in the case that he/she had knowledge of the imminent insolvency of the debtor and the adverse effects caused thereby to the position of the insolvent debtor's creditors. Pursuant to § 133(2) InsO, the suspect period of up to 10 years is reduced to a maximum period of four years in case the transaction gave or made possible to the other party security or satisfaction. Further, pursuant to § 133(3) InsO knowledge of the intention to damage is only presumed if the other party had knowledge of the actual inability of the debtor to make payments when due, instead of knowledge of the imminent insolvency of the debtor in case the transaction gave or made possible to the other party security or satisfaction. In case the other party has agreed to a payment agreement with the debtor or granted any other form of payment facilitation, it will be presumed that it did not have knowledge of imminent insolvency at the time of the transaction.

(v) Pursuant to § 133(4) InsO, a contract with consideration between the debtor and a related person by which the insolvency creditors are directly harmed shall be voidable. Voidability is excluded if the contract was concluded more than two years prior to the petition for commencement of the insolvency proceedings or if the other party had no knowledge of the intention of the debtor to harm creditors.

(vi) Pursuant to § 134 InsO, a transaction made without consideration that was effected during last four years prior to the petition for the opening of the insolvency proceedings or thereafter, shall be voidable.

As some of the most relevant statutory provisions on challenge of transactions require that the counterparty of the assignor had knowledge of the fact that the assignor was unable to make payments at the time the legal act (e.g., an assignment of receivables) takes place, the risks of challenge could to some extent be mitigated by the delivery of a solvency certificate.

With the exception of directly harmful transactions (*cf.* § 133(4) InsO) the length of the suspect periods, generally, is independent of whether the transaction was entered into with a related party or an unrelated party. Instead, § 130 InsO and § 131 InsO provide that in case of related parties it will be presumed that the respective related party had knowledge that the transaction has adverse effects (§ 131(2) second sentence InsO) or had knowledge of the insolvency or of the filing of a petition for the opening of insolvency proceedings (§ 130(3) InsO and § 132(3) InsO).

The term "related party" is defined in § 138 InsO. According to § 138(2) InsO related parties of legal entities are: general partners, persons holding more than 25% of the insolvent debtor's capital, members of the insolvent debtor's management or supervisory bodies or person who, on the basis of a comparable corporate or service relationship with the debtor, have the opportunity to inform themselves of the insolvent debtor's economic circumstances. Accordingly, in case an entity (directly or indirectly) holds more than 25% of the insolvent debtor's share capital, such entity would be considered as a related party. A comparable corporate relationship would exist, if the insolvent debtor is controlled by the other party. In case of control the controlling entity will in practice also be deemed to have had the opportunity to inform itself of the debtor's economic circumstances and accordingly will be considered as a related party. Whether this is also the case for an affiliate of the other party does have to be determined in each individual case. As a general rule, the granting of a guarantee by a party that is a related party of the insolvent debtor (seller) should generally not render a true sale transaction between seller and purchaser into a related party transaction.

6.4 Substantive Consolidation. Under what facts or circumstances, if any, could the insolvency official consolidate the assets and liabilities of the purchaser with those of the seller or its affiliates in the insolvency proceeding? If the purchaser is owned by the seller or by an affiliate of the seller, does that affect the consolidation analysis?

No consolidation of assets and liabilities of the purchaser, with those of the seller or its affiliates, exists under German insolvency law. While under general German corporate law, there may be exceptional cases where a liability under the "piercing the corporate veil" principles may arise, those are rare in practice due to the stringent requirements under applicable German law and such liability will in any case not result in a consolidation of assets and liabilities.

In April of 2018, the German Act to Facilitate the Handling of Group Insolvencies (*Gesetz zur Erleichterung der Bewältigung von Konzerninsolvenzen*) has entered into force and introduced special provisions for group insolvencies, potentially such provisions could also become applicable in scenarios where the purchaser is owned by the seller or an affiliate of the seller. These recently introduced provisions are, however, limited to procedural questions, such as improving and requiring coordination between insolvency officials of the various group companies, and mainly aim at increasing the chances of a successful restructuring of the group companies. A consolidation of assets and liabilities is not provided for under this or any other applicable German law.

6.5 Effect of Insolvency on Receivables Sales. If insolvency proceedings are commenced against the seller in your jurisdiction, what effect do those proceedings have on (a) sales of receivables that would otherwise occur after the commencement of such proceedings, or (b) on sales of receivables that only come into existence after the commencement of such proceedings?

As a general rule, an insolvency administrator may elect whether to accept or reject the performance of so-called executory contracts, i.e., contracts which have not been fully performed by at least one party. Where the receivables purchase agreement has not been fully performed by at least one party, it may be subject to the insolvency administrator's election right. This may affect transactions involving the sale of future receivables. However, term deals are generally not subject to the insolvency administrator's election right as the seller (by assigning the receivables) has fully performed its respective obligations. In order to prevent such cherry-picking risk for revolving securitisations, each sale under a master agreement should be structured as an independent transaction.

If the insolvency administrator elects performance of the underlying executory contracts between the (insolvent) seller and its debtors (obligors), any future payments by such obligors would fall into the

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insolvency estate and could not be segregated or collected by the purchaser. If the insolvency administrator rejects the performance of the underlying executory contract, future receivables would not become due. In order to exclude such risks the securitisation transaction would generally have to be structured such that the insolvency administrator would not have an election right in relation to the underlying contracts.

Moreover, any assignment of future receivables coming into existence after the opening of insolvency proceedings (*künftige Forderungen*) (as opposed to an assignment of previously existing receivables which only become due after the opening of the insolvency proceedings (*betagte Forderungen*)) is not enforceable.

Leases and leasing agreements over movable assets entered into by the seller (originator) as lessor are not subject to the election right of the insolvency administrator if the acquisition of the leased movable assets was financed by a third party and that third party has been granted security by way of a security transfer of the leased movable asset. There is no clear guidance for scenarios in which the lessor is not identical to the owner of the leased movable asset, which is not uncommon in the German leasing market. Whether or not the receivables under such lease agreements qualify as future receivables depends on the facts and circumstances in the individual case, in particular the terms of the applicable lease agreements. Instalments due under so-called "financial leasing" contracts are generally considered not to constitute future receivables but to come into existence upon the conclusion of the leasing agreement and are due from time to time.

Leases with regard to real estate are not subject to the insolvency administrator's election right but may be terminated by the insolvency administrator subject to certain statutory notice periods. In addition, lease receivables under real estate leases constitute future receivables and cannot be validly assigned *vis-à-vis* the seller's/lessor's insolvency estate in case they fall in the period after the month in which the insolvency proceedings are opened (or, if the opening date is later than the 15th day of a month, the following month). However, any such lease receivables can be covered by a land charge over the real estate which is generally enforceable in the seller's insolvency.

In relation to fully disbursed loans (advanced by the seller as lender), the insolvency administrator's election right does not apply. Moreover, receivables being due from time to time under loans are not considered future receivables, but existing receivables that are not yet due.

6.6 Effect of Limited Recourse Provisions. If a debtor's contract contains a limited recourse provision (see question 7.3 below), can the debtor nevertheless be declared insolvent on the grounds that it cannot pay its debts as they become due?

In Germany, special purpose entity debtors are generally established in the form of a limited liability company (*Gesellschaft mit beschränkter Haftung – GmbH* or *Unternehmergesellschaft – UG*). The managing directors of such companies are required by law to file a petition for the opening of the insolvency proceedings if the debtor has become unable to pay its debts as they are due or it is over-indebted. Where the creditors have validly agreed to a limited recourse provision (*see* questions 7.4 and 7.5 below), such agreement would prevent the debtor from becoming over-indebted or illiquid, as the respective payment obligations would not come into existence to the extent the debtor has insufficient assets. However, in case the debtor has insufficient funds to pay all of its obligations that are not subject to a limited-recourse provision, it could still become over-indebted or illiquid and would therefore not be insolvency-remote.

In addition, where a limited-recourse provision provides for the conditional cancellation of the obligations of the debtor that are not covered by its assets, additional tax considerations need to be taken into account for such contingent payment obligations in order to avoid adverse tax consequences.

7 Special Rules

7.1 Securitisation Law. Is there a special securitisation law (and/or special provisions in other laws) in your jurisdiction establishing a legal framework for securitisation transactions? If so, what are the basics? Is there a regulatory authority responsible for regulating securitisation transactions in your jurisdiction?

There is neither a special securitisation law nor any special provisions in other German laws that would establish a comprehensive legal framework for securitisation transactions in Germany. German securitisation transactions are subject to the general legal framework in Germany, in particular the German civil law regime under the German Civil Code (*Bürgerliches Gesetzbuch – BGB*) and the insolvency law regime under the German Insolvency Code (*Insolvenzordnung – InsO*) as well as the relevant banking and financial services regulatory laws, in particular under the German Banking Act (*Kreditwesengesetz – KWG*). However, certain aspects specifically relevant to securitisations are addressed in special statutes and regulations. For example, the German Legal Services Act (*Rechtsdienstleistungsgesetz – RDG*) contains an exemption from licensing requirements for the provision of legal services and debt collection activities for the servicing of securitised receivables by the originator of the receivables. The German Banking Act contains special provisions for refinancing register transactions (Sec. 22a *et. seqq. KWG*) aimed at facilitating true sale securitisations in Germany.

In addition, several European Directives and Regulations provide for special rules for securitisations and parties involved in securitisation transactions, namely originators, sponsors and certain regulated investors. These rules provide, *inter alia*, that credit institutions and investment firms are prohibited from investing in securitisation transactions if the originator does not retain on an ongoing basis a net economic interest in the transaction of at least 5% (so-called "skin-in-the-game" requirements; Art. 405 of the EU Capital Requirements Regulation (Regulation (EU) 575/2013 – CRR)). Moreover, such institutions are subject to special investor due diligence requirements; they must have comprehensive and thorough knowledge of the securitisation positions (and the underlying assets) and establish formal due diligence and monitoring procedures (Art. 406 CRR). Comparable provisions apply in relation to insurance companies and pension funds under Solvency II (Directive 2009/138/EC) and the related Delegated Regulation (EU) 2015/35 and in relation to alternative investment funds (AIFs) and their managers (AIFMs) under the Alternative Investment Fund Managers Directive (Directive 2011/61/EU – AIFMD) and the related Delegated Regulation (EU) 231/2013. Currently, these rules only impose obligations on the regulated investors but they indirectly also affect the originators who have to structure the transactions in compliance with the risk retention and investor due diligence rules in order to enable regulated investors to invest in securitisation positions.

Under the revised European framework for securitisations, the regulatory regime will change significantly. On 17 January 2018, the EU Regulation setting out a new regulatory framework for securitisation transactions (Securitisation Regulation) took effect. The

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Securitisation Regulation introduces the concept of simple, transparent and standardised (STS) securitisation into European law. It sets out detailed criteria which a securitisation transaction must satisfy in order to qualify as STS. Moreover, the amended European capital requirements rules (CRR Amendment Regulation) will introduce a preferential capital regime for investments in STS securitisations by credit institutions and investment firms. The Securitisation Regulation will generally apply from 1 January 2019 to new securitisation issuances or the creation of new securitisation positions after that date (subject to certain transitional provisions). Whilst the 5% risk retention requirement is generally maintained, the new rules impose risk retention requirements directly on originators, sponsors and original lenders.

Moreover, there are specific tax rules and regulations in Germany dealing with certain tax aspects of securitisations (*see* also question 9 below). In addition, the predecessor of the Federal Financial Services Supervisory Authority (*Bundesanstalt für Finanzdienstleistungsaufsicht – BaFin*) had published regulatory guidelines for securitisations originated by banks in its circular 4/97 which still serve as important regulatory guidelines (*see* also question 8.3 below).

In Germany there is no special authority responsible for regulating securitisations. Securitisations are supervised as part of the general regulatory supervision regime through BaFin and the European Central Bank (ECB).

7.2 Securitisation Entities. Does your jurisdiction have laws specifically providing for establishment of special purpose entities for securitisation? If so, what does the law provide as to: (a) requirements for establishment and management of such an entity; (b) legal attributes and benefits of the entity; and (c) any specific requirements as to the status of directors or shareholders?

No, there are no laws in Germany that specifically provide for the establishment of special purpose entities for securitisations.

7.3 Location and form of Securitisation Entities. Is it typical to establish the special purpose entity in your jurisdiction or offshore? If in your jurisdiction, what are the advantages to locating the special purpose entity in your jurisdiction? If offshore, where are special purpose entities typically located for securitisations in your jurisdiction? What are the forms that the special purpose entity would normally take in your jurisdiction and how would such entity usually be owned?

From a legal perspective, it is generally possible to use German or foreign special purpose entities for German securitisation transactions. However, the tax implications have to be analysed depending on the type of securitisation and assets securitised (*see* question 9.6 below). Due to the German taxation system, securitisation entities are usually located abroad in offshore jurisdictions such as Jersey, Guernsey or the Cayman Islands or in other European jurisdictions which provide for a more favourable tax treatment and double taxation treaties such as Luxembourg, The Netherlands and Ireland. German special purpose entities are frequently used for securitisations of bank loans for which an exemption in relation to trade tax applies.

Even for bank loans there are no specific legal or tax reasons for using a German special purpose entity. From a practical perspective, one advantage of using a German special purpose entity may be the reduction of costs for implementing the transaction given that no foreign corporate services providers or specific foreign law legal advice may be required when structuring a German bank loan securitisation transaction. On the other hand, foreign jurisdictions such as Luxembourg, which enables compartment structures which can be used for several transactions, may offer more flexibility to originators frequently refinancing through securitisations.

If the special purpose entity shall be a German law entity, it usually takes the form of a German limited liability company (*Gesellschaft mit beschränkter Haftung – GmbH*), including in the form of a so-called "small GmbH" (*Unternehmergesellschaft/ (haftungsbeschränkt) – UG*) which can be established very quickly and with a minimal share capital of one Euro. There is a recognised way for establishing orphan securitisation entities in Germany, which builds on the infrastructure provided by TSI GmbH, a company which has been established to promote (true sale) securitisations in Germany. The shares of the German special purpose entity established under the TSI platform will be owned by three existing charitable foundations which have obtained the required formal recognition by public authorities (so-called orphan structure). Setting up orphan German securitisation entity outside of this structure may be more costly and time-consuming.

7.4 Limited-Recourse Clause. Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) limiting the recourse of parties to that agreement to the available assets of the relevant debtor, and providing that to the extent of any shortfall the debt of the relevant debtor is extinguished?

See question 7.5 below.

7.5 Non-Petition Clause. Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) prohibiting the parties from: (a) taking legal action against the purchaser or another person; or (b) commencing an insolvency proceeding against the purchaser or another person?

Although there is no securitisation specific case law on the point, limited-recourse and non-petition clauses are generally considered valid and enforceable under German law, and German courts would generally give effect to such arrangements notwithstanding the governing law, provided that the parties have validly chosen such law (*see* question 2.3 above). If governed by German law, limited-recourse and non-petition clauses should generally be valid and enforceable unless the underlying claim is based on wilful misconduct or, if the clause is considered as general business conditions (*Allgemeine Geschäftsbedingungen*), gross negligence of the purchaser.

If the special purpose entity does not have enough funds available to meet its obligations that are not subject to effective limited-recourse provisions, it could still become insolvent. Moreover *see* question 7.7 below with respect to the obligation of the management of certain German companies to file for insolvency upon illiquidity or over-indebtedness.

7.6 Priority of Payments "Waterfall". Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) distributing payments to parties in a certain order specified in the contract?

Priority of payments ("waterfall") provisions may generally be

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validly agreed among creditors and with the debtor, and German courts would generally give effect to these in an agreement notwithstanding the governing law, provided that the parties have validly chosen such law (*see* question 2.3 above). However, in case of insolvency of the purchaser, customary contractual waterfall provisions found in securitisation transactions would generally not alter the statutory order of priority provided for by German insolvency law. Rather, the creditors would generally be treated as equal ranking for German insolvency law purposes and would only be contractually obligated to distribute any amounts received by them pursuant to the agreed priority of payments.

7.7 Independent Director. Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) or a provision in a party's organisational documents prohibiting the directors from taking specified actions (including commencing an insolvency proceeding) without the affirmative vote of an independent director?

A German court would generally give effect to such a contractual provision in an agreement notwithstanding the governing law, provided that the parties have validly agreed to such choice of law (*see* question 2.3 above). However, for German special purpose entities, there is a statutory obligation for the directors to file for the opening of insolvency proceedings in case the company becomes unable to pay its debts as they come due (illiquidity) or over-indebted (over-indebtedness). Non-compliance with such filing obligation may lead to personal liability for damages and even criminal liability for the company's management.

7.8 Location of Purchaser. Is it typical to establish the purchaser in your jurisdiction or offshore? If in your jurisdiction, what are the advantages to locating the purchaser in your jurisdiction? If offshore, where are purchasers typically located for securitisations in your jurisdiction?

See question 7.3 above.

8 Regulatory Issues

8.1 Required Authorisations, etc. Assuming that the purchaser does no other business in your jurisdiction, will its purchase and ownership or its collection and enforcement of receivables result in its being required to qualify to do business or to obtain any licence or its being subject to regulation as a financial institution in your jurisdiction? Does the answer to the preceding question change if the purchaser does business with more than one seller in your jurisdiction?

As a general rule, the purchase and ownership of receivables by a special purpose entity under a securitisation transaction does not trigger any licence requirements for the purchaser. As long as the purchase of the receivables is structured as a true sale and, in case of loans, does not encompass the acquisition of any undrawn commitments or other funding obligations, the purchaser generally does not require any licence under the German Banking Act, in particular no licences for lending business or factoring business are required. Likewise, the collection and enforcement of the receivables do not trigger any licence requirements for the purchaser in Germany (*see* question 8.2 below in relation to servicing licences).

8.2 Servicing. Does the seller require any licences, etc., in order to continue to enforce and collect receivables following their sale to the purchaser, including to appear before a court? Does a third-party replacement servicer require any licences, etc., in order to enforce and collect sold receivables?

Loan servicing may in principle trigger licence or registration requirements under the German Legal Services Act (*Rechtsdienstleistungsgesetz – RDG*) as debt collection generally qualifies as legal service under the RDG. Where a third party services the receivables on behalf of the purchaser, such party generally must be registered under the RDG. An important exemption applies in relation to the servicing by the seller, i.e., no licence or registration requirement under the RDG will be triggered if the seller (originator) acts as servicer. If, however, the servicer is different from the seller (originator), the licence/registration requirement under the RDG could be triggered. In particular, alternative servicing structures such as master servicer structures or replacement servicer features in the transaction documents would have to be analysed in more detail so as to ensure that no licence/registration requirements will be triggered under the RDG.

8.3 Data Protection. Does your jurisdiction have laws restricting the use or dissemination of data about or provided by obligors? If so, do these laws apply only to consumer obligors or also to enterprises?

Yes. In Germany, the Federal Data Protection Act (*Bundesdatenschutzgesetz – BDSG*) restricts the use and dissemination of personal data about or provided by obligors. If (some of) the underlying debtors are natural persons or enterprises operated by a sole trader (*Einzelkaufmann*) or a partnership (*Personengesellschaft*) where a natural person is a partner, data protection legislation needs to be complied with. If the relevant persons have not expressly consented to the transfer of their personal data in connection with the securitisation transaction, the use of a data trustee structure under which data is only transferred in encrypted form, is normally recommended. The current provisions of the Federal Data Protection Act will be replaced or modified by the new EU General Data Protection Regulation (and related German transposition laws) which will enter into force on 25 May 2018.

Further restrictions apply in the case of a securitisation of German bank loans where the originating bank will generally need to comply with German banking secrecy rules (*Bankgeheimnis*) which apply to all types of debtors including natural persons, partnerships and corporations. There are established procedures, such as the appointment of a data trustee, for ensuring that banking secrecy and data protection issues are complied with.

In a securitisation of bank loans by German banks, specific servicing requirements set out in circular 4/97 (*see* also question 7.1) need to be complied with, pursuant to which, *inter alia*, each replacement servicer generally needs to be a credit institution licensed in the European Economic Area (EEA) or a notary.

8.4 Consumer Protection. If the obligors are consumers, will the purchaser (including a bank acting as purchaser) be required to comply with any consumer protection law of your jurisdiction? Briefly, what is required?

In the first instance it is the seller as originator of the receivables who is responsible for compliance with any applicable German

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consumer protection laws. A violation of consumer protection laws may affect the validity or enforceability of the receivables and the underlying agreements and may give the obligors rescission rights. Compliance with applicable consumer protection laws will therefore be checked by the purchaser by conducting a legal due diligence. In addition, it is market practice, that the seller (originator) will give representations and warranties as to compliance with applicable consumer protection laws. Special consumer protection laws apply, for example, in case of consumer loans or receivables agreements entered into at the obligor's place of residence or by means of long distance communication and/or if receivables contracts are based on the seller's general business conditions.

In relation to consumer loans the lender is required to inform the obligor three months before an agreed interest rate expires or the loan matures, stating whether it is willing to agree on a new interest rate or to extend the loan. Such obligation generally also applies to the purchaser in a securitisation transaction unless the seller and the purchaser have previously agreed that the seller shall exclusively continue to deal with the consumer obligor. In addition, there are certain restrictions (acceleration trigger levels) for a lender (and the purchaser of a loan) to accelerate an annuity loan in case of payment defaults of the consumer.

8.5 Currency Restrictions. Does your jurisdiction have laws restricting the exchange of your jurisdiction's currency for other currencies or the making of payments in your jurisdiction's currency to persons outside the country?

There are no general laws in Germany restricting such exchange of currency or the making of payments other than those implementing United Nations, EU or other international sanctions in respect of transactions with certain countries and persons. Moreover, if a German resident receives from, or makes payments to, any non-German resident, it will have to notify the German Central Bank (*Deutsche Bundesbank*) in certain circumstances. Such notification, however, serves for statistical purposes only and non-compliance does not affect the validity of the payment or the underlying obligation.

8.6 Risk Retention. Does your jurisdiction have laws or regulations relating to "risk retention"? How are securitisation transactions in your jurisdiction usually structured to satisfy those risk retention requirements?

See question 7.1 above for the European risk retention rules for credit institutions and investment firms, banks, insurance companies and pension funds and AIFs that apply in Germany. Securitisation transactions in Germany can be structured in any way that is compliant with the applicable European risk retention requirements, such as the following CRR risk retention options:

(i) retention of no less than 5% of the nominal value of each of the tranches sold or transferred to the investors;

(ii) in case of securitisations of revolving exposures, retention of the originator's interest of no less than 5% of the nominal value of the securitised exposures;

(iii) retention of randomly selected exposures, equivalent to no less than 5% of the nominal value of the securitised exposures;

(iv) retention of the first loss tranche, so that the retention equals in total no less than 5% of the nominal value of the securitised exposures; or

(v) retention of a first loss exposure not less than 5% of every securitised exposure in the securitisation.

8.7 Regulatory Developments. Have there been any regulatory developments in your jurisdiction which are likely to have a material impact on securitisation transactions in your jurisdiction?

Regulatory change in the field of securitisation is mainly driven by new European legislation which forms part of the European financial reform agenda. The new Securitisation Regulation and the revised European capital requirements framework have the greatest impact (*see* question 7.1 above). *See* also question 8.3 above in relation to the new EU General Data Protection Regulation.

9 Taxation

9.1 Withholding Taxes. Will any part of payments on receivables by the obligors to the seller or the purchaser be subject to withholding taxes in your jurisdiction? Does the answer depend on the nature of the receivables, whether they bear interest, their term to maturity, or where the seller or the purchaser is located? In the case of a sale of trade receivables at a discount, is there a risk that the discount will be recharacterised in whole or in part as interest? In the case of a sale of trade receivables where a portion of the purchase price is payable upon collection of the receivable, is there a risk that the deferred purchase price will be recharacterised in whole or in part as interest? If withholding taxes might apply, what are the typical methods for eliminating or reducing withholding taxes?

As a general rule, payments on receivables (including interest payments) are not subject to withholding tax in Germany. However, certain exceptions may apply, in particular in relation to certain hybrid debt instruments such as profit-participating loans if the debtor is tax resident in Germany or in relation to interest payable on loans which are secured on German real estate or German registered ships (regardless of the debtor's tax residence). If Germany is entitled to tax such income from interest payments under an applicable tax treaty, tax withheld may be credited or refunded upon tax assessment on the purchaser, which requires a tax filing of the purchaser.

Interest payments made by a bank or financial services institution as obligor may be subject to withholding tax on interest unless the recipient is itself a bank or financial services institution or is not subject to tax in Germany (subject to certain formal requirements being met).

The sale of trade receivables at a discount generally does not create a risk that the calculated discount may be recharacterised as interest in whole or in part, provided that the sale qualifies as true sale for tax purposes. Otherwise the sale may be recharacterised as a secured loan in the form of a profit-participating loan.

9.2 Seller Tax Accounting. Does your jurisdiction require that a specific accounting policy is adopted for tax purposes by the seller or purchaser in the context of a securitisation?

No, there is currently no specific accounting policy for tax purposes in Germany in the context of a securitisation. As a general rule, German GAAP is also applicable for German tax law. The key question will be whether the economic ownership (*wirtschaftliches Eigentum*) in the underlying receivables is transferred to the purchaser which basically requires that the transaction qualifies as a

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true sale and is not recharacterised as a secured loan. There is a risk that economic ownership of the receivables stays with the seller and no true sale can be achieved if the seller continues to bear the default risk which is, in particular, the case if the retained purchase price portion covers or compensates for any credit risk exceeding the expected default rate (*see* also question 4.9 above). The accounting treatment under IFRS or US GAAP, which may differ from German GAAP, is not relevant from a German tax perspective.

9.3 Stamp Duty, etc. Does your jurisdiction impose stamp duty or other transfer or documentary taxes on sales of receivables?

Germany currently does not impose any stamp duty or other documentary taxes on the sale and transfer of receivables. This might change in the near future in relation to the sale of securitised receivables which might become subject to financial transaction tax (*Finanztransaktionsteuer*) once the new rules have been introduced in Germany as one of the 10 EU Member States that have announced to participate in the new European financial transaction tax concept.

9.4 Value Added Taxes. Does your jurisdiction impose value added tax, sales tax or other similar taxes on sales of goods or services, on sales of receivables or on fees for collection agent services?

Germany generally imposes value added tax (VAT) (at a rate of 19%) on the sale of goods and services. However, as a general rule, the sale of receivables is not subject to German VAT but the seller can elect to waive this VAT exemption as long as the purchaser is considered an entrepreneur.

Fees for collection agent services would generally be subject to VAT. However, from the German tax authorities' perspective an important exception applies where the seller continues to collect the receivables. Such servicing of receivables by the seller (originator) is customary for securitisation transactions in Germany. In these cases, the collection of the receivables by the seller is not considered as a separate service but as a mere ancillary service which is VAT exempt. If, by contrast, the purchaser itself or a third-party servicer is acting as collection agent, VAT may become payable by the purchaser or the third-party servicer.

9.5 Purchaser Liability. If the seller is required to pay value-added tax, stamp duty or other taxes upon the sale of receivables (or on the sale of goods or services that give rise to the receivables) and the seller does not pay, then will the taxing authority be able to make claims for the unpaid tax against the purchaser or against the sold receivables or collections?

The purchaser can be held secondarily liable for VAT included in the amount of the receivables assigned to it to the extent it collects payment on them and provided further that the seller (originator) does not pay VAT on the underlying sale of goods or services when due. If the special purpose entity further assigns or transfers the receivables, it will be deemed to have received full payment on the receivables. This will also hold true for any further assignment or pledge of the receivables to a third party (including a security assignment or pledge of the receivables to a security trustee).

However, the receivables are deemed uncollected if, and to the extent, the purchaser pays consideration for these to the seller without any particular restrictions. As a consequence, the risk for secondary liability of the purchaser is generally limited to the VAT included in the difference between the face value of the receivables sold and the purchase price paid by the seller (taking into account discounts and cash reserves).

9.6 Doing Business. Assuming that the purchaser conducts no other business in your jurisdiction, would the purchaser's purchase of the receivables, its appointment of the seller as its servicer and collection agent, or its enforcement of the receivables against the obligors, make it liable to tax in your jurisdiction?

As a general rule, the mere purchase of receivables should not give rise to tax liability of the purchaser in Germany. This may be different if the purchased receivables give rise to income from German sources such as in case of interest payments on hybrid debt instruments or on loans secured by German real estate or German registered ships (*see* question 9.1 above). In most of its tax treaties, Germany has waived the right to tax interest on such loans.

Moreover, the appointment of the seller as the purchaser's servicer and collection agent, or the purchaser's enforcement of the receivables against the obligors, should generally not give rise to tax liability of the purchaser in Germany. However, the German tax authorities indicated that the purchaser may be treated as a German tax resident if it qualifies as a corporate entity without any substantial presence (office space, infrastructure, staff, etc.) outside of Germany. In this case, the purchaser's effective place of management could be considered to be in Germany due to the fact that the commercial activities of a servicer and collection agent require decisions relating to the day-to-day management of the purchaser's business such as the enforcement of the receivables against the obligors in Germany. As a consequence, in such a case, the purchaser may be subject to German corporate income tax and trade tax. By carefully structuring the transaction (e.g., enough substance for the non-German purchaser, main business decisions and functions of the purchaser other than the debt collection only taken in its country of incorporation, no further services performed in Germany other than the servicing, etc.), it should be possible to mitigate the risk that the purchaser is considered to have its effective place of management or a permanent establishment in Germany.

Even where the purchaser's business is effectively managed from outside of Germany, the seller (originator) servicing and collecting the sold receivables on behalf of the purchaser could be considered a permanent representative of the purchaser. This depends mainly on whether the seller is bound by the purchaser's instructions. If the purchaser agrees that the seller continues the collection in accordance with pre-agreed servicing principles on basically the same terms as before and the purchaser is not permitted to intervene, there are good arguments to consider that the seller is not a permanent representative of the purchaser.

9.7 Taxable Income. If a purchaser located in your jurisdiction receives debt relief as the result of a limited recourse clause (see question 7.3 above), is that debt relief liable to tax in your jurisdiction?

As a general rule, a debt relief may be subject to German corporate income tax as well as trade tax, as it may be seen as extraordinary profit. When structuring a securitisation transaction involving a German purchaser, it will be important to discuss the specific wording of the limited recourse clause with the tax advisers in order to reduce related tax risks.

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Our securitisation practice is renowned for being innovative and creating benchmarks in the market and, most importantly, providing clients with commercially viable structures in the increasingly regulated international markets. Our team regularly advises arrangers, originators and trustees on transactions involving a wide variety of asset classes and structures, including ‘true sale’ and synthetic securitisations, CLOs, CDOs and the establishment of securitisation programmes. Our experience includes advising on precedent-setting residential and commercial mortgage-backed securitisations, whole business and public sector securitisations, as well as securitisations of trade receivables, auto loans, consumer loans, shipping loans and aircraft loans.

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1 Receivables Contracts

1.1 Formalities. In order to create an enforceable debt obligation of the obligor to the seller: (a) is it necessary that the sales of goods or services are evidenced by a formal receivables contract; (b) are invoices alone sufficient; and (c) can a binding contract arise as a result of the behaviour of the parties?

(a) Under Greek law, it is not necessary for the creation of an enforceable debt obligation of the debtor that a sale of goods or the provision of services is evidenced by a formal receivables contract, unless otherwise provided by law (see article 158 of the Greek Civil Code – **GCC**). Examples of such formality requirement may be found in the field of regulated financial services, consumer protection legislation or in respect of real property transfer.

(b) An invoice alone can be sufficient to create an enforceable debt obligation. Depending on its terms, it may represent the contract between the parties or evidence the respective debt obligation and, to the extent accepted by the obligor, it can be used, without any other supporting documentation, for the issuance of a court payment order.

(c) An oral agreement on the sale of goods or the provision of services or an implied agreement that is deemed to exist on the basis of certain facts and circumstances (including the behaviour of the parties) is sufficient to constitute a binding contract. In all cases, it is for the competent court to decide the specifics and the enforceability of the debt obligation arising under such contract.

1.2 Consumer Protections. Do your jurisdiction's laws: (a) limit rates of interest on consumer credit, loans or other kinds of receivables; (b) provide a statutory right to interest on late payments; (c) permit consumers to cancel receivables for a specified period of time; or (d) provide other noteworthy rights to consumers with respect to receivables owing by them?

(a) Non-banking interest rates and default interest rates for contractual obligations are subject to certain limits that are adjusted periodically by reference to the ECB interest rates. Compound interest is allowed, subject to certain restrictions.

Banking interest rates may be freely determined on the basis of applicable banking legislation. However, banking interest rates and compound interest are subject to certain restrictions, mainly concerning the criteria for their setting, the unilateral change by the banks and the frequency of interest capitalisation.

(b) A statutory right to interest on late payments in commercial transactions is provided by virtue of Paragraph Z of Greek law 4152/2013 that transposed the Late Payment Directive (i.e. Directive 2011/7/EU on combatting late payment in commercial transactions) into Greek legislation. For contracts concluded prior to the entry into force of said law (i.e. 16 March 2013), the provisions of Presidential Decree 166/2003, which was previously in force and implemented Directive 2000/35/EC, shall be applicable.

(c) The GCC provides for the general right of the purchaser to, *inter alia*, withdraw from a sales contract in case of actual defect or lack of agreed quality. Furthermore, consumer protection legislation provides for the right of the consumer to cancel, under certain circumstances, a contract within 14 days from its conclusion or from the notification of the contract's terms and conditions (if later).

(d) Greek law is harmonised with the European legal framework regulating consumer protection and in this respect it includes effective provisions relating to the content of standard terms and conditions of consumer contracts and the corresponding rights of the consumer to deny payment on the basis of abusive terms and conditions, notification obligations, etc. Furthermore, there is extensive court precedence regulating these issues.

1.3 Government Receivables. Where the receivables contract has been entered into with the government or a government agency, are there different requirements and laws that apply to the sale or collection of those receivables?

In general, the sale of goods or the provision of services to the state authorities and the public sector are governed by the specific provisions of the European legislation regulating public procurement, as these have been transposed into Greek legislation, and the special Greek law provisions that reserve favourable treatment to the Greek state in a series of matters (e.g. prolonged deadlines, prolonged prescription periods, special approval and/or authorisations required for the validity of certain contracts concluded with the state, special notification mechanisms, special requirements for enforcement against only the private property of the state authorities and not against property destined for public use).

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2 Choice of Law – Receivables Contracts

2.1 No Law Specified. If the seller and the obligor do not specify a choice of law in their receivables contract, what are the main principles in your jurisdiction that will determine the governing law of the contract?

In cases where both the seller and the obligor are Greek residents, delivery is agreed to take place in Greece and there are no foreign elements in their receivables contract, Greek law will apply. In cases where one of the parties is not a Greek resident and/or delivery is agreed to take place outside Greece and/or other foreign elements appear in the receivables contract, the governing law thereto will be determined, in the absence of a specific choice of law, pursuant to Regulation (EC) 593/2008 on the law applicable to contractual obligations (**Rome I Regulation**), which is directly applicable in Greece. In this respect, pursuant to article 4 of Rome I the receivables contract shall be governed by:

(a) the law determined pursuant to the criteria of article 4 par. 1, designating as applicable the law of the seller's or service provider's habitual residence; or, if this is not possible

(b) the law of the country where the party required to effect the characteristic performance of the contract has his habitual residence (article 4 par. 2); or, if this is not possible

(c) the law of the country with which the contract is most closely connected (article 4 par. 4).

Where it is clear from all the circumstances of the case that the contract is manifestly more closely connected with a country other than that indicated in article 4 par. 1 or 2, the law of that other country shall apply.

Specific contracts are regulated by special private international law provisions (such as consumer contracts and contracts of carriage).

2.2 Base Case. If the seller and the obligor are both resident in your jurisdiction, and the transactions giving rise to the receivables and the payment of the receivables take place in your jurisdiction, and the seller and the obligor choose the law of your jurisdiction to govern the receivables contract, is there any reason why a court in your jurisdiction would not give effect to their choice of law?

No, a Greek court would give effect to the parties' choice of law.

2.3 Freedom to Choose Foreign Law of Non-Resident Seller or Obligor. If the seller is resident in your jurisdiction but the obligor is not, or if the obligor is resident in your jurisdiction but the seller is not, and the seller and the obligor choose the foreign law of the obligor/seller to govern their receivables contract, will a court in your jurisdiction give effect to the choice of foreign law? Are there any limitations to the recognition of foreign law (such as public policy or mandatory principles of law) that would typically apply in commercial relationships such as that between the seller and the obligor under the receivables contract?

Pursuant to Rome I Regulation, a contract shall be governed by the law chosen by the contracting parties. Therefore, the parties are free to choose a law other than Greek law governing the receivables contract. However, this is with the proviso that where all other elements relevant to the situation at the time of the choice are located in Greece only, the choice of the parties shall not prejudice the application of provisions of the law of Greece which cannot be derogated from by agreement, and Greek courts may refuse to apply provisions that are considered contrary to Greek rules of mandatory law within the meaning of article 9 or to Greek public order within the meaning of article 21 of the Rome I Regulation. Additional exceptions apply to certain types of contracts, such as consumer contracts and contracts of carriage as per the respective provisions of the Rome I Regulation.

3 Choice of Law – Receivables Purchase Agreement

3.1 Base Case. Does your jurisdiction's law generally require the sale of receivables to be governed by the same law as the law governing the receivables themselves? If so, does that general rule apply irrespective of which law governs the receivables (i.e., your jurisdiction's laws or foreign laws)?

Greek law does not require the sales contract to be governed by the same law governing the receivables, irrespective of which law this is. However, the *in rem* transaction, i.e. the transfer of the receivables, shall be governed by the law governing the receivables with respect to the issues referred to in article 14 of the Rome I Regulation.

3.2 Example 1: If (a) the seller and the obligor are located in your jurisdiction, (b) the receivable is governed by the law of your jurisdiction, (c) the seller sells the receivable to a purchaser located in a third country, (d) the seller and the purchaser choose the law of your jurisdiction to govern the receivables purchase agreement, and (e) the sale complies with the requirements of your jurisdiction, will a court in your jurisdiction recognise that sale as being effective against the seller, the obligor and other third parties (such as creditors or insolvency administrators of the seller and the obligor)?

In principle, yes.

Article 14 of the Rome I Regulation provides that the relationship between the assignor (the seller in the example) and the assignee (the purchaser) under a voluntary assignment or contractual subrogation of a claim against another person (the obligor) shall be governed by the law that applies to the contract between the assignor and assignee, while the law governing the assigned claim shall determine the ability to transfer such claim, the relationship between the assignee and the debtor, the conditions under which the assignment or subrogation can be invoked against the debtor and whether the debtor's obligations have been discharged.

As regards, in particular, the sale of receivables for the purpose of a securitisation transaction under Greek law 3156/2003 (the **Securitisation Law**), which is applicable where the seller is a merchant domiciled or operating through a permanent establishment in Greece and the purchaser is a special purpose entity established in Greece or abroad with the sole purpose to acquire business claims and is the issuer of the bonds, certain specific provisions apply regarding the process of sale and transfer of the receivables. In this respect, among other things, a written agreement between the seller and the purchaser is required, which must be recorded in the public pledge registry. The sale of the receivables to be transferred is governed by the provision of the GCC on the sale of goods, unless otherwise provided in the sale contract by the parties, while the transfer agreement is governed by the provisions of the

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GCC on assignment, to the extent not contrary to the Securitisation Law. In most Greek securitisation transactions, the parties choose foreign law to govern the sale contract, while the actual transfer (assignment) agreement is governed by Greek law. It is noted that, although a different legal regime applies with respect to the securitisation of receivables where the seller is the Greek state, a legal entity of public law or public enterprise wholly owned by public sector entities, i.e. article 14 of Greek law 2801/2000, the seller and the purchaser may choose the law applicable to the sale contract.

As regards the recognition of the sale against third parties, it can be stated that the transfer of the relevant receivables can be invoked both against the obligor and third parties upon completion of the assignment formalities provided either under the GCC or the Securitisation Law. As regards, in particular, recognition by insolvency administrators, the Securitisation Law provides for the ring-fencing of the securitisation transaction and the transfer against insolvency proceedings for the seller once the publication requirement has been completed.

3.3 Example 2: Assuming that the facts are the same as Example 1, but either the obligor or the purchaser or both are located outside your jurisdiction, will a court in your jurisdiction recognise that sale as being effective against the seller and other third parties (such as creditors or insolvency administrators of the seller), or must the foreign law requirements of the obligor's country or the purchaser's country (or both) be taken into account?

To the extent that the receivables are governed by Greek law, Rome I shall apply and Greek law shall be applicable as to the relevant formalities for the validity of the transfer of the receivables, irrespective of the law chosen by the parties or the place of residence of the obligor or the purchaser. Therefore, the Greek courts shall recognise the sale as being effective against the seller and other third parties, under the condition that the formalities of the GCC or the Securitisation Law with regards to the completion of the assignment have been effected. As regards the insolvency of the Greek seller, please refer to the answer to question 3.2 above.

3.4 Example 3: If (a) the seller is located in your jurisdiction but the obligor is located in another country, (b) the receivable is governed by the law of the obligor's country, (c) the seller sells the receivable to a purchaser located in a third country, (d) the seller and the purchaser choose the law of the obligor's country to govern the receivables purchase agreement, and (e) the sale complies with the requirements of the obligor's country, will a court in your jurisdiction recognise that sale as being effective against the seller and other third parties (such as creditors or insolvency administrators of the seller) without the need to comply with your jurisdiction's own sale requirements?

Yes, in the sense that the Greek court will not examine compliance with the requirements of Greek law for the sale of the receivables.

3.5 Example 4: If (a) the obligor is located in your jurisdiction but the seller is located in another country, (b) the receivable is governed by the law of the seller's country, (c) the seller and the purchaser choose the law of the seller's country to govern the receivables purchase agreement, and (d) the sale complies with the requirements of the seller's country, will a court in your jurisdiction recognise that sale as being effective against the obligor and other third parties (such as creditors or insolvency administrators of the obligor) without the need to comply with your jurisdiction's own sale requirements?

Please refer to the answer to question 3.4 above.

3.6 Example 5: If (a) the seller is located in your jurisdiction (irrespective of the obligor's location), (b) the receivable is governed by the law of your jurisdiction, (c) the seller sells the receivable to a purchaser located in a third country, (d) the seller and the purchaser choose the law of the purchaser's country to govern the receivables purchase agreement, and (e) the sale complies with the requirements of the purchaser's country, will a court in your jurisdiction recognise that sale as being effective against the seller and other third parties (such as creditors or insolvency administrators of the seller, any obligor located in your jurisdiction and any third party creditor or insolvency administrator of any such obligor)?

To the extent that the receivable is governed by Greek law, its transfer should comply with the requirements of Greek law. In this respect, we refer you to the answer to question 3.1 above.

4 Asset Sales

4.1 Sale Methods Generally. In your jurisdiction what are the customary methods for a seller to sell receivables to a purchaser? What is the customary terminology – is it called a sale, transfer, assignment or something else?

Receivables are sold by way of a sales contract regulated by the sale of goods provisions of the GCC (articles 514 *et seq.*). The transfer thereof (i.e. the *in rem* transaction) is effected through assignment pursuant to articles 455 *et seq.* of the GCC.

Receivables may also be transferred through special financial structures, such as factoring and forfeiting agreements (Greek law 1905/1990), in case of issuance of specific forms of covered bonds (article 152 of Greek law 4261/2014) or securitisation transactions.

The terms commonly used are "sale" and "transfer" or "assignment", where "assignment" and "transfer" are used interchangeably.

4.2 Perfection Generally. What formalities are required generally for perfecting a sale of receivables? Are there any additional or other formalities required for the sale of receivables to be perfected against any subsequent good faith purchasers for value of the same receivables from the seller?

For sales and transfers effected pursuant to the general provisions of the GCC, the main condition for the perfection of the assignment of a claim against an obligor and third parties is the notification of

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the obligor by either the assignor or the assignee. In securitisation transactions, such notification is effected with the registration of the summary of the assignment and transfer agreement in the public registry book in accordance with article 3 of Greek law 2844/2000, kept with the competent pledge registry. Prior to the notification (or the registration in case of securitisation transactions), the assignee bears the risk of the release of the obligor from its obligations upon payment to the assignor and the risk of enforcement by third parties' creditors of the assignor upon the assigned claim, which will continue to be considered property of the assignor, as well as the clawback risk, since the assigned claim will be considered part of the bankruptcy estate.

4.3 Perfection for Promissory Notes, etc. What additional or different requirements for sale and perfection apply to sales of promissory notes, mortgage loans, consumer loans or marketable debt securities?

Promissory Notes and other forms of marketable debt instruments not registered with a central securities depository are transferred by way of endorsement and delivery to the new holder of the underlying debt. If the marketable debt instruments are registered with a central securities depository, they are transferred by way of a transfer order to the account of the purchaser held with the CSD. Mortgage loans and consumer loans are transferred in accordance with the answer to question 4.1 above. Mortgages and other securities are considered ancillary rights and are transferred together with the secured claims, subject to the relevant formalities (see question 4.11 below).

4.4 Obligor Notification or Consent. Must the seller or the purchaser notify obligors of the sale of receivables in order for the sale to be effective against the obligors and/or creditors of the seller? Must the seller or the purchaser obtain the obligors' consent to the sale of receivables in order for the sale to be an effective sale against the obligors? Whether or not notice is required to perfect a sale, are there any benefits to giving notice – such as cutting off obligor set-off rights and other obligor defences?

For the notification requirements for the perfection of the transfer, we refer you to the answer to question 4.2.

In general, the consent of the obligor is not required, unless otherwise provided in the underlying contract. With regards to the sale and transfer of receivables under the Securitisation Law in particular, the consent of the obligor is not required, even if it is expressly provided in the underlying contract as a prerequisite for the transferability of the claim. Notification (or registration in the case of securitisation transactions) also serves as a cut-off for the obligor to invoke against the assignee any rights and defences (including set-off) that it had against the assignor prior to such notification (or registration).

4.5 Notice Mechanics. If notice is to be delivered to obligors, whether at the time of sale or later, are there any requirements regarding the form the notice must take or how it must be delivered? Is there any time limit beyond which notice is ineffective – for example, can a notice of sale be delivered after the sale, and can notice be delivered after insolvency proceedings have commenced against the obligor or the seller? Does the notice apply only to specific receivables or can it apply to any and all (including future) receivables? Are there any other limitations or considerations?

Greek law does not require any particular form for the notice of assignment, provided that there is sufficient evidence that the notice has been received by the obligor. The method most commonly used is the service of the notice by court bailiff. There are special notification procedures with respect to assignments by way of security, in case the obligor is the state or a state-owned entity, or, in respect of the assignment of non-performing loans under Greek law 4354/2015, as amended and in force. With respect to transfers under the Securitisation Law, in particular, the registration is effected with the execution of a form containing the summary of the transfer and assignment agreement pursuant to the Securitisation Law and Decision of the Minister of Justice No. 161338/30.10.2003 and its registration with the competent pledge registry. No specific time limits for the notification are provided by law, subject always to the risks that may incur prior to the notification as per the answer to question 4.2 above.

4.6 Restrictions on Assignment – General Interpretation. Will a restriction in a receivables contract to the effect that "None of the [seller's] rights or obligations under this Agreement may be transferred or assigned without the consent of the [obligor]" be interpreted as prohibiting a transfer of receivables by the seller to the purchaser? Is the result the same if the restriction says "This Agreement may not be transferred or assigned by the [seller] without the consent of the [obligor]" (i.e., the restriction does not refer to rights or obligations)? Is the result the same if the restriction says "The obligations of the [seller] under this Agreement may not be transferred or assigned by the [seller] without the consent of the [obligor]" (i.e., the restriction does not refer to rights)?

As a general rule, the GCC recognises agreements limiting or restricting the assignability of claims. The presence of a contractual provision in a receivables contract stating that "[n]one of the [seller's] rights or obligations under this Agreement may be transferred or assigned without the consent of the [obligor]" may restrict the assignment of the relevant receivable and the consent of the other party would be required for the assignment and transfer of such receivable to the purchaser. However, if the agreement restricts the assignment of the agreement itself or the assignment of the obligations under this agreement only (in this case it is legally more precise to refer to an "assumption of debt"), it might be considered that such restriction refers to the assignment of the agreement and not the assignment of the receivables deriving thereunder. In any case, it is a matter of legal interpretation and Greek courts will focus on the contents of the entire agreement and seek to find the real intention of the parties.

As aforementioned, the transfer and assignment agreements under the Securitisation Law override any assignment restrictions found in receivables contracts.

4.7 Restrictions on Assignment; Liability to Obligor. If any of the restrictions in question 4.6 are binding, or if the receivables contract explicitly prohibits an assignment of receivables or "seller's rights" under the receivables contract, are such restrictions generally enforceable in your jurisdiction? Are there exceptions to this rule (e.g., for contracts between commercial entities)? If your jurisdiction recognises restrictions on sale or assignment of receivables and the seller nevertheless sells receivables to the purchaser, will either the seller or the purchaser be liable to the obligor for breach of contract or tort, or on any other basis?

Subject to the answers to question 4.6 above, contractual restrictions on transferability are recognised by Greek courts. The obligor may

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be entitled to damages mainly on the basis of a breach of the relevant contractual undertaking.

4.8 Identification. Must the sale document specifically identify each of the receivables to be sold? If so, what specific information is required (e.g., obligor name, invoice number, invoice date, payment date, etc.)? Do the receivables being sold have to share objective characteristics? Alternatively, if the seller sells *all* of its receivables to the purchaser, is this sufficient identification of receivables? Finally, if the seller sells *all* of its receivables *other than* receivables owing by one or more specifically identified obligors, is this sufficient identification of receivables?

The assigned claims should be defined or able to be defined. In this respect, they should be described in a clear and unambiguous manner, so as to clearly establish which are transferred to the purchaser and which remain with the seller and to avoid nullity of the transfer on the transferred receivables. The same applies to the identity of the obligor. In case the seller sells all of its receivables to the purchaser, other than receivables owing by one or more specifically identified obligors, the receivables are deemed to be sufficiently identified, to the extent that it may be deduced in a clear manner which receivables are transferred. It is noted that the form registered with the competent pledge registry pursuant to the Securitisation Law also includes a list of the transferred receivables with specific details such as loan ID (where applicable), name and address of obligors/guarantors, amount of the receivables, maturity date and securities.

4.9 Recharacterisation Risk. If the parties describe their transaction in the relevant documents as an outright sale and explicitly state their intention that it be treated as an outright sale, will this description and statement of intent automatically be respected or is there a risk that the transaction could be characterised by a court as a loan with (or without) security? If recharacterisation risk exists, what characteristics of the transaction might prevent the transfer from being treated as an outright sale? Among other things, to what extent may the seller retain any of the following without jeopardising treatment as an outright sale: (a) credit risk; (b) interest rate risk; (c) control of collections of receivables; (d) a right of repurchase/redemption; (e) a right to the residual profits within the purchaser; or (f) any other term?

Under Greek law, the legal relationship is characterised taking into account the overall terms agreed by the parties and not just the qualification given by the parties. In this respect, the Greek courts have the authority to examine the true legal nature of the transaction by analysing the agreement and its core elements.

The Securitisation Law requires that the sale of receivables is effected pursuant to the GCC provision on sale of goods and prohibits fiduciary transfers. In this respect, the Securitisation Law allows deferred purchase price mechanisms and provides that collection and servicing of the transferred claims may be effected by the seller in its capacity as servicer (which is common practice in Greece); alternatively, the servicing of the receivables portfolio may be assigned to a credit/financial institution of the EEA (that must have a permanent establishment in Greece, if the receivables are obligations of consumers, payable in Greece) or a third party which has either guaranteed or had undertaken collection of the receivables prior to the completion of the securitisation. Furthermore, repurchase by the seller of all or part of the securitised claims is allowed under the provisions of the Securitisation Law. All such provisions do not jeopardise *per se* the recharacterisation of the transaction.

4.10 Continuous Sales of Receivables. Can the seller agree in an enforceable manner to continuous sales of receivables (i.e., sales of receivables as and when they arise)? Would such an agreement survive and continue to transfer receivables to the purchaser following the seller's insolvency?

Subject to the relevant notification (or registration, as appropriate) formalities being met, continuous sales of receivables are possible, whether under sale and assignment pursuant to the general provisions of the GCC or pursuant to a securitisation transaction. Please also see our answer to question 4.7 above with regards to the identification of the receivables. Regarding transfer following the seller's insolvency, see our answer to question 4.11 below.

4.11 Future Receivables. Can the seller commit in an enforceable manner to sell receivables to the purchaser that come into existence after the date of the receivables purchase agreement (e.g., "future flow" securitisation)? If so, how must the sale of future receivables be structured to be valid and enforceable? Is there a distinction between future receivables that arise prior to *versus* after the seller's insolvency?

The response to question 4.10 applies accordingly with respect to the transfer of receivables coming into existence after the purchase agreement. As to what is the case for future receivables arising from a legal relationship prior to or post the seller's insolvency there are two prevailing theories regarding the perfection of the assignment. Pursuant to the first view, the assignment is concluded upon the execution of the relevant agreement. In this case, the bankruptcy of the assignor would have no impact on the assignment and the future claim, when it comes into existence, would not form part of its bankruptcy estate but it would belong to the assignee. Pursuant to the second view, the assignment is concluded upon the future claim coming into existence. In this case, if the assignor becomes insolvent prior to the future claim coming into existence, then such claim would not be finally transferred to the assignee and it will become part of its bankruptcy estate.

4.12 Related Security. Must any additional formalities be fulfilled in order for the related security to be transferred concurrently with the sale of receivables? If not all related security can be enforceably transferred, what methods are customarily adopted to provide the purchaser the benefits of such related security?

The formalities required for the creation of a security must be repeated to perfect their transfer (i.e. (a) registration of the change of the beneficiary of a mortgage/prenotation of mortgage with the competent land registry, (b) endorsement of marketable instruments, (c) court bailiff service of a pledge over receivables, or (d) registration of floating charge/equipment pledge). In securitisation transactions, security interests that are ancillary to the transferred claim are co-transferred to the purchaser upon registration of the transaction with the competent pledge registry, whereas in case of securities *in rem* the change of the beneficiary in the public books is effected by registering the certificate of registration of the securitisation transaction issued by the competent pledge registry (see also the answer to question 5.5 below).

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4.13 Set-Off; Liability to Obligor. Assuming that a receivables contract does not contain a provision whereby the obligor waives its right to set-off against amounts it owes to the seller, do the obligor's set-off rights terminate upon its receipt of notice of a sale? At any other time? If a receivables contract does not waive set-off but the obligor's set-off rights are terminated due to notice or some other action, will either the seller or the purchaser be liable to the obligor for damages caused by such termination?

An obligor may set off its claims against the seller against the obligor's obligations towards the purchaser, following transfer of the receivables to the purchaser, provided that the legal basis of the obligors' claims against the seller existed at the time of notification (or registration in case of securitisation transactions) of the sale and transfer agreement; and provided that the obligors' claims against the seller become due and payable not later than the time when the claims arising from the receivables become due and payable.

4.14 Profit Extraction. What methods are typically used in your jurisdiction to extract residual profits from the purchaser?

Common methods for profit extraction, especially in securitisation transactions, are deferred price mechanisms and payment of special servicing fees (when the seller and the servicer are the same entity). Additionally, profit extraction mechanism may take the form of issuance of residual notes subscribed by the seller for a nominal amount and giving right to the excess cash available.

5 Security Issues

5.1 Back-up Security. Is it customary in your jurisdiction to take a "back-up" security interest over the seller's ownership interest in the receivables and the related security, in the event that an outright sale is deemed by a court (for whatever reason) not to have occurred and have been perfected (see question 4.9 above)?

No, this is not customary.

5.2 Seller Security. If it is customary to take back-up security, what are the formalities for the seller granting a security interest in receivables and related security under the laws of your jurisdiction, and for such security interest to be perfected?

This is not applicable in Greece.

5.3 Purchaser Security. If the purchaser grants security over all of its assets (including purchased receivables) in favour of the providers of its funding, what formalities must the purchaser comply with in your jurisdiction to grant and perfect a security interest in purchased receivables governed by the laws of your jurisdiction and the related security?

In general, the security that is established upon claims under Greek law takes the form of a pledge. The establishment of such a pledge requires different formalities depending on the legal framework selected. Generally, pledge under the GCC requires conclusion of a pledge agreement in written form and notification of the establishment of the pledge to the pledgor's debtors. If Legislative Decree 17.7/13.8.1923 on special provisions pertaining to Greek *societes anonymes*, which applies *ipso iure* to banks established in Greece or operating (through a branch) in Greece as pledgees, is opted for, service of a copy of the pledge agreement to the underlying debtors by a court bailiff is required. Registered pledge according to Greek Law 2844/2000 with regard to business claims requires registration of the pledge to the competent pledge registry. Finally, Greek Law 3301/2004 on financial collateral arrangements, to the extent that its provisions are applicable, requires a written pledge agreement and a list of credit claims notified to the collateral taker.

As regards securitisation transactions, the Securitisation Law provides for a pledge by operation of law in favour of the noteholders and the other beneficiaries, which is established over the transferred receivables and collection account maintained by the servicer automatically upon the registration of the receivables assignment and transfer agreement in the public registry book of article 3 of Law 2844/2000 (see above in question 4.2). In respect of pledges established under the Securitisation Law, registration in the public registry book is deemed a notification to the underlying debtors and no individual notifications are required.

5.4 Recognition. If the purchaser grants a security interest in receivables governed by the laws of your jurisdiction, and that security interest is valid and perfected under the laws of the purchaser's jurisdiction, will the security be treated as valid and perfected in your jurisdiction or must additional steps be taken in your jurisdiction?

The perfection requirements under Greek law need to be followed.

5.5 Additional Formalities. What additional or different requirements apply to security interests in or connected to insurance policies, promissory notes, mortgage loans, consumer loans or marketable debt securities?

With regard to formalities for the pledge of claims, please refer to question 5.3. As regards financial instruments pursuant to article 1244 GCC, for pledges over financial instruments in bearer form ("*anonyma*") (a) an agreement between the pledgee and the pledgor in the form of either a notarial deed or a private agreement bearing a certified ("certain") date, and (b) physical delivery of the eligible collateral to the creditor (pledgee) are required.

A pledge over registered ("*onomastika*") instruments is regulated by the provisions on pledge over rights; namely for the creation of the pledge the following are required: (a) an agreement between the pledgee and the pledgor in the form of either a notarial deed or a private agreement bearing a certified ("certain") date; (b) physical delivery of the eligible collateral to the creditor (pledgee); and (c) notification of the pledge to the debtor to the extent that the instrument incorporates a claim. In the case of registered ("*onomastikes*") shares, endorsement and registration of the pledge in the shareholders' book is additionally required pursuant to article 8b of Codified Law 2190/1920.

As regards the Securitisation Law, any collateral rights are co-transferred to the purchaser together with the receivables. If the receivable is secured through a mortgage or a pre-notice of mortgage or a pledge or other ancillary right or lien, which has been made public by way of its registration with a public registry or record book, in order that the purchaser be able to enforce such security, a certificate by the competent pledge registry confirming registration of a summary of the receivables transfer agreement, and a summary description of the particular security, must be submitted to the

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pledge registry where the security was initially registered in order for the registrar to enter a note on such pledge registry's records for the change of beneficiary (see question 4.12).

5.6 Trusts. Does your jurisdiction recognise trusts? If not, is there a mechanism whereby collections received by the seller in respect of sold receivables can be held or be deemed to be held separate and apart from the seller's own assets (so that they are not part of the seller's insolvency estate) until turned over to the purchaser?

Trust is not recognised by the Greek legal system. The mechanism of segregation of collections out of transferred receivables is achieved through a contractual arrangement with the servicer. According to the Securitisation Law, the servicer is obliged, immediately upon collection, to deposit the proceeds of the securitised receivables in a separate interest bearing account kept with it if the servicer is a credit institution, or otherwise with a credit institution operating in the European Economic Area. Such a deposit must be accompanied with a special note that this constitutes an account separate from the servicer's personal assets and that of the financial institution's where the deposit is made. In addition, a pledge operated by law is automatically established upon such deposit for the benefit of the noteholders. Any such pledge as well as the funds that are collected by the servicer are excluded from foreclosure, set-off or any other attachment whatsoever by the latter or his creditors, nor are they included in the bankruptcy estate of the servicer.

5.7 Bank Accounts. Does your jurisdiction recognise escrow accounts? Can security be taken over a bank account located in your jurisdiction? If so, what is the typical method? Would courts in your jurisdiction recognise a foreign law grant of security (for example, an English law debenture) taken over a bank account located in your jurisdiction?

Escrow accounts can be put in place on the basis of contractual arrangements without an *erga omnes* effect. The lien available under Greek law for bank accounts which are governed by Greek law is a pledge over claims which have an *erga omnes* effect. There is no requirement to specify a maximum secured amount. Pledges of this type are expressed to secure all obligations under a specific relation. The only perfection requirement for pledges over claims is the notification of the underlying debtor, i.e. the account bank (see above in question 5.3).

According to international private law rules and article 14 of the Rome I Regulation, the governing law of the pledge is the governing law of the pledged claim. Thus, a Greek law account pledge assumes that the bank account agreement is governed by Greek law. Foreign law can be agreed to govern a bank account by a Greek bank in which case a foreign law lien would be established over the bank account. Pledges are established by operation of law on the collection account maintained in the name of the servicer (see above in question 5.3).

5.8 Enforcement over Bank Accounts. If security over a bank account is possible and the secured party enforces that security, does the secured party control all cash flowing into the bank account from enforcement forward until the secured party is repaid in full, or are there limitations? If there are limitations, what are they?

A pledge over a bank account entitles the pledgee to satisfy its claim by the proceeds of the pledged bank account upon the secured claim becoming due and payable without being obliged first to acquire the pledgor's consent or a court judgment or order. In effect, upon the occurrence of a default under the transaction documents which gives rise to acceleration, the pledgee shall be entitled, without any further consent or authority from the pledgor, to require the account bank to effect payment of all monies due by it in connection with the bank account directly to the pledgee. According to Greek law, there are several claims that enjoy general privileges such as state and municipality claims, social security contributions, and employee's claims. Claims secured with a pledge enjoy a special privilege, though the following limitations apply in case of a concurrence of general and special privileges and non-privileged claims:

- the percentage of satisfaction of creditors with general privileges from enforcement proceeds is limited to twenty-five per cent (25%);
- the percentage of satisfaction of creditors with special privileges is limited to sixty-five per cent (65%); and
- the remaining ten percent (10%) of the distribution price of the auction is reserved for non-privileged creditors.

According to a recent law amendment, creditors with special privileges (i.e. pledge or mortgage) are ranked before creditors with general privileges and unsecured creditors after the satisfaction of the claims of unpaid employees up to an amount prescribed by law are satisfied. However, the above apply only to claims arising after the entry into force of Law 4512/2018 and if a pledge or mortgage is registered on an asset which is unencumbered.

As regards pledges established by virtue of Legislative Decree 17.7/13.8.1923 (see above in question 5.3), pledges over a bank account are equivalent to assignment of claims to the effect that the claim is entirely alienated from the pledgor and the above risk of satisfaction from the priority of holders of general liens does not exist.

5.9 Use of Cash Bank Accounts. If security over a bank account is possible, can the owner of the account have access to the funds in the account prior to enforcement without affecting the security?

This is feasible subject to the contractual provisions of the pledge agreement.

6 Insolvency Laws

6.1 Stay of Action. If, after a sale of receivables that is otherwise perfected, the seller becomes subject to an insolvency proceeding, will your jurisdiction's insolvency laws automatically prohibit the purchaser from collecting, transferring or otherwise exercising ownership rights over the purchased receivables (a "stay of action")? If so, what generally is the length of that stay of action? Does the insolvency official have the ability to stay collection and enforcement actions until he determines that the sale is perfected? Would the answer be different if the purchaser is deemed to only be a secured party rather than the owner of the receivables?

As a general matter, there is no stay of action after the opening of insolvency procedures. However, in case of assignment of receivables outside a securitisation transaction and the ambit of the Securitisation Law, any transfer of receivables is subject to clawback if effected during the suspect period (see question 6.3).

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As regards the transfer of receivables in a securitisation transaction as of the moment of the registration, the validity of the sale and transfer is not affected by the imposition of any collective creditors measure that could result in the prohibition or restriction of the transferor's right to dispose of its assets.

6.2 Insolvency Official's Powers. If there is no stay of action, under what circumstances, if any, does the insolvency official have the power to prohibit the purchaser's exercise of its ownership rights over the receivables (by means of injunction, stay order or other action)?

To the extent that the transfer is perfected properly and the transfer is a true sale and not subject to the restrictions of the suspect period, there is no such possibility.

6.3 Suspect Period (Clawback). Under what facts or circumstances could the insolvency official rescind or reverse transactions that took place during a "suspect" or "preference" period before the commencement of the seller's insolvency proceedings? What are the lengths of the "suspect" or "preference" periods in your jurisdiction for (a) transactions between unrelated parties, and (b) transactions between related parties? If the purchaser is majority-owned or controlled by the seller or an affiliate of the seller, does that render sales by the seller to the purchaser "related party transactions" for purposes of determining the length of the suspect period? If a parent company of the seller guarantee's the performance by the seller of its obligations under contracts with the purchaser, does that render sales by the seller to the purchaser "related party transactions" for purposes of determining the length of the suspect period?

Any acts of the debtor effected from the cease of payments up to declaration of bankruptcy – a maximum of two years prior to the declaration of bankruptcy (the so-called "suspect period") – which are detrimental for the creditors, are revoked or are revocable. The Bankruptcy Code makes the following distinctions:

- acts that are mandatorily revoked (endowments and agreements in which the consideration owed by the debtor is disproportional to the benefit thereof, establishment of *in rem* security for securing pre-existing unsecured claims, payment of obligations which have not fallen due); and
- acts which may be optionally revoked (any agreement or payment of an obligation of the debtor to a party which was aware of the cease of payment of the debtor and such act or payment is detrimental to the creditors).

Certain acts are exempted, in particular those performed in the ordinary course of business and those exempted from the insolvency annulment by special laws (e.g. the netting of claims under securities settlement system, transactions related to derivatives, agreements for establishing financial collateral). In addition, such judicial review for the revocation of acts of the debtor can go back five years from the declaration of bankruptcy if the debtor acted fraudulently, aiming at the detriment of its creditors or at favouring some creditors, to the extent that the counterparty was aware of the debtor's fraud. Knowledge of the cease of payment of the debtor and detrimental character of the payment are presumed in case of related parties. Please refer to question 6.1 as regards the ring-fencing achieved in securitisation transactions.

6.4 Substantive Consolidation. Under what facts or circumstances, if any, could the insolvency official consolidate the assets and liabilities of the purchaser with those of the seller or its affiliates in the insolvency proceeding? If the purchaser is owned by the seller or by an affiliate of the seller, does that affect the consolidation analysis?

There are no such provisions under Greek law.

6.5 Effect of Insolvency on Receivables Sales. If insolvency proceedings are commenced against the seller in your jurisdiction, what effect do those proceedings have on (a) sales of receivables that would otherwise occur after the commencement of such proceedings, or (b) on sales of receivables that only come into existence after the commencement of such proceedings?

See question 6.1.

6.6 Effect of Limited Recourse Provisions. If a debtor's contract contains a limited recourse provision (see question 7.3 below), can the debtor nevertheless be declared insolvent on the grounds that it cannot pay its debts as they become due?

A borrower should mandatorily file a petition for declaration into bankruptcy if it is unable in a permanent and generic way to meet its monetary debts which have fallen due and payable. A petition may also be filed to the court by any creditor who has a legitimate interest or the competent district attorney. If there is a limited recourse provision, relevant payment obligations will not become due and thus cannot cause the debtor to become illiquid. However, this would not be the case if a mere subordination has been agreed. In addition, if the debtor cannot meet other obligations which are not subject to limited recourse provisions in a generic manner, bankruptcy is still possible.

7 Special Rules

7.1 Securitisation Law. Is there a special securitisation law (and/or special provisions in other laws) in your jurisdiction establishing a legal framework for securitisation transactions? If so, what are the basics? Is there a regulatory authority responsible for regulating securitisation transactions in your jurisdiction?

The Securitisation Law is the special securitisation law in place. "Securitisation" is defined by said law as a transfer of business claims of contractual or non-contractual nature by way of sale, by means of a written agreement between a party (the transferor) and another party (the transferee) in combination with the issue and offer, by private placement only, of any kind of bonds, the repayment of which is funded by (a) the proceeds of the transferred business claims, or (b) loans, credits or financial derivative agreements. The transferor must be a commercial person resident or having a permanent establishment in Greece. The transferee must be an entity established solely for the purpose of acquiring the business claims and must be the issuer of the bonds. Securitisation is a useful tool for transfer of claims since it provides for some tax benefits and protective provisions for the holders of the bonds. Law 3156/2003 also covers real estate claims. Law 2801/2000 governs

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securitisation of state receivables. There is no regulatory authority responsible for securitisation transactions in Greece. The Bank of Greece supervises and regulates the capital adequacy requirements when the originator is a bank.

7.2 Securitisation Entities. Does your jurisdiction have laws specifically providing for establishment of special purpose entities for securitisation? If so, what does the law provide as to: (a) requirements for establishment and management of such an entity; (b) legal attributes and benefits of the entity; and (c) any specific requirements as to the status of directors or shareholders?

If the Special Purpose Vehicle is established in Greece, it should have the form of company limited by shares (*société anonyme*) and be subject to the laws governing this corporate form. According to Greek law, a *société anonyme* cannot be an orphan vehicle.

Although, according to general law, *sociétés anonyme*s should always have own funds higher than the 1/10 of the share capital, otherwise their licence may be revoked, SPVs are exempted from such requirement. The management of *sociétés anonymes* is entrusted to the Board of Directors and any specifically appointed officers, whereas the general meeting of shareholders is the supreme body of the corporation. The directors owe a fiduciary duty towards the company.

7.3 Location and form of Securitisation Entities. Is it typical to establish the special purpose entity in your jurisdiction or offshore? If in your jurisdiction, what are the advantages to locating the special purpose entity in your jurisdiction? If offshore, where are special purpose entities typically located for securitisations in your jurisdiction? What are the forms that the special purpose entity would normally take in your jurisdiction and how would such entity usually be owned?

Usually in securitisation transactions in Greece, SPVs are structured offshore (typically in the UK due to the favourable double taxation avoidance treaties ensuring that payments from debtors to the SPV can be made free of withholding tax). There are no adverse implications in case an SPV is located abroad, especially in view of par. 13 of Article 14 of the Securitisation Law, according to which all provisions of such law, save the provision for the applicable laws for the establishment and operation of SPV if it is located in Greece, also apply to foreign SPVs. Although Greek SPVs cannot follow the orphan structure, no requirement is set by the Securitisation Law in respect of the shareholding of the SPV, apart from the form of the shares, which are mandatorily registered.

7.4 Limited-Recourse Clause. Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) limiting the recourse of parties to that agreement to the available assets of the relevant debtor, and providing that to the extent of any shortfall the debt of the relevant debtor is extinguished?

As a general matter, this clause would give effect to this agreement under Greek law subject to the limitations mentioned under question 5.8 and to the extent that it does not contain a limitation of liability arising from grossly negligent (*vareia ameleia*) or fraudulent/wilful conduct (*dolos*). For consumer contracts, stricter rules apply with regard to limitation of liability and exclusion from slight negligence is not feasible. Such laws form part of Greece's public policy and, as such, the validity of provisions in an agreement governed by foreign law in violation of such laws could be challenged before Greek courts.

7.5 Non-Petition Clause. Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) prohibiting the parties from: (a) taking legal action against the purchaser or another person; or (b) commencing an insolvency proceeding against the purchaser or another person?

A Greek court would give effect to a non-petition clause only to the extent that it would give rise to a claim for compensation for any damage incurred by the non-defaulting party. However, any filing of bankruptcy by the defaulting party would not be deemed as invalid by the court.

7.6 Priority of Payments "Waterfall". Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) distributing payments to parties in a certain order specified in the contract?

Please refer to questions 2.2 and 2.3 above. Within the context of enforcement proceedings, the enforceability of such provisions relating to the application of proceeds will be subject to any obligations mandatorily preferred by Greek law. This will be the case even if that agreement's governing law is the law of another country, since these provisions of Greek law constitute public order rules.

7.7 Independent Director. Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) or a provision in a party's organisational documents prohibiting the directors from taking specified actions (including commencing an insolvency proceeding) without the affirmative vote of an independent director?

The members of the Board of Directors of a *société anonyme* owe a fiduciary duty towards the company and, given the relevant liability and the mandatory character of such provisions of law, a contractual arrangement according to which the members of the Board of Directors of a *société anonyme* are prohibited from taking certain actions to the detriment of the corporate interest would be deemed void even if that agreement's governing law is the law of another country. With regard to commencement of insolvency proceedings, kindly note that any failure of the Board of Directors to commence relevant proceedings, where relevant requirements are fulfilled, entails penal and civil liability for its members.

7.8 Location of Purchaser. Is it typical to establish the purchaser in your jurisdiction or offshore? If in your jurisdiction, what are the advantages to locating the purchaser in your jurisdiction? If offshore, where are purchasers typically located for securitisations in your jurisdiction?

See question 7.3. The purchaser is not typically established in Greece. This is the case mainly for banking securitisations because, according to Greek law, the SPV cannot be conceived as an orphan entity whereas, again according to Greek law, a global note held by

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the common depository system is not conceivable. Bonds held by each bondholder depending on the subscription participation of each of them should be issued.

8 Regulatory Issues

8.1 Required Authorisations, etc. Assuming that the purchaser does no other business in your jurisdiction, will its purchase and ownership or its collection and enforcement of receivables result in its being required to qualify to do business or to obtain any licence or its being subject to regulation as a financial institution in your jurisdiction? Does the answer to the preceding question change if the purchaser does business with more than one seller in your jurisdiction?

There is no such requirement.

8.2 Servicing. Does the seller require any licences, etc., in order to continue to enforce and collect receivables following their sale to the purchaser, including to appear before a court? Does a third-party replacement servicer require any licences, etc., in order to enforce and collect sold receivables?

According to the Securitisation Law, the entity which carries out servicing duties should be a financial or credit institution licensed to offer such services, in accordance with its scope of business, within the European Economic Area. A servicer or third party may act as the transferor, provided the latter acts as the guarantor of the transferred receivables or has been entrusted with the management or collection of the receivables prior to their transfer to the transferee. If the special purpose company does not have its place of business in Greece and the receivables under transfer are receivables against consumers payable in Greece, the parties whom the management has been assigned to must have an establishment in Greece. So, no licence is required for the seller to continue to enforce and collect receivables as the seller.

Appearance in court generally requires the attendance of a lawyer. For the purpose of supporting the appointment of a servicer with regards to certain actions by the servicer that require formal delegation of powers by the SPV (mainly of a judicial nature such as representation before the courts, out-of-court settlements, etc.), it is common that the SPV issues a general power of attorney to the servicer in the form of a notarial act (via the Apostille of the Hague Convention of 1961, if the SPV is foreign) authorising it to manage the affairs deriving from the transfer of the receivables and the service agreement that would otherwise be within the competence of the SPV.

As regards the replacement servicer, it should fulfil the above requirements.

8.3 Data Protection. Does your jurisdiction have laws restricting the use or dissemination of data about or provided by obligors? If so, do these laws apply only to consumer obligors or also to enterprises?

There are data protection restrictions in Greece in line with relevant European legislation. Par. 21 of Article 10 of the Securitisation Law provides that, to the extent required for the purposes of the securitisation transaction, the processing of personal data of the debtors does not require the prior written consent of the latter, nor the prior approval of the Data Protection Authority.

In any case, par. 21 of Article 10 of the Securitisation Law does not exclude the originator and/or the servicer and/or the SPV from abiding with the rest of the provisions of data protection legislation, which include, *inter alia*, the notification to the Data Protection Authority of the establishment and operation of a personal data record or the commencement of their processing. Data protection laws also apply to enterprises with regard to personal data of individuals (e.g. personal data of shareholders or directors).

8.4 Consumer Protection. If the obligors are consumers, will the purchaser (including a bank acting as purchaser) be required to comply with any consumer protection law of your jurisdiction? Briefly, what is required?

Consumer protection that is applicable to purchasers can be summarised as follows:

- Terms and conditions of loans that create an unbalance between rights and obligations of the parties to the detriment of the consumers are deemed as abusive and are null and void. Indicative enumeration of abusive terms and conditions are set forth in Greek Law 2251/1994 (Consumer Protection Law) and relevant legislation and have been ruled as such by relevant court precedents. For example, any term of the loan, which grants to the bank the right of unilateral amendment of the interest rate in a loan agreement without objective criteria justifiable by the market conditions, has been found as invalid (see also question 1.2 (d) above).
- The Act of Bank of Greece Governor 2501/2002 introduces minimum information to be provided by the credit institutions to borrowers prior to the conclusion of the loan, including, *inter alia*, the level of the fixed interest rate and any spread thereof, interest periods, special contributions, taxes, duties and other expenses, in the cases of loan agreements with a floating interest rate, the general reference rate as well as default interest should be disclosed. Same legislation imposes on credit institutions the obligation of reporting periodic information of the borrowers and the establishment of a procedure for examination and resolution of complaints.

The above laws also apply to purchasers.

8.5 Currency Restrictions. Does your jurisdiction have laws restricting the exchange of your jurisdiction's currency for other currencies or the making of payments in your jurisdiction's currency to persons outside the country?

Generally, there are no such restrictions. Greek courts are obliged to render judgments in respect of claims in foreign currency in such foreign currency but payment thereof will be made in euro at the exchange rate prevailing on the date of such payment, such rate being published in the daily foreign exchange bulletin of the Bank of Greece. Money transfers outside the country are subject to capital control restrictions. However, as regards payments made in the context of securitisation, credit institutions operating in Greece are exempted from such restrictions. Banking institutions are subject to reporting to the Bank of Greece regarding fund transfer for the purposes of avoidance of money laundering.

8.6 Risk Retention. Does your jurisdiction have laws or regulations relating to "risk retention"? How are securitisation transactions in your jurisdiction usually structured to satisfy those risk retention requirements?

Greece follows the risk retention requirements found in the relevant European legislation. In this respect, in the very few securitisation transactions completed in the recent years under Regulation (EU)

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575/2013 (Capital Requirements Regulation – **CRR**) that we are aware of, the originators undertook for the purposes of the CRR, Regulation (EU) No 231/2013 (the Alternative Investments Fund Manager Regulation – **AIFM**) and Regulation (EU) 2015/35 (Solvency II Regulation) to retain a material net economic interest of not less than 5% in the securitisation (representing downside risk and economic outlay). Such retention is comprised of the purchase and holding of an interest in the first loss tranche which was equal to at least 5% of the nominal value of the securitised exposures as at the closing of the transaction. Greece is expected to follow the new securitisation regime (and, accordingly, the new rules on risk retention, due diligence and disclosure) of Regulation (EU) 2017/2402 (the STS Regulation) and Regulation (EU) 2017/2401 (the Securitisation Prudential Regulation, or SPR) that will be effective as of 1 January 2019.

8.7 Regulatory Developments. Have there been any regulatory developments in your jurisdiction which are likely to have a material impact on securitisation transactions in your jurisdiction?

Through recent reforms, many impediments which could hinder the enforcement of monetary claims have been eased. These include the reform of the Civil Procedure Code to expedite enforcement proceedings and the reform of Bankruptcy Code. In the same context, Greek Law 4354/2015 (NPL Law), as in force, established a regulatory framework for servicing and transferring NPLs, to the effect that transfer of NPLs in Greece can now be effected under two different legal regimes, namely securitisation under the Securitisation Law and transfer by virtue of the NPL Law.

9 Taxation

9.1 Withholding Taxes. Will any part of payments on receivables by the obligors to the seller or the purchaser be subject to withholding taxes in your jurisdiction? Does the answer depend on the nature of the receivables, whether they bear interest, their term to maturity, or where the seller or the purchaser is located? In the case of a sale of trade receivables at a discount, is there a risk that the discount will be recharacterised in whole or in part as interest? In the case of a sale of trade receivables where a portion of the purchase price is payable upon collection of the receivable, is there a risk that the deferred purchase price will be recharacterised in whole or in part as interest? If withholding taxes might apply, what are the typical methods for eliminating or reducing withholding taxes?

It depends on the kind of receivables, the location of the issuer and the underlying obligors. As a general matter, interest income generated by loan receivables will be considered as income arising from commercial operations and would, *prima facie*, be taxable under Greek law. However, under the terms of a bilateral treaty for the avoidance of double taxation between Greece and the place of establishment of the issuer, the latter will not be subject to tax in Greece in respect of this interest income.

Deferred purchase price and discount are not considered as interest. Generally, as for tax status, deferred purchase price received by the originator is not differentiated from the initial price and therefore, to the extent that profit is made from the transfer of the receivables, such profit is exempted from the income tax according to par. 6 of Article 14 of the Securitisation Law, provided that such profit appears in a special tax free reserve account, which if distributed or capitalised will be subject to tax in accordance with general tax law (par. 9 of Article 14). However, the tax authorities have the discretion to recharacterise a tax status.

9.2 Seller Tax Accounting. Does your jurisdiction require that a specific accounting policy is adopted for tax purposes by the seller or purchaser in the context of a securitisation?

The IAS/IFRS are obligatory in Greece for banks, listed companies and companies issuing debt instruments in public. For such entities, there is a requirement for consolidation of the SPV. Bank of Greece has issued regulations transposing European legislation outlining, broadly speaking, the off-balance-sheet of the securitisation positions of banks in accordance with the Securitisation Law.

9.3 Stamp Duty, etc. Does your jurisdiction impose stamp duty or other transfer or documentary taxes on sales of receivables?

Generally speaking, sale of receivables outside the ambit of the Securitisation Law may entail stamp duty. However, any transfer of receivables under the Securitisation Law is exempted from any direct or indirect tax, including stamp duty.

9.4 Value Added Taxes. Does your jurisdiction impose value added tax, sales tax or other similar taxes on sales of goods or services, on sales of receivables or on fees for collection agent services?

The sale of receivables within the context of the Securitisation Law are exempted from VAT. The Servicing Agreement will be exempted from VAT only if the originator acts as the servicer. If any other entity acts as the servicer, VAT will be applicable.

9.5 Purchaser Liability. If the seller is required to pay value-added tax, stamp duty or other taxes upon the sale of receivables (or on the sale of goods or services that give rise to the receivables) and the seller does not pay, then will the taxing authority be able to make claims for the unpaid tax against the purchaser or against the sold receivables or collections?

In the context of securitisation transactions, there are no joint tax liabilities between the seller and purchaser. However, the seller and the purchaser are jointly liable to pay to Bank of Greece all monies they collect under the securitised receivables that correspond to the levy of Greek Law 128/1975. This levy is imposed on the interest which is passed by the banks to the obligors of the loans as an add-on to the interest.

9.6 Doing Business. Assuming that the purchaser conducts no other business in your jurisdiction, would the purchaser's purchase of the receivables, its appointment of the seller as its servicer and collection agent, or its enforcement of the receivables against the obligors, make it liable to tax in your jurisdiction?

Ownership of the receivables does not of itself amount or give rise to establishment as a purchaser in Greece. Similarly, the authorisations given by the purchaser to the servicer under the Servicing Agreement do not constitute an authorisation such as the one referred to by relevant legislation for the existence of a

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permanent establishment in Greece. Accordingly, the income of the purchaser in respect of the receivables will not be subject to taxation (including withholding tax) in Greece.

9.7 Taxable Income. If a purchaser located in your jurisdiction receives debt relief as the result of a limited recourse clause (see question 7.3 above), is that debt relief liable to tax in your jurisdiction?

A case-by-case analysis should be performed. In general, debt relief could be recognised as taxable profit. In addition, debt relief bears stamp duty.

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They are known for international, high-profile, pioneering (mostly first of its kind in Greece) and sophisticated financial legal work, having acted for some of the world's leading investment and commercial banks.

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Hong Kong

King & Wood Mallesons

Paul McBride

Darwin Goei

1 Receivables Contracts

1.1 Formalities. In order to create an enforceable debt obligation of the obligor to the seller: (a) is it necessary that the sales of goods or services are evidenced by a formal receivables contract; (b) are invoices alone sufficient; and (c) can a binding contract arise as a result of the behaviour of the parties?

Other than with respect to certain types of contracts (and provided that the common law requirements of contract formation, such as offer, acceptance, consideration, legal formalities and capacity are met), there is no general requirement under Hong Kong law that a sale of goods or services be evidenced by a formal contract (assuming "formal" means an agreement be in writing or evidenced in writing). As such, it is possible for a contract to arise solely from the behaviour of the seller and obligor in the absence of a written contract to the contrary.

An invoice, depending on the detail and nature of its terms, may be sufficient to evidence a contract between the obligor and the seller. In particular, an invoice may incorporate, by way of reference, the seller's standard terms and conditions. Furthermore, a court in Hong Kong may also imply further terms by examining the course of previous dealings between the obligor and the seller or imply terms which may arise by custom or trade usage within a particular industry.

1.2 Consumer Protections. Do your jurisdiction's laws: (a) limit rates of interest on consumer credit, loans or other kinds of receivables; (b) provide a statutory right to interest on late payments; (c) permit consumers to cancel receivables for a specified period of time; or (d) provide other noteworthy rights to consumers with respect to receivables owing by them?

Yes, there are Hong Kong laws that may limit the applicable rates of interest. The Money Lenders Ordinance (Cap. 163) operates to limit rates of interest in certain circumstances. In particular, any loan agreement that contains a provision requiring the payment of interest where:

(a) the rate of interest exceeds 48% – is deemed to be extortionate and the terms of such an agreement are susceptible to amendment by a Hong Kong court; or

(b) the rate of interest exceeds 60% – is rendered unenforceable (together with any security provided to support such loan) and is a criminal offence with a maximum penalty of HK$5million and 10 years' imprisonment.

In this context, the Money Lenders Ordinance does not apply to "authorized institutions" as lenders as defined in the Banking Ordinance (Cap. 155), nor does it apply to loans made to a company with paid-up share capital of at least HK$1million.

A provision in a contract which provides for the payment of an additional sum of money upon breach of the contract may amount to a penalty and be unenforceable under Hong Kong law if the sum stipulated to be paid for such a breach is not a genuine pre-estimate of the greatest conceivable loss likely to be suffered by the non-defaulting party.

There is no general consumer protection legislation in Hong Kong. However, there are specific regulations which are relevant in certain industries, such as insurance and structured products. In addition to the Money Lenders Ordinance, there are also several ordinances of general application which may provide rights to consumers, such as the Sale of Goods Ordinance (Cap. 26), the Control of Exemption Clauses Ordinance (Cap. 71), Supply of Services (Implied Terms) Ordinance (Cap. 457) and the Unconscionable Contracts Ordinance (Cap. 458). Please see the response to question 8.4 below for further details.

1.3 Government Receivables. Where the receivables contract has been entered into with the government or a government agency, are there different requirements and laws that apply to the sale or collection of those receivables?

Contracts entered into by the government or a governmental body are governed by ordinary principles of Hong Kong law, subject to, in the case of a governmental body, any limitations that may be set out in the statutory instrument that establishes such body.

Neither sovereign immunity nor crown immunity applies to the Hong Kong government and its entities. The Hong Kong government has effectively waived its immunity from legal proceedings under the Crown Proceedings Ordinance (Cap. 300).

However, care must be taken to distinguish contractual arrangements with the Hong Kong government and contractual arrangements with the mainland government of the People's Republic of China. The *Hua Tian Long (No. 3)* [2010] 3 HKC 557 decision confirmed

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that the mainland government of the PRC is entitled in certain circumstances to exercise crown immunity before the Hong Kong courts unless waived. The essential test is whether the counterparty can be considered an instrumentality of the PRC government or any of its ministries and regional counterparts. Other factors include whether: (a) the board of directors are able to exercise independent discretion; (b) the entity is managed and/or established by a PRC state or government entity; (c) whether it has statutory powers conferred upon it or carried out the functions of a PRC state or government entity; and (d) whether it is required to seek approval for its day-to-day or commercial operations by any PRC state or governmental entity.

The Hong Kong Court of Final Appeal in the *Congo* [2011] HKCFA 41 decision followed the Hua Tian Long decision to hold that absolute sovereign immunity applies in Hong Kong.

2 Choice of Law – Receivables Contracts

2.1 No Law Specified. If the seller and the obligor do not specify a choice of law in their receivables contract, what are the main principles in your jurisdiction that will determine the governing law of the contract?

In the absence of a choice of law provision (express or implied), the courts of Hong Kong would look to the jurisdiction which has the most real and substantial connection to the dispute.

2.2 Base Case. If the seller and the obligor are both resident in your jurisdiction, and the transactions giving rise to the receivables and the payment of the receivables take place in your jurisdiction, and the seller and the obligor choose the law of your jurisdiction to govern the receivables contract, is there any reason why a court in your jurisdiction would not give effect to their choice of law?

There is no reason.

2.3 Freedom to Choose Foreign Law of Non-Resident Seller or Obligor. If the seller is resident in your jurisdiction but the obligor is not, or if the obligor is resident in your jurisdiction but the seller is not, and the seller and the obligor choose the foreign law of the obligor/seller to govern their receivables contract, will a court in your jurisdiction give effect to the choice of foreign law? Are there any limitations to the recognition of foreign law (such as public policy or mandatory principles of law) that would typically apply in commercial relationships such as that between the seller and the obligor under the receivables contract?

Hong Kong courts will generally give effect to the choice of foreign law, provided that such choice has been made *bona fide* and is not against public policy.

Notwithstanding the valid choice of a foreign law to govern the receivables contract, Hong Kong mandatory laws may nevertheless apply to certain aspects of any agreement between the obligor and the seller. For example, transfers of an interest in land would be governed by Hong Kong law, irrespective of the otherwise valid choice of a foreign law to govern the contract.

3 Choice of Law – Receivables Purchase Agreement

3.1 Base Case. Does your jurisdiction's law generally require the sale of receivables to be governed by the same law as the law governing the receivables themselves? If so, does that general rule apply irrespective of which law governs the receivables (i.e., your jurisdiction's laws or foreign laws)?

No, Hong Kong law does not require the sale of the receivables to be governed by the same governing law as the receivables themselves.

However, if the receivables contract is governed by Hong Kong law, the assignment of the receivables would be subject to perfection requirements as established under Hong Kong law. This is in addition to the issues set out above in the response to question 2.3 (i.e. Hong Kong mandatory laws).

3.2 Example 1: If (a) the seller and the obligor are located in your jurisdiction, (b) the receivable is governed by the law of your jurisdiction, (c) the seller sells the receivable to a purchaser located in a third country, (d) the seller and the purchaser choose the law of your jurisdiction to govern the receivables purchase agreement, and (e) the sale complies with the requirements of your jurisdiction, will a court in your jurisdiction recognise that sale as being effective against the seller, the obligor and other third parties (such as creditors or insolvency administrators of the seller and the obligor)?

Yes, a court in Hong Kong will recognise the sale as being effective against the seller, the obligor and third parties.

For this response and the responses below, we have assumed that "located in Hong Kong" means that the relevant party is (for a company) incorporated in Hong Kong, rather than a non-Hong Kong company that has an established place of business in Hong Kong and registered under Part 16 of the Companies Ordinance (Cap. 622). Whether the sale of the receivables is upheld as a "true sale" against the insolvent estate of a non-Hong Kong company also depends on the insolvency laws of the jurisdiction of incorporation of that company.

3.3 Example 2: Assuming that the facts are the same as Example 1, but either the obligor or the purchaser or both are located outside your jurisdiction, will a court in your jurisdiction recognise that sale as being effective against the seller and other third parties (such as creditors or insolvency administrators of the seller), or must the foreign law requirements of the obligor's country or the purchaser's country (or both) be taken into account?

Yes, a court in Hong Kong will recognise the sale as being effective against the seller and third parties.

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3.4 Example 3: If (a) the seller is located in your jurisdiction but the obligor is located in another country, (b) the receivable is governed by the law of the obligor's country, (c) the seller sells the receivable to a purchaser located in a third country, (d) the seller and the purchaser choose the law of the obligor's country to govern the receivables purchase agreement, and (e) the sale complies with the requirements of the obligor's country, will a court in your jurisdiction recognise that sale as being effective against the seller and other third parties (such as creditors or insolvency administrators of the seller) without the need to comply with your jurisdiction's own sale requirements?

In the event of enforcement against the seller before any insolvency proceeding in relation to it, it is likely that a Hong Kong court will recognise the sale as valid and enforceable against the seller (assuming of course the receivables purchase agreement is itself valid, binding and enforceable). As the relevant agreements in this scenario are governed by non-Hong Kong law, the situation envisaged here is enforcement post-foreign judgment against the seller. The response to this question therefore turns on whether a Hong Kong court would recognise and enforce a foreign judgment against the seller (for example, it may not be enforceable if it is against Hong Kong public policy).

However, notwithstanding that the transaction is recognised as a sale by the laws of the obligor's jurisdiction, in the event of insolvency proceedings commencing with respect to the seller, it is likely that a Hong Kong court would apply Hong Kong law true sale analysis to the transaction to determine whether it is treated as a true sale in accordance with the legal tests set out in the response to question 4.9 below.

3.5 Example 4: If (a) the obligor is located in your jurisdiction but the seller is located in another country, (b) the receivable is governed by the law of the seller's country, (c) the seller and the purchaser choose the law of the seller's country to govern the receivables purchase agreement, and (d) the sale complies with the requirements of the seller's country, will a court in your jurisdiction recognise that sale as being effective against the obligor and other third parties (such as creditors or insolvency administrators of the obligor) without the need to comply with your jurisdiction's own sale requirements?

There is no requirement in Hong Kong that the sale be in accordance with Hong Kong law for it to be enforceable against the obligor (subject to the limitations listed in the response to question 4.4 below). However, the question of whether the receivable is enforceable by the purchaser against a Hong Kong obligor depends on the nature of the receivable and the identity and characteristics of the obligor (for example, if the obligor is a consumer, he or she may have remedies available under Hong Kong law notwithstanding the location of the seller or purchaser or the governing law of the receivable – as further set out in the response to question 8.4 below).

3.6 Example 5: If (a) the seller is located in your jurisdiction (irrespective of the obligor's location), (b) the receivable is governed by the law of your jurisdiction, (c) the seller sells the receivable to a purchaser located in a third country, (d) the seller and the purchaser choose the law of the purchaser's country to govern the receivables purchase agreement, and (e) the sale complies with the requirements of the purchaser's country, will a court in your jurisdiction recognise that sale as being effective against the seller and other third parties (such as creditors or insolvency administrators of the seller, any obligor located in your jurisdiction and any third party creditor or insolvency administrator of any such obligor)?

As noted in the response to question 3.4 above, on the insolvency of the Hong Kong seller, a court in Hong Kong is likely to apply Hong Kong law true sale analysis to determine whether it is treated as a sale or a secured transaction.

For an obligor located in Hong Kong, the same considerations as set out in the response to question 3.5 apply. True sale analysis is not relevant with respect to the obligor, as its obligations under the receivables contract remain unchanged irrespective of whether the sale amounts to a sale or to a secured transaction between the seller and the purchaser.

4 Asset Sales

4.1 Sale Methods Generally. In your jurisdiction what are the customary methods for a seller to sell receivables to a purchaser? What is the customary terminology – is it called a sale, transfer, assignment or something else?

The customary method to sell receivables in Hong Kong is a legal or equitable assignment by way of sale. However, receivables may also be sold by way of novation or through a declaration of trust. The term "transfer" has no legal meaning under Hong Kong law but is typically synonymous with a legal or equitable assignment.

A legal assignment is an assignment which meets the criteria set out in Law Amendment and Reform (Consolidation) Ordinance (Cap. 23), being:

(a) an absolute assignment by way of sale of the assignor's entire legal interest in the receivables;

(b) in writing and signed by the assignor; and

(c) with express written notice of the assignment (in particular the date of assignment and the identity of the assignee) given to the obligor. The notice need not be in any particular form and may be given by any party.

An equitable assignment is an assignment which has not met all the required criteria necessary to create a legal assignment. Typically, an equitable assignment arises due to a commercial or practical decision to not provide notice to the obligor at the time of assignment and/or a transfer of a part (but not all) of a receivable. Nevertheless, the courts of Hong Kong recognise an equitable assignment, but such an assignment has a number of practical and legal limitations (for example, priority is affected as set out in the response to question 4.2 below).

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4.2 Perfection Generally. What formalities are required generally for perfecting a sale of receivables? Are there any additional or other formalities required for the sale of receivables to be perfected against any subsequent good faith purchasers for value of the same receivables from the seller?

The requirements to perfect the sale of receivables are, for an assignment by way of sale, set out in the criteria to establish a legal assignment in the response to question 4.1 above.

Perfection and priority against a subsequent good faith purchaser for value of the same receivables requires notice to be given to the obligor before the subsequent good faith purchaser has given its notice to the same obligor (unless the subsequent purchaser had knowledge of the earlier assignment at the time that they were assigned the same receivables).

4.3 Perfection for Promissory Notes, etc. What additional or different requirements for sale and perfection apply to sales of promissory notes, mortgage loans, consumer loans or marketable debt securities?

The sale of promissory notes is governed by the Bills of Exchange Ordinance (Cap. 19), which requires transfer by way of delivery or by way of endorsement and delivery.

For the sale of mortgage loans, the Conveyancing and Property Ordinance (Cap. 219) requires that the assignment of any equitable interest in land be created or disposed of by an instrument in writing and signed by the person creating or disposing of the equitable interest. The assignment of a mortgage loan must also be registered with the Land Registry pursuant to the Land Registration Ordinance (Cap. 128) within one month of the assignment in order to maintain priority over subsequent interests in the same land.

Marketable debt securities may either be in bearer form or registered form. By their very nature, bearer notes only require delivery of the relevant instrument from the seller to the purchaser in order to transfer title. The sale and transfer of ownership of registered notes requires an entry to be made to a register maintained by a registrar on behalf of the issuer of the registered notes. It is only when such register is updated that legal ownership in the notes is transferred from the seller to the purchaser. Please see the response to question 5.5 below for further information.

For consumer loans, please see the response to question 8.4 below.

4.4 Obligor Notification or Consent. Must the seller or the purchaser notify obligors of the sale of receivables in order for the sale to be effective against the obligors and/or creditors of the seller? Must the seller or the purchaser obtain the obligors' consent to the sale of receivables in order for the sale to be an effective sale against the obligors? Whether or not notice is required to perfect a sale, are there any benefits to giving notice – such as cutting off obligor set-off rights and other obligor defences?

Notification to the obligor is not mandatory in order for the sale of receivables to be effective against the obligor or creditors of the seller. However, as noted above in the response to question 4.1, there are a number of practical and legal difficulties that arise from an assignment without notice to the obligor (that is, an equitable assignment rather than a legal assignment). Therefore, unless notice is given, the following issues may arise:

(a) the obligor may discharge its liabilities by making payments solely to the seller, regardless of whether the seller must account to the purchaser for moneys received from the obligor;

(b) the obligor may claim set-off and raise equities and defences against the seller which it may not have been able to raise against the purchaser;

(c) as set out in the response to question 4.2 above, a subsequent purchaser of the same receivables may give notice to the obligor prior to the purchaser such that they gain priority;

(d) the purchaser must join the seller to any proceedings against the obligor; and

(e) the seller and the obligor may amend the relevant receivables contract without the consent or knowledge of the purchaser (although, as a matter of practice, the seller would usually covenant not to do so under any receivables purchase agreement).

Consent from the obligor is required where the underlying receivables contract prohibits assignment of the contract to a third party. A sale will not be enforceable against the obligor if the assignment is made in breach of such a prohibition.

The assignment of a contract, where such contract is silent as to the ability of a party to assign its rights, will generally be valid and effective, although Hong Kong law prohibits assignment for certain specific types of contracts or where it is against public policy to do so.

4.5 Notice Mechanics. If notice is to be delivered to obligors, whether at the time of sale or later, are there any requirements regarding the form the notice must take or how it must be delivered? Is there any time limit beyond which notice is ineffective – for example, can a notice of sale be delivered after the sale, and can notice be delivered after insolvency proceedings have commenced against the obligor or the seller? Does the notice apply only to specific receivables or can it apply to any and all (including future) receivables? Are there any other limitations or considerations?

There are no specific legal requirements as to the form of notice to be given to the obligor. However, English case law decided prior to 30 June 1997 and which continues to apply in Hong Kong (as developed by the common law in Hong Kong), has emphasised that any notice of assignment must, at the very least, specify the relevant date of such assignment and clearly specify the identity of the assignee. It must also be sufficiently clear as to the receivables being assigned. Furthermore, such notice must be expressly provided to the obligor – it is not sufficient that notice to the obligor be inferred or implied in the circumstances.

Notice may be given after the obligor or seller has entered insolvency proceedings.

English case law also has held that notice of assignment of a future receivable is not valid if such receivable had not come into existence before such notice was given.

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4.6 Restrictions on Assignment – General Interpretation. Will a restriction in a receivables contract to the effect that "None of the [seller's] rights or obligations under this Agreement may be transferred or assigned without the consent of the [obligor]" be interpreted as prohibiting a transfer of receivables by the seller to the purchaser? Is the result the same if the restriction says "This Agreement may not be transferred or assigned by the [seller] without the consent of the [obligor]" (i.e., the restriction does not refer to rights or obligations)? Is the result the same if the restriction says "The obligations of the [seller] under this Agreement may not be transferred or assigned by the [seller] without the consent of the [obligor]" (i.e., the restriction does not refer to rights)?

Restrictions on assignment are generally enforceable in Hong Kong as between the assignor and the assignee. It is not legally correct to state that an agreement is "assigned" or "transferred", but this is taken in layman's terms to mean the assignment of any rights arising under the relevant agreement. As such, whichever way the relevant clause is drafted, it is taken to be referring to the assignment of rights under the relevant agreement. The interpretation of assignment restriction clauses follows the English decision of *Linden Gardens Trust Limited v Lenesta Sludge Disposals Limited* [1994] 1 AC 85 (which has been considered by the courts of Hong Kong in *Zhang Qiyun v Shun Shing Construction & Engineering Co Ltd* [2010] HKCU 604), which held that such a clause will be effective as against the obligor and the purchaser, but will not affect relationships between the obligor and seller and the seller and purchaser (i.e. the assignor will remain liable to the assignee for the failed assignment).

It is not possible to "transfer" or "assign" an obligation under Hong Kong law; this must be completed by way of novation, which would require express consent and agreement of both the seller and obligor (together with the purchaser). This is the case even if the "transfer" is by way of book entry only (i.e. the debiting of account with the simultaneous crediting of another account) as this is considered under English law to be a novation rather than an assignment (*R v Preddy* [1996] AC 815).

The final formulation does not specifically prohibit the transfer of rights (with or without consent). Therefore, under the final formulation, it may be possible to assign certain rights without consent.

4.7 Restrictions on Assignment; Liability to Obligor. If any of the restrictions in question 4.6 are binding, or if the receivables contract explicitly prohibits an assignment of receivables or "seller's rights" under the receivables contract, are such restrictions generally enforceable in your jurisdiction? Are there exceptions to this rule (e.g., for contracts between commercial entities)? If your jurisdiction recognises restrictions on sale or assignment of receivables and the seller nevertheless sells receivables to the purchaser, will either the seller or the purchaser be liable to the obligor for breach of contract or tort, or on any other basis?

Notwithstanding the general enforceability of a prohibition of assignment, the decision of *Don King (Productions) Inc v Warren (No 1)* [2000] Ch 291 affirmed that it is possible to establish a trust over the rights that the seller would have under the contract. Therefore, provided that there is no clear prohibition (which the *Barbados Trust Co Ltd v Bank of Zambia* [2007] EWCA Civ 148 decision confirmed could be enforceable and binding as against the seller) over establishing a trust over the rights of a contract, it is possible under Hong Kong law (assuming the Hong Kong courts follow the English common law position) to nevertheless replicate the commercial effect of assigning an interest in the receivables contract to the purchaser notwithstanding the existence of a prohibition of assignment clause.

If a seller sells a receivable in breach of contractual restriction of assignment, the seller may be liable to the obligor for breach of contract and the purchaser may be liable for the tort of inducing another (that is, the seller) to breach a contract.

4.8 Identification. Must the sale document specifically identify each of the receivables to be sold? If so, what specific information is required (e.g., obligor name, invoice number, invoice date, payment date, etc.)? Do the receivables being sold have to share objective characteristics? Alternatively, if the seller sells *all* of its receivables to the purchaser, is this sufficient identification of receivables? Finally, if the seller sells *all* of its receivables *other than* receivables owing by one or more specifically identified obligors, is this sufficient identification of receivables?

The sale document must identify the receivables with such specificity that they are capable of being ascertained, whether they are in existence or will come into existence in the future. Furthermore, a declaration of trust will not be validly established if there is a lack of certainty in the subject matter of the trust (being the receivables in this case).

There is no requirement that receivables share any objective characteristics.

It is sufficient to identify all receivables of the seller for the purposes of ascertaining which receivables are to be the subject of any receivable sale agreement.

4.9 Recharacterisation Risk. If the parties describe their transaction in the relevant documents as an outright sale and explicitly state their intention that it be treated as an outright sale, will this description and statement of intent automatically be respected or is there a risk that the transaction could be characterised by a court as a loan with (or without) security? If recharacterisation risk exists, what characteristics of the transaction might prevent the transfer from being treated as an outright sale? Among other things, to what extent may the seller retain any of the following without jeopardising treatment as an outright sale: (a) credit risk; (b) interest rate risk; (c) control of collections of receivables; (d) a right of repurchase/redemption; (e) a right to the residual profits within the purchaser; or (f) any other term?

The label which parties give to a transaction is not determinative as to the true characterisation of that transaction. As such, the fact that the parties agree that the transaction be treated as a sale is one factor which a court in Hong Kong would consider when determining whether the transaction is a "true sale" or whether it should be characterised as another type of transaction (such as the granting of security or a secured loan).

The first step of any analysis is to examine whether the transaction is of a different legal nature than that which it purports to be. The Court of Appeal in *Welsh Development Agency v Export Finance Co Ltd* [1992] BCLC 148 used a two-stage test to determine the answer to this first question. Firstly, is the arrangement a sham intended to hide the true agreement reached between the parties?

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Secondly, assuming that the transaction is not a sham, what is the legal characterisation of the transaction between the parties?

This approach to categorising transactions was confirmed by the Hong Kong Court of Final Appeal in *Secretary for Justice v Global Merchant Funding Ltd* (2016) 19 HKCFAR. Assuming the transaction is not merely a sham, the court would consider whether a transaction was a loan or a sale by construing the relevant transaction documents and analysing the legal effect (as opposed to the economic or commercial substance of effect) of what the parties had actually agreed.

The English decision of *Re George Inglefield Ltd* [1933] Ch 1 (which has been applied by the Hong Kong courts in the decision of *Hallmark Cards Inc v Yun Choy Ltd* [2012] 1 HKLRD 396) illustrates a number of factors which the court would consider when determining the answer to the second step of the analysis, by looking at whether a particular transaction is a sale or whether it amounts to a transaction involving the granting of security. The non-exhaustive factors include the following:

(a) under a sale, the seller is not entitled to recover the property sold by returning the purchase money to the purchaser. In contrast, the provider of security is entitled to recover the property that is the subject of the transaction as a right called an "equity of redemption" upon return of the money (together with any interest or other amounts owed);

(b) under a sale, the purchaser is free to sell the property without having to account for any profit to the seller. In contrast, the provider of security is entitled to any surplus arising from the sale of the property (after discharge of any secured obligations) that was subject to the relevant security interest; and

(c) conversely, under a sale, if the purchaser sells the property at a loss, it cannot look to the seller to make good that loss, whereas under a secured transaction, the provider of security may be required to make good that loss to the security taker.

Notwithstanding the factors listed above, courts in Hong Kong (and England) have nevertheless found that a transaction amounts to a sale even though:

(a) the purchaser has recourse against the seller to recover the shortfall if the obligor fails to pay the debt in full;

(b) the purchaser may have to make adjustments and payments to the seller after the full amounts of the debts have been received from the obligor;

(c) the seller remains as servicer and responsible for collections from the obligors; and

(d) the seller assumes interest rate risk through the provision of any interest rate hedging arrangement.

Retaining control over collections will not, of itself, affect the true sale analysis. However, an unfettered right of the seller to repay the purchase price to repurchase all the receivables may undermine the true sale nature of the transaction.

4.10 Continuous Sales of Receivables. Can the seller agree in an enforceable manner to continuous sales of receivables (i.e., sales of receivables as and when they arise)? Would such an agreement survive and continue to transfer receivables to the purchaser following the seller's insolvency?

Yes, under Hong Kong law the seller can agree to the continuous sale of receivables.

The sale of any receivable after the date of a winding-up petition (assuming that a winding-up order has been made by a Hong Kong court) is void without court approval.

4.11 Future Receivables. Can the seller commit in an enforceable manner to sell receivables to the purchaser that come into existence after the date of the receivables purchase agreement (e.g., "future flow" securitisation)? If so, how must the sale of future receivables be structured to be valid and enforceable? Is there a distinction between future receivables that arise prior to *versus* after the seller's insolvency?

Yes, under Hong Kong law the seller can agree to assign in equity receivables that come into existence after the date of the receivables purchase agreement. In such a case, the promise to transfer the receivables as they come into existence is enforced in equity so that the purchaser has a right to the receivables as soon as they come into existence. However, notice will still be required to the obligor in accordance with the Law Amendment and Reform (Consolidation) Ordinance to perfect such an assignment.

Note that the sale of any receivable after the date of a winding-up petition (assuming that a winding-up order has been made by a Hong Kong court) is void without court approval.

4.12 Related Security. Must any additional formalities be fulfilled in order for the related security to be transferred concurrently with the sale of receivables? If not all related security can be enforceably transferred, what methods are customarily adopted to provide the purchaser the benefits of such related security?

The response to the question depends on the nature of the asset to which the related security relates. For example, a transfer of a mortgage in Hong Kong would require registration with the Land Registry offices.

In the event that related security cannot be transferred completely, a security taker may be able to rely on an equitable interest rather than a legal interest.

4.13 Set-Off; Liability to Obligor. Assuming that a receivables contract does not contain a provision whereby the obligor waives its right to set-off against amounts it owes to the seller, do the obligor's set-off rights terminate upon its receipt of notice of a sale? At any other time? If a receivables contract does not waive set-off but the obligor's set-off rights are terminated due to notice or some other action, will either the seller or the purchaser be liable to the obligor for damages caused by such termination?

Hong Kong recognises a number of types of set-off. The effect of notice of a sale will depend on the type of set-off in question. For example, insolvency set-off is mandatory; however, the mutuality requirement for insolvency set-off will not survive the sale.

The purchaser of a receivables contract will take the assigned rights "subject to equities", being, in this context, any rights that the debtor has against the seller to set off any amounts owing between the seller and the debtor that the debtor could have been able to set off. Therefore, the purchaser has obtained a qualified right to the debt arising from the relevant receivable contract (*Tito v Waddell (No 2)* [1977] Ch 106). However, generally the right to set-off against the purchaser must have arisen before the relevant date of notice of assignment and must be in relation to the receivables contract itself (*Business Computers Ltd v Anglo-African Leasing Ltd* [1977] 2 All ER 741) and the set-off amount must not exceed the sum due under the receivables contract to the purchaser (*Honour Finance Co Ltd v Chan Yan Pak* [1988] HKC 864).

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Set-off rights that arise after the date of notice of assignment (and subject to the set-off provisions of the receivable contract) cannot be exercised by the debtor to set off against payments due to the purchaser under the receivable contract unless the claims of the debtor and the purchaser are sufficiently closely connected. As between the debtor and the seller (and, again, subject to any set-off provision), the debtor may still nevertheless continue to assert set-off rights against the seller.

Subject to the terms of the relevant agreements between the parties, the mere operation of these principles is unlikely to give rise to liability for damages.

4.14 Profit Extraction. What methods are typically used in your jurisdiction to extract residual profits from the purchaser?

There are typically two ways to extract residual profits from the purchaser.

As a subscriber for the most subordinated tranche of notes, the seller can extract returns on these notes.

The seller can also extract fees by acting as servicer or manager.

5 Security Issues

5.1 Back-up Security. Is it customary in your jurisdiction to take a "back-up" security interest over the seller's ownership interest in the receivables and the related security, in the event that an outright sale is deemed by a court (for whatever reason) not to have occurred and have been perfected (see question 4.9 above)?

It is not customary in Hong Kong to take any form of security interest over the seller's ownership in the receivables. The reason being is that this may prejudice any true sale analysis as it may show an objective intention of the parties to treat the transaction as a security arrangement rather than a true sale of the receivables.

5.2 Seller Security. If it is customary to take back-up security, what are the formalities for the seller granting a security interest in receivables and related security under the laws of your jurisdiction, and for such security interest to be perfected?

Security created by way of charge over some assets must be registered in accordance with section 335 of the Companies Ordinance (Cap. 622). Most relevant to the purchase of receivables is, among other things, the requirement to register charges over land and interests in land, charges over book debts of a company and floating charges over the property or undertaking of a company. "Company" in this context means a company incorporated in Hong Kong or a non-Hong Kong company registered under Part 16 of the Companies Ordinance (which must register the charges in accordance with section 336 of the Companies Ordinance (Cap. 622)).

Failure to register within one month after its creation renders the charge void as against any liquidator of the company and any third party creditor of the company. As such, registration is purely a perfection requirement against third parties and is not a condition to the validity of the charge as against the seller.

Perfection (with respect to priority over subsequent purchasers of the receivables) depends on whether the charge is fixed or floating. However, for practical reasons, it is unlikely that a fixed charge will be taken over receivables. Please see the response to question 5.3 below for further commentary on perfection and priority of security interests.

5.3 Purchaser Security. If the purchaser grants security over all of its assets (including purchased receivables) in favour of the providers of its funding, what formalities must the purchaser comply with in your jurisdiction to grant and perfect a security interest in purchased receivables governed by the laws of your jurisdiction and the related security?

The formalities required to perfect security interests granted by the purchaser depends on the nature of the security interests granted over the purchased receivables.

For security interests granted by assignment by way of security, the legal assignment requirements as set out above in the response to question 4.1 apply.

Security interests may also be granted by way of mortgage, fixed charge or floating charge. Although other forms of consensual security exist under Hong Kong law (i.e. pledge and lien), it is most likely that such security is provided by way of charge or mortgage. In Hong Kong, financing is usually secured by means of taking a fixed charge (or mortgage) over real property owned by the purchaser and a floating charge over the assets and undertaking of the purchaser.

Registration is required for some fixed charges, and all floating charges, in accordance with the Companies Ordinance (Cap. 622) (being within one month of the date of creation of such charge). Failure to register in accordance with the Companies Ordinance will render the charge void as against the liquidator of the purchaser as well as its creditors.

Perfection (with respect to priority over subsequent purchasers or subsequent chargors of the same assets) depends on whether the charge is fixed or floating. Assuming that the third-party purchaser is acquiring the receivables in good faith and for value, the question of whether such a third-party purchaser acquires priority over the previous security taker turns on the question of what notice such a third-party purchaser actually had or is deemed to have (constructive notice).

In the case of a fixed charge, the chargor has neither actual nor ostensible authority to deal with the assets free of the fixed charge. As such, provided that the third-party purchaser has actual notice (irrespective of whether they had notice of the terms of the relevant charging document) or deemed constructive notice of the existence of a fixed charge, the third-party purchaser for value will have priority over the first security taker.

However, the application of the doctrine of constructive notice in relation to the existence of a floating charge is not so straightforward, as a third-party subsequent purchaser (or subsequent chargor) is entitled to assume that the seller has the freedom to dispose of the receivables without actual notice to the contrary. As such, without actual notice of the content of the relevant charging document, establishing notice of any negative pledge or other restriction on disposal of the relevant asset is more difficult to achieve.

In either case, when determining priority between competing interests, a party will be held to have constructive notice of the existence of the fixed or floating charge on the basis of whether it could reasonably have been expected to search the register. That means that, for example, a third-party purchaser buying goods in the ordinary course of business is unlikely to search the register whereas a financial institution taking security is likely to have deemed constructive notice of the existence of the charge.

It is likely that a person with constructive notice of a charge registered with the Hong Kong Companies Registry will also have constructive notice of its terms (including any prohibition of

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disposal or negative pledge clauses therein), although there is no case law on point. With the implementation of the new Companies Ordinance (Cap. 622) in Hong Kong, certified copies of certain prescribed charge instruments must be registered with the Hong Kong Companies Registry, and as such, the terms of such charge will be publicly available through a search. This statutory development appears to reverse the legal position established in the Hong Kong case of *ABN Amro Bank NV v Chiyu Banking Corporation Ltd and Ors* [2000] 3 HKC 381 which limited the doctrine of constructive notice to the existence of a registered charge, but not of its terms.

To the extent that security relates to assets such as land, ships or aircraft, special registration requirements apply under Hong Kong law.

5.4 Recognition. If the purchaser grants a security interest in receivables governed by the laws of your jurisdiction, and that security interest is valid and perfected under the laws of the purchaser's jurisdiction, will the security be treated as valid and perfected in your jurisdiction or must additional steps be taken in your jurisdiction?

If the purchaser is a non-Hong Kong company that is registered under Part 16 of the Companies Ordinance (Cap. 622), it will be required to register any security in accordance with Hong Kong law (for example, a floating charge will need to be registered in accordance with the Companies Ordinance (Cap. 622), notwithstanding that the security interest is valid and perfected under the laws of the purchaser's country).

5.5 Additional Formalities. What additional or different requirements apply to security interests in or connected to insurance policies, promissory notes, mortgage loans, consumer loans or marketable debt securities?

Security over insurance policies is typically achieved through assignment of the rights, title, interests and benefits in the insurance policy as well as an assignment of any proceeds received under such insurance policy to the secured party (or security trustee). An additional measure that is typically taken by secured parties is to have the secured party (or security trustee) recorded as a "loss payee" under the relevant insurance policy.

Security over promissory notes or marketable debt securities (in each case, where they are in definitive bearer form) is usually taken by way of a pledge – although definitive bearer instruments are very uncommon nowadays. Security over bearer instruments may also be made by such instruments being mortgaged by delivery.

Taking security over marketable debt securities is complex and depends on a number of factors. However, key points are summarised below:

(a) if the debt securities are not cleared – for a legal mortgage, the security taker's name and details would be entered on the register maintained by the registrar of the relevant issuer until such time as the obligations of the security provider are discharged. For an equitable mortgage or charge, the security provider completes all necessary transfer certificates but transfer by way of registration is not effected until enforcement steps are undertaken by the security taker;

(b) if the debt securities are cleared – for a legal mortgage, the security taker's name would be entered into the relevant securities account of an intermediary/custodian who itself holds an interest directly from the issuer or (as is most likely the case) from a higher-tier intermediary. Alternatively, security may be taken by way of an assignment of rights against the relevant intermediary together with an assignment of the rights, title and interests in or relating to the debt security; and

(c) security taken over mortgage loans would typically be required to be registered with the Land Registry in Hong Kong in accordance with the Land Registration Ordinance (Cap. 128) as it creates or transfers an interest in real property. Please see the response to question 4.3 above for further information.

5.6 Trusts. Does your jurisdiction recognise trusts? If not, is there a mechanism whereby collections received by the seller in respect of sold receivables can be held or be deemed to be held separate and apart from the seller's own assets (so that they are not part of the seller's insolvency estate) until turned over to the purchaser?

Yes, trusts are recognised under Hong Kong law.

5.7 Bank Accounts. Does your jurisdiction recognise escrow accounts? Can security be taken over a bank account located in your jurisdiction? If so, what is the typical method? Would courts in your jurisdiction recognise a foreign law grant of security (for example, an English law debenture) taken over a bank account located in your jurisdiction?

Yes, escrow accounts are recognised under Hong Kong law.

Security is typically taken over a bank account located in Hong Kong by the granting of either a fixed charge or a floating charge (which may crystallise (i.e. convert) into a fixed charge upon the occurrence of a default or other like circumstance under the relevant transaction documents).

A court in Hong Kong would generally recognise effective foreign law-governed security over a bank account in Hong Kong, although ideal practice would be to have security over a Hong Kong bank account governed by Hong Kong law to minimise delays or complications in enforcement.

5.8 Enforcement over Bank Accounts. If security over a bank account is possible and the secured party enforces that security, does the secured party control all cash flowing into the bank account from enforcement forward until the secured party is repaid in full, or are there limitations? If there are limitations, what are they?

In general, a secured party would control all cash flowing in and out of a bank account during enforcement. The ability of the secured party to enforce the security would remain subject to the terms agreed in the relevant security document establishing a charge over the bank account and, in particular, whether a floating charge over the bank account has crystallised into a fixed charge.

5.9 Use of Cash Bank Accounts. If security over a bank account is possible, can the owner of the account have access to the funds in the account prior to enforcement without affecting the security?

Yes; the granting of a floating charge over the bank account provides for (prior to crystallisation) the chargor to access funds in accordance with the terms and conditions of the relevant security document.

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6 Insolvency Laws

6.1 Stay of Action. If, after a sale of receivables that is otherwise perfected, the seller becomes subject to an insolvency proceeding, will your jurisdiction's insolvency laws automatically prohibit the purchaser from collecting, transferring or otherwise exercising ownership rights over the purchased receivables (a "stay of action")? If so, what generally is the length of that stay of action? Does the insolvency official have the ability to stay collection and enforcement actions until he determines that the sale is perfected? Would the answer be different if the purchaser is deemed to only be a secured party rather than the owner of the receivables?

Insolvency proceedings with respect to the seller will not affect the rights of the purchaser if the sale meets the requirements of a "true sale" or legal assignment under Hong Kong law.

The situation will be different if the sale was conducted as an equitable assignment (rather than a legal assignment or through novation). On the making of a winding-up order, or on the appointment of a provisional liquidator, with respect to the seller, it may not be possible to compel the seller to perform its obligations under the relevant transaction documents without leave of the court.

If a transaction, which was intended by the parties to be a sale, is subsequently recharacterised as a secured transaction under Hong Kong law, there is a risk that such a transaction would be held void against the liquidator of the seller as well as creditors of the seller due to lack of registration in accordance with the Companies Ordinance (Cap. 622).

There are no formal corporate rescue procedures in the present regime in Hong Kong.

With the introduction of the new Companies Ordinance (Cap. 622) on 3 March 2014, all of the sections except for the prospectus regime and the winding-up and insolvency provisions are now regulated by the new Companies Ordinance. These remaining sections remain under the old Companies Ordinance which has been renamed as the Companies (Winding Up and Miscellaneous Provisions) Ordinance ("**CWUMPO**").

Various consultations by the government in Hong Kong over a number of years have outlined a proposal to introduce the concept of provisional supervision. The current proposals envisage such provisional supervision being initiated by filing a notice with the Companies Registry (without requiring court approval). This would then create a moratorium for, initially a 45-day period, where the provisional supervisor would prepare a voluntary agreement. Creditors will be able to extend the 45-day period up to a maximum of six months. A court will be able to extend the period for as long as it deems necessary. Discussions and further consultations regarding this arrangement and its exemptions are still taking place and are yet to be finalised.

Additionally, the Financial Institutions (Resolution) Ordinance (Cap. 628) came into operation on 7 July 2017. Under the Ordinance, a range of general resolution powers will be provided to regulators to ensure stability in the financial markets in the event of any insolvency or restructuring of troubled financial institutions. Some of the powers allow regulators to affect contractual and property rights as well as payments (including in respect of any priority of payment) that creditors would receive in resolution, including but not limited to powers to write off, or convert into equity, all or a part of the liabilities of a troubled financial institution. These discretionary powers may affect the sale of receivables from a troubled financial institution to a third party.

6.2 Insolvency Official's Powers. If there is no stay of action, under what circumstances, if any, does the insolvency official have the power to prohibit the purchaser's exercise of its ownership rights over the receivables (by means of injunction, stay order or other action)?

Please see the response to question 6.3 below.

6.3 Suspect Period (Clawback). Under what facts or circumstances could the insolvency official rescind or reverse transactions that took place during a "suspect" or "preference" period before the commencement of the seller's insolvency proceedings? What are the lengths of the "suspect" or "preference" periods in your jurisdiction for (a) transactions between unrelated parties, and (b) transactions between related parties? If the purchaser is majority-owned or controlled by the seller or an affiliate of the seller, does that render sales by the seller to the purchaser "related party transactions" for purposes of determining the length of the suspect period? If a parent company of the seller guarantee's the performance by the seller of its obligations under contracts with the purchaser, does that render sales by the seller to the purchaser "related party transactions" for purposes of determining the length of the suspect period?

There are a number of circumstances where pre-insolvency transactions may be set aside:

(a) transaction at an undervalue and unfair preference (CWUMPO, sections 265D and 266);
   - a. transaction at an undervalue:
     - i. a company enters into a transaction with a person at an undervalue if: (x) the company enters into a transaction with that person on terms that provide for the company to receive no consideration; or (y) the company enters into a transaction with that person for a consideration value of which is significantly less than the value of the consideration provided by the company;
     - ii. however, a Hong Kong court would not make an order for restoring the position if it is satisfied that: (x) the company entered into the transaction in good faith and for the purpose of carrying on its business; and (y) at the time the company did so, there were reasonable grounds for believing that the transaction would benefit the company;
   - b. unfair preference:
     - i. a company gives an unfair preference to a person if: (x) that person is one of the company's creditors; and (y) the company does anything which has the effect of putting that person into a position which, in the event of the company going into insolvent liquidation, will be better than the position that person would have been in if that thing had not been done;
   - c. length of the "suspect" or "preference" period:
     - i. for a transaction at an undervalue, the relevant period is five years;
     - ii. for an unfair preference which is not a transaction at an undervalue and is given to a person who is connected with the company, the relevant period is two years;
     - iii. in any other case of an unfair preference which is not a transaction at an undervalue, the relevant period is six months; and
     - iv. the relevant periods above apply only if either of the following conditions is satisfied:

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1. the company is unable to pay its debts at that time; or
2. the company becomes unable to pay its debts in consequence of the transaction or unfair preference;

(b) anti-deprivation rule – any agreement which, on insolvency, increases a creditor's claim or transfers assets to a particular creditor, is void. There is no preference or suspect period;

(c) invalidation of floating charges (CWUMPO, section 267) – any floating charge created within one year before the commencement of winding-up of a company may be set aside where the company was insolvent or became so as a result of the entering into the charge or associated transactions, except to the extent of the value of any consideration received by the company on or after the creation of such floating charge (i.e. the floating charge remains valid to the extent that it secured fresh funds);

(d) extortionate credit transactions (CWUMPO, section 264B) – a transaction entered into within three years of the commencement of winding-up of a company may be set aside where payments in relation to such a transaction are considered grossly exorbitant or the terms of the credit grossly contravene ordinary principles of fair dealing;

(e) transactions defrauding creditors (Conveyancing and Property Ordinance (Cap. 219), section 60) – any disposition of property made with the intent to defraud creditors may be voidable. There is no preference or suspect period. However, such a claim would need to be made by a person prejudiced by such a disposition and would be subject to normal limitation periods; and

(f) disclaiming of onerous property (CWUMPO, section 268) – the liquidator of a company may disclaim onerous property, which includes unprofitable contracts, effectively converting a counterparty's rights under the relevant agreement into an unsecured claim. Again, there is no preference or suspect period.

6.4 Substantive Consolidation. Under what facts or circumstances, if any, could the insolvency official consolidate the assets and liabilities of the purchaser with those of the seller or its affiliates in the insolvency proceeding? If the purchaser is owned by the seller or by an affiliate of the seller, does that affect the consolidation analysis?

There are limited circumstances under Hong Kong law where liabilities of a company may be imposed on another company. The typical circumstances are where the company was formed principally as a sham, to evade existing liabilities or to perpetrate a fraud.

Furthermore, there is no law in Hong Kong that provides for the pooling of assets. The pooling of assets and liabilities in Hong Kong is based on judicial discretion. Pooling is only allowed when it appears that it is the best or only method of distributing assets back to creditors. However, court sanction is required and the reasons for pooling assets must be clearly stated.

6.5 Effect of Insolvency on Receivables Sales. If insolvency proceedings are commenced against the seller in your jurisdiction, what effect do those proceedings have on (a) sales of receivables that would otherwise occur after the commencement of such proceedings, or (b) on sales of receivables that only come into existence after the commencement of such proceedings?

The commencement of insolvency proceedings would have no immediate legal effect on either the sale of receivables after such proceedings have commenced or the sale of receivables that have come into existence after such proceedings have commenced. The general rule is that insolvency does not terminate contracts nor extinguish rights, although remedies are restricted post-insolvency.

One example in particular of this restriction is that, in the event that a court has granted a winding-up order with respect to a party, any disposition of the assets of such a party from the date that the winding-up petition was presented is void (or deemed void) unless the court otherwise approves.

Notwithstanding this, if there has been a true sale of the future receivables (for example, such that legal assignment has been perfected by the purchaser giving notice to the obligors), then subject to the issues outlined in the response to question 6.3 above, the seller's insolvency would not affect the purchaser's rights in the relevant receivables.

6.6 Effect of Limited Recourse Provisions. If a debtor's contract contains a limited recourse provision (see question 7.3 below), can the debtor nevertheless be declared insolvent on the grounds that it cannot pay its debts as they become due?

This issue recently arose for determination in the English decision of *ARM Asset Backed Securities S.A.* [2013] EWHC 3351 (Ch), where the court held that a Luxembourg company (with its centre of main interests determined to be in England) could be wound-up where the court was satisfied that the company was unable to pay its debts, notwithstanding the inclusion of limited recourse wording (and "non-petition" wording – see our response to question 7.4 below) for the bonds which the company had issued. The court considered, among other things, the question of whether or not a company should be wound-up should be separate and unrelated from the question as to the quantum that creditors would receive from the liquidation of that company.

Such a question has not, to date, been considered by Hong Kong courts. Although persuasive, decisions of English courts are not binding on courts in Hong Kong. This case is unusual in that it was the directors of the issuer who petitioned the court rather than creditors of the issuer.

As a matter of market practice and drafting convention, documentation which contain limited recourse wording also invariably include non-petition clauses to limit the ability of creditors (but not directors) to seek to wind-up the relevant company. Therefore, it is unlikely that the opportunity will arise for a Hong Kong court to consider a limited recourse provision in isolation from a non-petition provision.

7 Special Rules

7.1 Securitisation Law. Is there a special securitisation law (and/or special provisions in other laws) in your jurisdiction establishing a legal framework for securitisation transactions? If so, what are the basics? Is there a regulatory authority responsible for regulating securitisation transactions in your jurisdiction?

There are no laws in Hong Kong specifically for securitisation.

The Hong Kong Monetary Authority (the "**HKMA**") is the regulator in Hong Kong most relevant to securitisation transactions and is responsible for regulating financial institutions. The Securities and Futures Commission is also involved where there is an issuance of securities.

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7.2 Securitisation Entities. Does your jurisdiction have laws specifically providing for establishment of special purpose entities for securitisation? If so, what does the law provide as to: (a) requirements for establishment and management of such an entity; (b) legal attributes and benefits of the entity; and (c) any specific requirements as to the status of directors or shareholders?

There are no laws in Hong Kong specifically for the establishment of special purpose vehicles.

7.3 Location and form of Securitisation Entities. Is it typical to establish the special purpose entity in your jurisdiction or offshore? If in your jurisdiction, what are the advantages to locating the special purpose entity in your jurisdiction? If offshore, where are special purpose entities typically located for securitisations in your jurisdiction? What are the forms that the special purpose entity would normally take in your jurisdiction and how would such entity usually be owned?

While it is possible to establish SPVs in Hong Kong, it is more typical to establish the SPV offshore. In Hong Kong, SPVs established for securitisations are typically located in the Cayman Islands or British Virgin Islands. There are many advantages to using an offshore SPV in a securitisation transaction including no or low taxation rates, secure economic and political backdrops and reputations for being innovative in offshore services. Ultimately, the choice may depend on investor preference, location of counterparties and regulatory requirements.

For SPVs established in Hong Kong, the Companies Ordinance (Cap. 622) provides the legal framework for their establishment. As a company, a SPV has its own distinct legal personality. It is common for such an SPV to use an orphan structure (shares held by a trustee on a charitable purpose trust).

7.4 Limited-Recourse Clause. Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) limiting the recourse of parties to that agreement to the available assets of the relevant debtor, and providing that to the extent of any shortfall the debt of the relevant debtor is extinguished?

It is likely that a Hong Kong court would give effect to a limited-recourse clause, although there is no case law to date in Hong Kong which has considered its validity.

7.5 Non-Petition Clause. Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) prohibiting the parties from: (a) taking legal action against the purchaser or another person; or (b) commencing an insolvency proceeding against the purchaser or another person?

It is likely that a Hong Kong court would give effect to a non-petition clause, although there is no case law to date in Hong Kong which has considered its validity. However, enforcing such a clause to prevent a party from taking legal action would require a court to exercise its discretion as to whether to grant an injunction or not – injunctive relief is not a right *per se* available to a plaintiff under Hong Kong law.

Similarly, the court in Hong Kong retains the discretion under the Companies Ordinance (Cap. 622) to have a company wound-up where it is, in the opinion of the court, just and equitable to do so. As such, although unlikely, it is possible that a court exercises such discretion to allow insolvency proceedings to commence against the purchaser or another person.

7.6 Priority of Payments "Waterfall". Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) distributing payments to parties in a certain order specified in the contract?

Waterfall or payment priority provisions are likely to be valid and enforceable under Hong Kong law for a Hong Kong law-governed document, although this has not been considered by any Hong Kong court to date. Assuming validity and enforceability under Hong Kong law, there is no reason why a court in Hong Kong would not give effect to such a clause with respect to a Hong Kong entity for a contract governed by a foreign law (subject to any foreign law-governed contract being void for public policy reasons or illegality in Hong Kong and payments mandatorily preferred by law).

Although not binding on a Hong Kong court, the English Court of Appeal decision of *Belmont Park Investments Pty Ltd v BNY Corporate Trustee Services Ltd* [2012] 1 AC 383 has also affirmed the validity of "flip-clauses" which have the effect of altering the priority of payments upon an event of default (including insolvency) of a party to an agreement containing such a clause. As such, it is likely that a Hong Kong court would also uphold the validity of a "flip-clause" and, by necessary extension, the validity in general of priority of payment provisions.

7.7 Independent Director. Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) or a provision in a party's organisational documents prohibiting the directors from taking specified actions (including commencing an insolvency proceeding) without the affirmative vote of an independent director?

Provided that directors act in accordance with their fiduciary duties as directors and any requirements as set out in the Companies Ordinance and the Hong Kong listing rules (if applicable), there is no specific law which would prohibit contractual provisions or provisions in the company's memorandum and articles of association that prevent a director from acting or not acting in particular circumstances. Of course, such provisions (whether in a Hong Kong law-governed document or not) would remain subject to principles of general law, such as contracts being void for public policy reasons or illegality in Hong Kong.

7.8 Location of Purchaser. Is it typical to establish the purchaser in your jurisdiction or offshore? If in your jurisdiction, what are the advantages to locating the purchaser in your jurisdiction? If offshore, where are purchasers typically located for securitisations in your jurisdiction?

It is typical to establish the purchaser offshore. The purchasers are typically located in the Cayman Islands and the British Virgin Islands.

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8 Regulatory Issues

8.1 Required Authorisations, etc. Assuming that the purchaser does no other business in your jurisdiction, will its purchase and ownership or its collection and enforcement of receivables result in its being required to qualify to do business or to obtain any licence or its being subject to regulation as a financial institution in your jurisdiction? Does the answer to the preceding question change if the purchaser does business with more than one seller in your jurisdiction?

Depending on the nature of the receivables, the purchaser may be required to obtain a particular licence or be subject to regulations. For example, the receivables may be relevant to business regulated by the Money Lenders Ordinance or the Banking Ordinance. If so, the purchaser will need to obtain the required licences or approvals before purchasing the relevant receivables.

A non-Hong Kong company must register in accordance with the Business Registration Ordinance (Cap. 310) if it is carrying on in Hong Kong "any form of trade, commerce, craftsmanship, profession, calling or other activity carried on for the purpose of gain". This is irrespective of whether it is required to register under Part 16 of the Companies Ordinance (see question 3.2 above). Please see the commentary below in question 9.6 as to whether mere ownership of receivables may result in the purchaser "carrying on a business" under Hong Kong law.

8.2 Servicing. Does the seller require any licences, etc., in order to continue to enforce and collect receivables following their sale to the purchaser, including to appear before a court? Does a third-party replacement servicer require any licences, etc., in order to enforce and collect sold receivables?

There are no specific requirements under Hong Kong law to collect and enforce receivables (other than any requirements specific to the industry or nature of receivables).

8.3 Data Protection. Does your jurisdiction have laws restricting the use or dissemination of data about or provided by obligors? If so, do these laws apply only to consumer obligors or also to enterprises?

Yes, in Hong Kong the Personal Data (Privacy) Ordinance (Cap. 486) ("**PDPO**") governs the collection, use and dissemination of personal data of living individuals. This does not apply to information with respect to enterprises.

The PDPO applies to anyone who collects or uses personal information which is capable of identifying an individual. In such circumstances, the "data user" must comply with a number of data protection principles that are set out in schedule 1 of the PDPO. In April 2013, criminal liability was introduced in respect of the new direct marketing provisions, which deal with unauthorised transfers of personal data of the third parties for direct marketing purposes.

The Code of Banking Practice may also apply if the relevant entity is an "authorized institution" – please see the response to question 8.4 below. This imposes on such "authorized institutions" a duty to maintain privacy when handling information relating to individual customers.

Data about, or provided by, obligors may also be protected by more general Hong Kong legal and regulatory principles that require the protection of confidential information. Largely, these apply irrespective of the legal structure of the obligor, but their precise application depends on the circumstances.

8.4 Consumer Protection. If the obligors are consumers, will the purchaser (including a bank acting as purchaser) be required to comply with any consumer protection law of your jurisdiction? Briefly, what is required?

Yes, a purchaser would be required to comply with certain consumer protection laws to the extent they apply with respect to the nature of the receivables and the identity and nature of the purchaser.

In particular (but not necessarily exhaustive):

(a) the Banking Ordinance (Cap. 155) and the Code of Banking Practice where the purchaser is an "authorized institution" as defined in the Banking Ordinance – "authorized institutions" are expected to act in accordance with the Code when dealing with individual customers (please also see paragraph (h) below);

(b) the Control of Exemption Clauses Ordinance (Cap. 71) – which limits the extent to which civil liability for breach of contract, or for negligence or other breach of duty, can be avoided by means of contract terms or otherwise;

(c) the Money Lenders Ordinance (Cap. 163) – as discussed in the response to question 1.2 above;

(d) the Sale of Goods Ordinance (Cap. 26) – which provides basic protection for sales of goods to consumers, such as requiring any goods sold to be of satisfactory quality, fit for purpose and for such goods to correspond with any description given in the packaging. Sellers who fail to meet the prescribed standards will be required to issue any consumer or purchaser a full refund;

(e) the Supply of Services (Implied Terms) Ordinance (Cap. 457) – which implies certain reasonableness qualifiers to terms of a consumer contract in the absence of express terms;

(f) the Unconscionable Contracts Ordinance (Cap. 458) – which grants to Hong Kong courts the power to determine that part or whole of a contract with a consumer may be unenforceable if found to be unconscionable;

(g) the Trade Descriptions Ordinance (Cap. 362) – which prohibits false trade descriptions, false, misleading or incomplete information, false marks and misstatements in respect of goods and services, and in respect of services, includes further offences for misleading omissions, aggressive commercial practices, bait advertising, bait-and-switch and wrongly accepting payment; and

(h) the various circulars and guidelines issued by the Securities and Futures Commission where the purchaser is licensed by the Securities and Futures Commission and by Hong Kong Monetary Authority where the purchaser is an "authorized institution" – which requires the purchaser in such circumstances to comply with such various circulars, codes and guidelines.

8.5 Currency Restrictions. Does your jurisdiction have laws restricting the exchange of your jurisdiction's currency for other currencies or the making of payments in your jurisdiction's currency to persons outside the country?

There are no currency exchange controls in Hong Kong. However, the flow of funds in and out of Hong Kong may be restricted or prohibited by laws such as the United Nations Sanctions Ordinance (Cap. 537), the United Nations (Anti-Terrorism Measures) Ordinance (Cap. 575), and related regulations.

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The exchange of currencies is also generally confined to "authorized institutions" as defined in the Banking Ordinance and money changing service providers that are licensed under the Anti-Money Laundering and Counter-Terrorist Financing (Financial Institutions) Ordinance (Cap. 615).

8.6 Risk Retention. Does your jurisdiction have laws or regulations relating to "risk retention"? How are securitisation transactions in your jurisdiction usually structured to satisfy those risk retention requirements?

Yes, but no specific Hong Kong retention requirements *per se*. Under the HKMA Supervisory Policy Manual CR-G-12, an originating authorized institution (as defined in the Banking Ordinance) of a securitisation transaction should ensure that investors have readily available access to all materially relevant data including the amount of risk retention by the originating authorised institution in the transaction and the manner in which the risk is retained. In addition, unless otherwise agreed with the HKMA, authorised institutions are required to refrain from investing in, or incurring an exposure to a securitisation transaction the originator of which has not disclosed its compliance with applicable risk retention requirements (namely requirements imposed by relevant authorities of other jurisdictions). As such, in Hong Kong it is important to be aware of any applicable risk retention policies of other jurisdictions (such as the US or Europe) which may impact on the transaction.

8.7 Regulatory Developments. Have there been any regulatory developments in your jurisdiction which are likely to have a material impact on securitisation transactions in your jurisdiction?

Regulatory developments concerning securitisation have primarily been occurring in the US and Europe. These changes have mainly concerned retention of risk (see our response to 8.6 above) and due diligence and disclosure requirements. These changes may impact a Hong Kong securitisation transaction if the transaction has a connection with the US or Europe.

9 Taxation

9.1 Withholding Taxes. Will any part of payments on receivables by the obligors to the seller or the purchaser be subject to withholding taxes in your jurisdiction? Does the answer depend on the nature of the receivables, whether they bear interest, their term to maturity, or where the seller or the purchaser is located? In the case of a sale of trade receivables at a discount, is there a risk that the discount will be recharacterised in whole or in part as interest? In the case of a sale of trade receivables where a portion of the purchase price is payable upon collection of the receivable, is there a risk that the deferred purchase price will be recharacterised in whole or in part as interest? If withholding taxes might apply, what are the typical methods for eliminating or reducing withholding taxes?

No, there is no withholding of taxes in Hong Kong. Whether any amount (such as a discount or deferred purchase price) is to be treated as interest for profits tax purposes depends upon whether such amount satisfies sections 16(1) and 16(2) of the Inland Revenue Ordinance (Cap. 112) of Hong Kong ("**IRO**"). There are no specific provisions which deem a discount or deferred purchase price as being treated as interest for profits tax purposes, although the Inland Revenue Department in Hong Kong has stated that its position, at least with respect to initial discounting of securities, is that such discount may be deductible as interest (amortised over the life of such security) provided that the tests in sections 16(1) and 16(2) are also satisfied. This conclusion is not, however, directly relevant to discounted receivables, which are not thought of as lending or borrowing arrangements.

9.2 Seller Tax Accounting. Does your jurisdiction require that a specific accounting policy is adopted for tax purposes by the seller or purchaser in the context of a securitisation?

No, there is no specific accounting policy to be adopted for tax purposes in the context of securitisation. Hong Kong companies are required under the Companies Ordinance to prepare financial statements that give a true and fair view and are expected to prepare such statements under local GAAP (Hong Kong Financial Reporting Standards).

9.3 Stamp Duty, etc. Does your jurisdiction impose stamp duty or other transfer or documentary taxes on sales of receivables?

No, there is no stamp duty on the sale of receivables. There is, however, stamp duty imposed on the transfer of interests in land (including the transfer of mortgages – although the collector of stamps in Hong Kong has been willing to adjudicate that a mortgage transfer is not subject to stamp duty) as well as on certain transfers of stock.

9.4 Value Added Taxes. Does your jurisdiction impose value added tax, sales tax or other similar taxes on sales of goods or services, on sales of receivables or on fees for collection agent services?

There is no value added tax, sales tax or any other similar taxes in Hong Kong.

9.5 Purchaser Liability. If the seller is required to pay value-added tax, stamp duty or other taxes upon the sale of receivables (or on the sale of goods or services that give rise to the receivables) and the seller does not pay, then will the taxing authority be able to make claims for the unpaid tax against the purchaser or against the sold receivables or collections?

There are no such taxes applicable in the context of the sale of receivables.

However, under Hong Kong law, tax may be recovered from a third party if the taxpayer is in default of their taxation payment obligations. Such outstanding taxes may be recovered from any third party who (i) owes or is about to pay money to the taxpayer, (ii) holds money on account of another person for payment to the taxpayer, or (iii) has authority to pay money from some other person to the taxpayer. Failure to comply with a notice from the Commissioner of Inland Revenue may result in the third party becoming personally liable for the whole of the tax that was to be paid.

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9.6 Doing Business. Assuming that the purchaser conducts no other business in your jurisdiction, would the purchaser's purchase of the receivables, its appointment of the seller as its servicer and collection agent, or its enforcement of the receivables against the obligors, make it liable to tax in your jurisdiction?

There is a profits tax payable by every person "carrying on a trade, profession or business in Hong Kong" in respect of profits "arising or derived from Hong Kong … from such trade, profession or business" (Inland Revenue Ordinance (Cap. 112)).

Whether a person is carrying on business is ultimately a question of fact having regard to the circumstances as a whole and determined by a number of indicia, with no single indicia being determinative. However, it is important to note that courts in England have considered that the passive receipt of share profits was held to be a business (*IRC v Korean Syndicate Ltd* (1921) 3 KB 258), as well as passive receipt of a fixed annuity (*South Behar Railway Co Ltd v IRC* (1925) AC 476).

9.7 Taxable Income. If a purchaser located in your jurisdiction receives debt relief as the result of a limited recourse clause (see question 7.3 above), is that debt relief liable to tax in your jurisdiction?

Section 15(1)(c) of the IRO deems "sums received by or accrued to a person by way of grant, subsidy or similar financial assistance in connection with the carrying on of a trade, profession or business in Hong Kong …" chargeable to profits tax. A debt relief is considered as a financial assistance to the purchaser by the Inland Revenue Department and, therefore, section 15(1)(c) of the IRO applies.

Moreover, where a deduction for the interest on the debt had previously been claimed and allowed as a trading expense, the amount relieved would be treated as a trading receipt under section 15(2) of the IRO at the time of the relief and is, therefore, liable to tax.

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We are ranked band 1 in Capital Markets: Securitisation by both *Chambers Asia Pacific* and *IFLR 1000* for 2017. Our team has won the Structured Finance and Securitisation Team of The Year by *IFLR* Asia Awards for three consecutive years (2014–2016) and was shortlisted for 2017.

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India

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1 Receivables Contracts

1.1 Formalities. In order to create an enforceable debt obligation of the obligor to the seller: (a) is it necessary that the sales of goods or services are evidenced by a formal receivables contract; (b) are invoices alone sufficient; and (c) can a binding contract arise as a result of the behaviour of the parties?

Under Indian law governing contracts, even oral contracts, are enforceable. Therefore, for sales of goods or services it is not necessary that a formal receivables contract should evidence the same. However, if any security interest in immovable property is created to secure the debt obligations of the obligor, then depending on the nature of security created, the same must be evidenced by a formal contract. Therefore: (i) invoices would also be sufficient to establish a debt obligation; and (ii) a binding contract can be established under Indian law based on the actions taken by the parties if the proposal of terms and acceptance thereof (concluding into a contract) are made by means other than in words and do not involve any creation or transfer of interest in immovable property. However, given that establishing the behaviour of parties to conclusively determine that a contract has been entered into is quite difficult; it would always be advisable to record the terms of the receivables contract in a formal agreement.

1.2 Consumer Protections. Do your jurisdiction's laws: (a) limit rates of interest on consumer credit, loans or other kinds of receivables; (b) provide a statutory right to interest on late payments; (c) permit consumers to cancel receivables for a specified period of time; or (d) provide other noteworthy rights to consumers with respect to receivables owing by them?

There are restrictions on rates of interest that can be charged under Indian laws. These are set out under the Usurious Loans Act, 1918 and various other state laws. However, there are no clearly defined limits which one can analyse to determine the applicable limits as the law only stipulates that the rate charged should not be 'excessive'. We note that banking and non-banking financial institutions would also have to be prudent when determining interest rates as India's central bank, being the Reserve Bank of India ("**RBI**") and the regulatory authority for such institutions, could question excessive rates, irrespective of whether such rates fall foul of any general laws. In certain situations, even where the parties have agreed upon a rate of interest, there is the possibility of a court where enforcement proceedings are initiated, not granting full effect to the interest/default interest clause based on the principles of equity, justice and good conscience.

For lending to certain sectors, like the priority sector, which are regulatory mandated exposures, there are certain interest rate caps imposed by the RBI. The consequence of breaching the rate cap is that the relevant loan will not be treated as a priority sector exposure; however, this will not render such interest rates void.

Whilst there is no statutory right to interest on late payments, the courts in India would normally award nominal interest, where the contract is silent in respect of the same.

Under Indian law, there are no circumstances under which a consumer is permitted to breach repayment obligations and cancel payment. However, when the consumer is under insolvency proceedings or subject to proceedings more particularly described under the paragraph below, there are restrictions on enforcing such obligations.

Under Indian law, in terms of the Insolvency and Bankruptcy Code, 2016 ("**IBC**"), once the National Company Law Tribunal ("**Adjudicating Authority**") has admitted the application filed for corporate insolvency resolution of a company or a limited liability partnership, a moratorium or a standstill period shall commence and all the payment obligations shall remain suspended until the completion of such corporate insolvency resolution process. Further, if the Adjudicating Authority approves a corporate insolvency resolution plan or passes an order for liquidation, then the enforcement of obligations against the company would be subject to such plan or order.

1.3 Government Receivables. Where the receivables contract has been entered into with the government or a government agency, are there different requirements and laws that apply to the sale or collection of those receivables?

The legal provisions applicable to the sale and collection of receivables due from the government, are the same as those applicable to other receivables. However, in relation to enforcement proceedings we note that the government officers may have immunity for criminal breach of trust provisions.

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2 Choice of Law – Receivables Contracts

2.1 No Law Specified. If the seller and the obligor do not specify a choice of law in their receivables contract, what are the main principles in your jurisdiction that will determine the governing law of the contract?

The key tests for determining jurisdiction under Indian law, in any recovery of debt action where jurisdiction has not been agreed upon, would be the place of business of the debtor and the place where the subject matter of the dispute, being the debt, is located.

2.2 Base Case. If the seller and the obligor are both resident in your jurisdiction, and the transactions giving rise to the receivables and the payment of the receivables take place in your jurisdiction, and the seller and the obligor choose the law of your jurisdiction to govern the receivables contract, is there any reason why a court in your jurisdiction would not give effect to their choice of law?

Such choice of law would be recognised by Indian courts under all circumstances.

2.3 Freedom to Choose Foreign Law of Non-Resident Seller or Obligor. If the seller is resident in your jurisdiction but the obligor is not, or if the obligor is resident in your jurisdiction but the seller is not, and the seller and the obligor choose the foreign law of the obligor/seller to govern their receivables contract, will a court in your jurisdiction give effect to the choice of foreign law? Are there any limitations to the recognition of foreign law (such as public policy or mandatory principles of law) that would typically apply in commercial relationships such as that between the seller and the obligor under the receivables contract?

In a situation where a receivables contract is governed by foreign law and one of the parties to the transaction is located in India, the choice of foreign law would be recognised by Indian courts; provided that the jurisdiction chosen as the governing law is the law of the domicile of the non-Indian party or is a neutral venue. In the event that the intention is that the receivables contract should be interpreted in accordance with foreign law by courts in India, so long as the foreign law in question is not contrary to laws applicable in India and is not opposed to public policy, the courts in India would interpret the contract accordingly; however, in such a case foreign law must be established before a court of law in India, as any other question of fact. Further, if the award of a court located in a foreign jurisdiction is sought to be enforced in India, Indian courts may not permit such enforcement if the obligation being enforced is contrary to Indian law or contrary to public policy.

3 Choice of Law – Receivables Purchase Agreement

3.1 Base Case. Does your jurisdiction's law generally require the sale of receivables to be governed by the same law as the law governing the receivables themselves? If so, does that general rule apply irrespective of which law governs the receivables (i.e., your jurisdiction's laws or foreign laws)?

There is no requirement under Indian law that the law governing the receivables contract should be the same law which governs the sale of receivables transaction. However, if the debtor, the originator and the assignee are located in India and the receivables are due in respect of the goods sold or services rendered in India, it would be practical to keep the jurisdiction as India so as to avoid any conflict of law issues.

3.2 Example 1: If (a) the seller and the obligor are located in your jurisdiction, (b) the receivable is governed by the law of your jurisdiction, (c) the seller sells the receivable to a purchaser located in a third country, (d) the seller and the purchaser choose the law of your jurisdiction to govern the receivables purchase agreement, and (e) the sale complies with the requirements of your jurisdiction, will a court in your jurisdiction recognise that sale as being effective against the seller, the obligor and other third parties (such as creditors or insolvency administrators of the seller and the obligor)?

While the technical answer to this question is yes, given that under foreign exchange laws in India, sale of receivables to a foreign person/entity is restricted, the transaction itself could be challenged for being in violation of the foreign exchange laws, unless the prior consent of the RBI has been obtained or the same is permitted in terms of the extant RBI regulations including the Master Circular on Rupee/Foreign Currency Export Credit & Customer Service to Exporters.

3.3 Example 2: Assuming that the facts are the same as Example 1, but either the obligor or the purchaser or both are located outside your jurisdiction, will a court in your jurisdiction recognise that sale as being effective against the seller and other third parties (such as creditors or insolvency administrators of the seller), or must the foreign law requirements of the obligor's country or the purchaser's country (or both) be taken into account?

Such a sale would be effective against the seller, however, if the purchaser or the obligor is located outside India; such a transaction would fall under the purview of foreign exchange laws and it would be necessary to analyse whether RBI approval would be required for such a transaction.

3.4 Example 3: If (a) the seller is located in your jurisdiction but the obligor is located in another country, (b) the receivable is governed by the law of the obligor's country, (c) the seller sells the receivable to a purchaser located in a third country, (d) the seller and the purchaser choose the law of the obligor's country to govern the receivables purchase agreement, and (e) the sale complies with the requirements of the obligor's country, will a court in your jurisdiction recognise that sale as being effective against the seller and other third parties (such as creditors or insolvency administrators of the seller) without the need to comply with your jurisdiction's own sale requirements?

This sale would be effective against the seller, subject to restrictions noted in questions 3.2 and 3.3 above. For such a sale to be effective against the creditors of the seller/liquidator appointed in an insolvency proceeding of the seller, the sale must comply with the sale requirements under Indian law, including applicable accounting standards.

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3.5 Example 4: If (a) the obligor is located in your jurisdiction but the seller is located in another country, (b) the receivable is governed by the law of the seller's country, (c) the seller and the purchaser choose the law of the seller's country to govern the receivables purchase agreement, and (d) the sale complies with the requirements of the seller's country, will a court in your jurisdiction recognise that sale as being effective against the obligor and other third parties (such as creditors or insolvency administrators of the obligor) without the need to comply with your jurisdiction's own sale requirements?

Such a sale, if carried out in compliance with foreign exchange laws, would be effective against the obligor and any person claiming through the obligor, including the creditors/insolvency administrators of the obligor.

3.6 Example 5: If (a) the seller is located in your jurisdiction (irrespective of the obligor's location), (b) the receivable is governed by the law of your jurisdiction, (c) the seller sells the receivable to a purchaser located in a third country, (d) the seller and the purchaser choose the law of the purchaser's country to govern the receivables purchase agreement, and (e) the sale complies with the requirements of the purchaser's country, will a court in your jurisdiction recognise that sale as being effective against the seller and other third parties (such as creditors or insolvency administrators of the seller, any obligor located in your jurisdiction and any third party creditor or insolvency administrator of any such obligor)?

Please see our response to question 3.4 above.

4 Asset Sales

4.1 Sale Methods Generally. In your jurisdiction what are the customary methods for a seller to sell receivables to a purchaser? What is the customary terminology – is it called a sale, transfer, assignment or something else?

For an originator to sell receivables, the common method is to execute an assignment agreement/deed of assignment. In certain cases where the obligor is also involved in the assignment transaction, a novation agreement is also common. These transactions could be referred to as sale/transfer/assignment/novation/factoring.

4.2 Perfection Generally. What formalities are required generally for perfecting a sale of receivables? Are there any additional or other formalities required for the sale of receivables to be perfected against any subsequent good faith purchasers for value of the same receivables from the seller?

When perfecting the sale of receivables, the following formalities need to be complied with: (i) if the receivables are secured by any immovable property, then the instrument evidencing the sale of receivables and underlying security interest need to be registered with the relevant sub-registrar of assurances; (ii) if the receivables are due from a company incorporated in India, and any charge has been created over assets of any company to secure the receivables, the transfer of the receivables would amount to a modification of charge and may have to be filed with the relevant registrar of companies; and (iii) if the transaction in question is a factoring transaction (being a transaction of assignment of receivables from a corporate to a factor governed by the Factoring Regulation Act, 2011) then (A) the obligor must be notified of the transfer for the assignee to be able to directly claim from the obligor, and (B) the transaction must also be registered with the Central Registry set up under the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002.

Apart from the above, stamp duty and registration fees also need to be paid, which is dealt with in the responses to the questions in section 9 below.

Further, if the assignor has contractually agreed with the debtor to provide notice of, or take consent for, assignment or any other covenant, then the same will have to be complied with.

4.3 Perfection for Promissory Notes, etc. What additional or different requirements for sale and perfection apply to sales of promissory notes, mortgage loans, consumer loans or marketable debt securities?

Sale of promissory notes would happen by way of endorsement and, where the endorsement is in favour of the acquirer, the only formality required for the same is delivery of the endorsed promissory note to the acquirer. For requirements in relation to the sale of mortgage loans and consumer loans, please see our response to question 4.2 above. For transfer of marketable debt securities the formalities differ if they are in physical form or dematerialised form. If the securities are in dematerialised form, which is quite common in India now, instructions must be provided to the depository, where such securities are held, for effecting such transfer. If the securities are in physical form, the transfer form as stipulated by the issuer of the securities must be executed and submitted to the issuer for its records.

4.4 Obligor Notification or Consent. Must the seller or the purchaser notify obligors of the sale of receivables in order for the sale to be effective against the obligors and/or creditors of the seller? Must the seller or the purchaser obtain the obligors' consent to the sale of receivables in order for the sale to be an effective sale against the obligors? Whether or not notice is required to perfect a sale, are there any benefits to giving notice – such as cutting off obligor set-off rights and other obligor defences?

For the transfer of receivables, unless otherwise provided for in the receivables contract, there is no requirement for providing notice to, or obtaining the consent of, the obligor, unless the transaction is a factoring transaction, in which case the obligor needs to be informed of the transaction if the assignee wants to directly enforce the payment obligations against the obligor.

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4.5 Notice Mechanics. If notice is to be delivered to obligors, whether at the time of sale or later, are there any requirements regarding the form the notice must take or how it must be delivered? Is there any time limit beyond which notice is ineffective – for example, can a notice of sale be delivered after the sale, and can notice be delivered after insolvency proceedings have commenced against the obligor or the seller? Does the notice apply only to specific receivables or can it apply to any and all (including future) receivables? Are there any other limitations or considerations?

There is no evolved separate law or principle regarding the manner of issuance of notice and, as stated under question 4.4 above, notice mechanics would generally be governed by the receivables contract.

4.6 Restrictions on Assignment – General Interpretation. Will a restriction in a receivables contract to the effect that "None of the [seller's] rights or obligations under this Agreement may be transferred or assigned without the consent of the [obligor]" be interpreted as prohibiting a transfer of receivables by the seller to the purchaser? Is the result the same if the restriction says "This Agreement may not be transferred or assigned by the [seller] without the consent of the [obligor]" (i.e., the restriction does not refer to rights or obligations)? Is the result the same if the restriction says "The obligations of the [seller] under this Agreement may not be transferred or assigned by the [seller] without the consent of the [obligor]" (i.e., the restriction does not refer to rights)?

If the clause is worded in the first and second manner, it would be interpreted to mean that no transfer is possible without permission of the obligor. If the clause is worded in the third manner, and no other clauses in the receivables contract restrict assignment of receivables, then the receivables can be assigned under Indian contract law without obtaining the consent of the obligor.

4.7 Restrictions on Assignment; Liability to Obligor. If any of the restrictions in question 4.6 are binding, or if the receivables contract explicitly prohibits an assignment of receivables or "seller's rights" under the receivables contract, are such restrictions generally enforceable in your jurisdiction? Are there exceptions to this rule (e.g., for contracts between commercial entities)? If your jurisdiction recognises restrictions on sale or assignment of receivables and the seller nevertheless sells receivables to the purchaser, will either the seller or the purchaser be liable to the obligor for breach of contract or tort, or on any other basis?

The contracting parties' agreement as to restrictions on assignment of receivables or 'seller's rights' under the receivables contract would generally be upheld by Indian courts, and unless other circumstances require it, no distinction would be made where the parties are commercial entities. Remedies for breach of contract in India are twofold, one being specific performance and the other being damages. The general rule is that specific performance will not be awarded if damages would be sufficient to remedy the breach. Therefore, if a seller in breach of the receivables contract transfers the receivables without providing notice to or obtaining the consent of the obligor, and if the breach can be remedied by damages being paid to the obligor, there will be no consequence of such a breach to the purchaser of the receivables. However, if damages will not be sufficient to remedy such a breach, which can be established if the restriction on the transfer was inserted with an intent that the obligor did not want to deal with anyone other than the transferor or that the obligor did not want any other person to have knowledge of the receivables contract, then specific performance would be awarded in which the transfer itself can be held to be void and the parties to the transfer held liable for damages resulting to the obligor as a consequence thereof. In this regard if any confidentiality obligations have been breached, damages under tort could also be imposed.

4.8 Identification. Must the sale document specifically identify each of the receivables to be sold? If so, what specific information is required (e.g., obligor name, invoice number, invoice date, payment date, etc.)? Do the receivables being sold have to share objective characteristics? Alternatively, if the seller sells *all* of its receivables to the purchaser, is this sufficient identification of receivables? Finally, if the seller sells *all* of its receivables *other than* receivables owing by one or more specifically identified obligors, is this sufficient identification of receivables?

It would be advisable to identify the receivables being sold, rather than state 'all receivables' or 'all receivables except certain receivables'. Under Indian law, if receivables have not been generated, a sale of the same cannot be effected, i.e., future receivables (being receivables in respect of which there is no existing obligation to pay) cannot be transferred.

Further, if the loans are being transferred by a financial institution, the sale must be of a homogenous pool of assets. What would constitute a homogenous pool of assets has not been set out by the RBI, however, where certain common characteristics such as the size of loan disbursed, residual tenure of loans, etc. can be established, this test would be met.

4.9 Recharacterisation Risk. If the parties describe their transaction in the relevant documents as an outright sale and explicitly state their intention that it be treated as an outright sale, will this description and statement of intent automatically be respected or is there a risk that the transaction could be characterised by a court as a loan with (or without) security? If recharacterisation risk exists, what characteristics of the transaction might prevent the transfer from being treated as an outright sale? Among other things, to what extent may the seller retain any of the following without jeopardising treatment as an outright sale: (a) credit risk; (b) interest rate risk; (c) control of collections of receivables; (d) a right of repurchase/redemption; (e) a right to the residual profits within the purchaser; or (f) any other term?

For a valid sale under Indian law, one must look into the economic characteristics of the transaction, as an asset can be derecognised from the books of accounts of the seller only once the substantial risks and rewards associated with the asset have been transferred and other criteria with respect to the 'true sale' of the asset, as set out under the RBI's guidelines of 2006 (as amended from time to time) for governing securitisation of standard assets by banks and non-banking financial companies ("NBFCs"), have been met. Even if the parties describe their transaction in the relevant documents as an outright sale, in the case that the 'true sale' criteria as identified above is not met and the assets are not derecognised from the books of accounts of the seller, the transaction would be recharacterised as a collateralised loan.

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The seller cannot retain any credit risk other than in the form of credit enhancement (in the case of a securitisation transaction regulated by the RBI), unless the seller is a bank or an NBFC, in which case the seller has a regulatory requirement to hold a minimum percentage (up to a maximum of 10%) in the asset. The credit enhancement to be made available by the seller in a securitisation transaction should generally not go beyond 20% of the asset assigned (after taking into consideration the minimum retention already held by the seller).

The seller cannot retain any interest rate risk other than to the extent of the minimum retention. If there are excess cashflows generated from the asset due to the pricing from the purchaser being less than the pricing stated in the receivables contract, the excess cashflows can be utilised to set off the interest rate risk.

The seller can continue to collect the receivables, however, the assignee should have the power to remove the seller as the collection agent. The key analysis to be carried out when determining whether servicing obligations can vitiate the validity of the sale is as follows: (i) has the seller undertaken certain additional responsibilities, including recourse responsibilities, which a third-party servicer would not undertake; and (ii) is the seller being adequately compensated for its services for acting as a servicer.

The seller can retain residual cashflows and this would not impact the sale.

While the seller can exercise a clean-up call option once the receivable value has reduced to 10%, any other buyback arrangement would defeat the sale arrangement and could result in the transaction being treated as a collateralised loan.

4.10 Continuous Sales of Receivables. Can the seller agree in an enforceable manner to continuous sales of receivables (i.e., sales of receivables as and when they arise)? Would such an agreement survive and continue to transfer receivables to the purchaser following the seller's insolvency?

Such an agreement would be valid and enforceable, however, the sale will come into effect only once the receivables have arisen and therefore if a charge exists in favour of the creditors of the seller and over all assets of the seller, then each time such receivables arise the consent of the creditor would be required for such transfer. Please see our response to question 6.5 below on the effect of a seller's insolvency in dealing with assets of the seller.

4.11 Future Receivables. Can the seller commit in an enforceable manner to sell receivables to the purchaser that come into existence after the date of the receivables purchase agreement (e.g., "future flow" securitisation)? If so, how must the sale of future receivables be structured to be valid and enforceable? Is there a distinction between future receivables that arise prior to *versus* after the seller's insolvency?

Since sales under Indian law can only be of receivables in existence, such an agreement may not be enforceable. However, subject to the appropriate consents being taken from the creditors and the monitoring of tax liabilities (which if unpaid can attach onto the assets) of the seller and the employee liabilities (which if unpaid can attach onto the assets) of the seller, an appropriate structure can be evolved for achieving this. Please see our response to question 6.5 below on the effect of a seller's insolvency on dealing with assets of the seller.

4.12 Related Security. Must any additional formalities be fulfilled in order for the related security to be transferred concurrently with the sale of receivables? If not all related security can be enforceably transferred, what methods are customarily adopted to provide the purchaser the benefits of such related security?

If the underlying security comprises of immovable property, then the transfer must happen by way of a written instrument, and the assignment document needs to be registered with the relevant sub-registrar of interest for such security interests to stand transferred to the purchaser. Further, if the obligor is a company, then a modification of charge also needs to be filed with the relevant registrar of companies. However, since obligors are not informed of the assignment, in many cases, this modification of charge with the registrar of companies is not recorded. The consequences of such non-filing, is that the purchaser's charge, pursuant to the assignment, may not be enforceable against the liquidator of the obligor or creditors of the obligor. To mitigate this risk, in most assignment documents, clauses are set out to ensure that charge filings shall continue in the name of the seller for the benefit of the purchaser and that, when required, the seller will join in enforcement action so that the purchaser gets the benefit of the charge. Further, a power of attorney is also issued by the seller in favour of the purchaser in some cases, to ensure that the purchaser can take enforcement action in the name of the seller without disclosing the assignment.

4.13 Set-Off; Liability to Obligor. Assuming that a receivables contract does not contain a provision whereby the obligor waives its right to set-off against amounts it owes to the seller, do the obligor's set-off rights terminate upon its receipt of notice of a sale? At any other time? If a receivables contract does not waive set-off but the obligor's set-off rights are terminated due to notice or some other action, will either the seller or the purchaser be liable to the obligor for damages caused by such termination?

The general principle of assignment is that the same terms and conditions which governed the assignor and the obligor will govern the relationship between the assignee and the obligor. The right of set-off would generally be available in a recovery proceeding for debt under Indian law, however, such set-off can be exercised only between the debtor and the creditor. For example, if there is no provision under the receivables contract permitting set-off, then the obligor will not be able to exercise any set-off against the monies due to the assignee, even though there are dues from the assignor to the obligor, so long as the assignment is carried out in compliance with the receivables contract and there are no dues from the assignee to the obligor. However, it would be advisable to ensure that the assignee has clawback rights against the assignor if the obligor exercises any such set-off, as long as such clawback right would not vitiate the validity of the sale.

Further, the seller and the purchaser will not have any liability to the obligor other than in terms of the receivables contract.

4.14 Profit Extraction. What methods are typically used in your jurisdiction to extract residual profits from the purchaser?

The common forms of profit extraction are the flowing back of residual cashflows and the incentive-based servicing fee. The flow back of residual cashflows is not permitted in a regulated

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bilateral assignment transaction and is only permitted in a regulated securitisation transaction; therefore in a regulated bilateral assignment transaction, a possible profit extraction method would be to charge a different interest for the retained portion or to levy a fee for collection and enforcement, which is based on the actual collections realised.

5 Security Issues

5.1 Back-up Security. Is it customary in your jurisdiction to take a "back-up" security interest over the seller's ownership interest in the receivables and the related security, in the event that an outright sale is deemed by a court (for whatever reason) not to have occurred and have been perfected (see question 4.9 above)?

This is not customary and having such back-up security interest could result in the transaction being seen as a collateralised loan.

5.2 Seller Security. If it is customary to take back-up security, what are the formalities for the seller granting a security interest in receivables and related security under the laws of your jurisdiction, and for such security interest to be perfected?

This is not customary; however, if at all such security is required to be created, then a deed of hypothecation must be executed to create a charge over the receivables in favour of the purchaser. Furthermore, this charge will have to be registered with the registrar of companies where the seller's registered office is located.

5.3 Purchaser Security. If the purchaser grants security over all of its assets (including purchased receivables) in favour of the providers of its funding, what formalities must the purchaser comply with in your jurisdiction to grant and perfect a security interest in purchased receivables governed by the laws of your jurisdiction and the related security?

Please see our response to question 5.2 above.

5.4 Recognition. If the purchaser grants a security interest in receivables governed by the laws of your jurisdiction, and that security interest is valid and perfected under the laws of the purchaser's jurisdiction, will the security be treated as valid and perfected in your jurisdiction or must additional steps be taken in your jurisdiction?

This will be treated as valid and perfected in India if the sale of receivables have been entered into in compliance with Indian laws.

5.5 Additional Formalities. What additional or different requirements apply to security interests in or connected to insurance policies, promissory notes, mortgage loans, consumer loans or marketable debt securities?

Depending on the kind of security interest being created, the formalities that must be complied with are charge filings with the Central Registry set-up under the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002, charge filings with the registrar of companies and with the sub-registrar of assurances. Additionally with respect to insurance policies and demand promissory notes, assuming that the originator does not continue to act as the collection and servicing agent, it would also be advisable to transfer the benefit of the same by way of endorsement.

5.6 Trusts. Does your jurisdiction recognise trusts? If not, is there a mechanism whereby collections received by the seller in respect of sold receivables can be held or be deemed to be held separate and apart from the seller's own assets (so that they are not part of the seller's insolvency estate) until turned over to the purchaser?

Trusts are recognised under Indian law under the Indian Trusts Act, 1882.

5.7 Bank Accounts. Does your jurisdiction recognise escrow accounts? Can security be taken over a bank account located in your jurisdiction? If so, what is the typical method? Would courts in your jurisdiction recognise a foreign law grant of security (for example, an English law debenture) taken over a bank account located in your jurisdiction?

Indian law recognises escrow accounts. Security can be taken over a bank account in India. The typical process for this is to mark a lien over the bank account and the monies lying to the credit thereof in the records of the bank. Additionally, in some cases a hypothecation is also created over the bank account and the monies lying to the credit thereof, through a deed of hypothecation and this document is filed with the relevant registrar of companies.

Further, since bankers have a general lien over bank accounts, unless they have contracted to the contrary, it would be advisable to get the charge over the bank account recognised by the bank itself and obtain an express declaration waiving its lien over the bank account.

For a security over an asset owned by an Indian person to be valid in an Indian court of law, the security creation procedure stipulated under Indian law must be complied with.

5.8 Enforcement over Bank Accounts. If security over a bank account is possible and the secured party enforces that security, does the secured party control all cash flowing into the bank account from enforcement forward until the secured party is repaid in full, or are there limitations? If there are limitations, what are they?

Save for and except for the bank lien discussed above, which can be overcome in the manner also discussed above, so long as the security provider is not under bankruptcy proceedings, post enforcement the charge holder will have sole access to cashflows that come into the account, provided the cashflows have no other security created thereon. If the security provider is under winding up proceedings, the charge over the account may have to be shared with outstanding statutory dues of the security provider and the claims of employees of the security provider.

5.9 Use of Cash Bank Accounts. If security over a bank account is possible, can the owner of the account have access to the funds in the account prior to enforcement without affecting the security?

If the charge is being operated through an escrow mechanism and the escrow agreement permits such an access to the owner, only then

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will the owner have access; otherwise the owner would require the consent of the charge beneficiary for any operation.

6 Insolvency Laws

6.1 Stay of Action. If, after a sale of receivables that is otherwise perfected, the seller becomes subject to an insolvency proceeding, will your jurisdiction's insolvency laws automatically prohibit the purchaser from collecting, transferring or otherwise exercising ownership rights over the purchased receivables (a "stay of action")? If so, what generally is the length of that stay of action? Does the insolvency official have the ability to stay collection and enforcement actions until he determines that the sale is perfected? Would the answer be different if the purchaser is deemed to only be a secured party rather than the owner of the receivables?

Once a sale of receivables has been perfected, even if the seller was made subject to insolvency proceedings, the purchaser's right to the receivables would remain unaffected. However, if the seller was acting as a collection agent, the administrator appointed in the insolvency proceeding would take over the collection agency function, unless the same is terminated by the purchaser. Having stated the above, if the insolvency officials are questioning the validity of the sale itself, then there is a possibility that until the same is determined, the purchaser's right to collect the receivables would be dependent on the court's determination of the case put forward by the insolvency official regarding validity of the sale. If the purchaser was to be treated as a secured creditor, the purchaser would be more affected by the insolvency of the seller, regarding recovery from the obligor, than in a situation where the sale has been perfected.

6.2 Insolvency Official's Powers. If there is no stay of action, under what circumstances, if any, does the insolvency official have the power to prohibit the purchaser's exercise of its ownership rights over the receivables (by means of injunction, stay order or other action)?

There are no grounds other than as specified under question 6.3 below, that a purchaser, claiming under a perfected sale, can be prevented by the insolvency official from recovering the monies from the obligors.

6.3 Suspect Period (Clawback). Under what facts or circumstances could the insolvency official rescind or reverse transactions that took place during a "suspect" or "preference" period before the commencement of the seller's insolvency proceedings? What are the lengths of the "suspect" or "preference" periods in your jurisdiction for (a) transactions between unrelated parties, and (b) transactions between related parties? If the purchaser is majority-owned or controlled by the seller or an affiliate of the seller, does that render sales by the seller to the purchaser "related party transactions" for purposes of determining the length of the suspect period? If a parent company of the seller guarantee's the performance by the seller of its obligations under contracts with the purchaser, does that render sales by the seller to the purchaser "related party transactions" for purposes of determining the length of the suspect period?

The law pertaining to the suspect period in India is codified under Section 328 and 329 of the Companies Act 2013 and Section 43 and 45 of the IBC.

If winding up of the seller commences (or is deemed to have commenced) under the Companies Act 2013, within six months of the transaction being entered into, then the assignment of the assets may be assailed on the grounds of 'fraudulent preference' as provided under Section 328 of the Companies Act 2013. However, in such a case, it may have to be first established that the assignment was made in favour of a creditor (or a surety or a guarantor in respect of any of the liabilities of the company under winding up), and not made in favour of a *bona fide* transferee or for valuable consideration. Section 328 of the Companies Act 2013 has been notified recently and it is yet to be seen how the courts/tribunals will interpret the term 'preference transfer' as used in the provision.

If winding up of the seller commences (or is deemed to have commenced) under the Companies Act 2013, within a period of one year of the transaction being entered into, then the assignment of the assets may be assailed on the ground that the same is void under the provisions of Section 329 of the Companies Act 2013. However, in such a case, it has to be first established that the transfer was not made, either in the ordinary course of business of the seller, or in good faith and for valuable consideration.

If the corporate insolvency resolution process of the seller commences (or is deemed to have commenced in accordance with the IBC) within one year of the transaction being entered into, then the assignment of the assets may be assailed on the grounds of 'preferential transactions' as provided under Section 43 of the IBC. However, in such a case, it has to be first established that the assignment was made in favour of a creditor or guarantor or a surety on account of an antecedent or financial or operational debt or liability of the seller and has not been made in the ordinary course of business.

If the corporate insolvency resolution process of the seller commences (or is deemed to have commenced in accordance with IBC) within one year of the transaction being entered into, then the assignment of the assets may be assailed on the grounds of an 'undervalued transaction' pursuant to Section 45 of the IBC. However, in such a case, the liquidator has to first establish that the assignment was made for a consideration, which is significantly lower than the value of the assets and was not made in the ordinary course of business.

If the purchaser is majority-owned or controlled by the seller or an affiliate of the seller, the sale transaction would be treated as a 'related party transaction'. If a parent company of the seller guarantees the performance by the seller of its obligations under contracts with the purchaser, this would not necessarily be treated as a related party transaction, however, under RBI guidelines governing securitisation, all group companies are also considered as 'originators' and therefore the guarantee provided by the parent, would be seen as recourse made available by the originator and accordingly the sale transaction itself could be recharacterised as a collateralised loan.

6.4 Substantive Consolidation. Under what facts or circumstances, if any, could the insolvency official consolidate the assets and liabilities of the purchaser with those of the seller or its affiliates in the insolvency proceeding? If the purchaser is owned by the seller or by an affiliate of the seller, does that affect the consolidation analysis?

The only circumstance under which this can happen is if the courts were to pierce the corporate veil of the seller and the purchaser and determine that they were always acting as one entity with common

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interests. However, it is in very rare circumstances that a court would pierce the corporate veil and for this to happen it will have to be established that the seller was effectively being controlled by the purchaser or *vice versa*. Therefore, if the purchaser is owned by the seller or an affiliate of the seller, the question regarding whether the corporate veil of the purchaser should be pierced would need to be addressed.

6.5 Effect of Insolvency on Receivables Sales. If insolvency proceedings are commenced against the seller in your jurisdiction, what effect do those proceedings have on (a) sales of receivables that would otherwise occur after the commencement of such proceedings, or (b) on sales of receivables that only come into existence after the commencement of such proceedings?

Once the insolvency proceedings have commenced in India against the seller (being a company or a limited liability partnership), there shall be a moratorium or standstill period with respect to dealing with assets of the seller until the completion of the corporate insolvency resolution process and thereafter, the assets of the seller shall be subject to the conditions laid down in the corporate insolvency resolution plan or order for liquidation, as passed by the Adjudicating Authority.

6.6 Effect of Limited Recourse Provisions. If a debtor's contract contains a limited recourse provision (see question 7.3 below), can the debtor nevertheless be declared insolvent on the grounds that it cannot pay its debts as they become due?

If the contract clearly stipulates that the debtor is liable only up to a certain amount of the debt and that there is no recourse on the debtor for the balance, the debtor cannot be declared insolvent if the portion of debt that the debtor is contractually bound by has been discharged.

7 Special Rules

7.1 Securitisation Law. Is there a special securitisation law (and/or special provisions in other laws) in your jurisdiction establishing a legal framework for securitisation transactions? If so, what are the basics? Is there a regulatory authority responsible for regulating securitisation transactions in your jurisdiction?

The Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 ("**Securitisation Act**") is an act that has been introduced to specifically deal with the securitisation of assets and the enforcement of security interests. The Securitisation Act, in relation to securitisation, deals with asset reconstruction companies ("**ARCs**") that can acquire financial assets from financial institutions (which are banks and certain notified NBFCs currently). We note that the Securitisation Act has mostly been used in relation to the assignment of stressed assets, as the debt recovery provisions which are made available to ARCs under the Securitisation Act are very favourable. The Securitisation Act, however, does not govern securitisation transactions conducted by entities governed by guidelines for securitisation, which have been issued by the RBI.

The RBI has formulated guidelines in 2006 and modified the same in 2012 for governing securitisation of standard assets by banks and NBFCs. In 2005, the RBI formulated guidelines for assignment of non-performing assets for banks and NBFCs which are consolidated in the RBI's Master Circular on 'Prudential Norms on Income Recognition, Asset Classification and Provisioning pertaining to Advances'. The national housing board, which governs housing finance companies, has also adopted similar guidelines.

However, there is no single regulatory authority responsible for regulating all securitisation transactions in India.

The key concepts under the securitisation guidelines of the RBI, relating to standard assets, are:

1. True Sale: This sets out, in detail, the parameters which would determine whether a sale has been perfected.
2. Securitisation Special Purpose Vehicle ("**SPV**"): This requires that every securitisation transaction is routed through an SPV, engaged with no other activity. The SPV could be in the form of a trust or a company. However, given the tax inefficiencies for using companies for this purpose, mostly only trusts are used for securitisation transactions in India.
3. Servicing: This deals with the role of servicing that the originator can undertake and the limits thereof.
4. Credit Enhancement: This deals with how credit enhancement can be made available and limits thereof.
5. Minimum Holding Period: This sets out that all assets need to be held by the originator for a minimum period before being securitised.
6. Minimum Retention Requirement: It sets out that the originator should continue to stay invested in the assets to a certain extent (between 5–10%).
7. Accounting Treatment: It sets out the accounting treatment with respect to securitisation transactions.

7.2 Securitisation Entities. Does your jurisdiction have laws specifically providing for establishment of special purpose entities for securitisation? If so, what does the law provide as to: (a) requirements for establishment and management of such an entity; (b) legal attributes and benefits of the entity; and (c) any specific requirements as to the status of directors or shareholders?

The Securitisation Act specifically deals with the licensing of ARCs and how they will conduct business. The requirements for establishing and managing such an entity are: (i) they should be registered under the companies law; (ii) they should be registered with the RBI; and (iii) for the purposes of such registration with the RBI, the RBI will, *inter alia*, consider (A) profit and loss track record, (B) existing appropriate mechanisms for the recovery of financial assets, and (C) whether the directors have adequate experience. The benefit of being registered as an ARC under the Securitisation Act, is that, amongst others, the ARC: (i) has access to the beneficial recovery provisions under the Securitisation Act; (ii) is able to access insurance companies, mutual funds, etc. for raising monies to invest in financial assets which these investors are not permitted to invest in directly; and (iii) is exempted from: (A) stamp duty, in case the document is executed by any bank or financial institution in favour of the ARC acquiring financial assets for the purposes of asset reconstruction or securitisation; and (B) registration requirements, in respect of transfer of underlying security interests which comprise immovable property.

Apart from the above, in the context of securitisation of standard assets, the RBI in the guidelines referred to in question 7.1 above, stipulates the following key conditions to be met by the securitisation entity: (A) transactions between the originator and the SPV should be on an arm's-length basis; (B) there should be no resemblance

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in name between the SPV and the originator; (C) the SPV should be independent of the originator; (D) for every four directors in the SPV, the originator is entitled to appoint only one without veto power; and (E) the trust deed should clearly set out the role and function of the SPV. Other than tax certainty, there are no benefits of being a SPV under the RBI securitisation guidelines.

7.3 Location and form of Securitisation Entities. Is it typical to establish the special purpose entity in your jurisdiction or offshore? If in your jurisdiction, what are the advantages to locating the special purpose entity in your jurisdiction? If offshore, where are special purpose entities typically located for securitisations in your jurisdiction? What are the forms that the special purpose entity would normally take in your jurisdiction and how would such entity usually be owned?

Typically, the special purpose entity is established onshore, as setting up the same in an offshore jurisdiction would require additional approvals under applicable foreign exchange laws.

See our response to question 7.2 above for the requirements on form and ownership of an ARC. SPVs are normally structured as a special purpose non-discretionary trust. Generally, the trustee itself acts as the settlor and settles the trust for the benefit of the investors and appoints itself as the trustee. While the legal ownership of such an entity vests with the trustee, the powers of the trustee are always exercised based on instructions provided by the investors and accordingly the investors control the voting rights in the entity.

7.4 Limited-Recourse Clause. Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) limiting the recourse of parties to that agreement to the available assets of the relevant debtor, and providing that to the extent of any shortfall the debt of the relevant debtor is extinguished?

Indian law would normally give effect to this contractual position, however, in the event that the debtor has issued non-convertible debentures and contractually carved out personal liability and limited recourse only to certain assets, given that a debenture is an absolute debt obligation, there is a likely chance that the courts would require such a debtor to discharge the balance part of the debt also.

7.5 Non-Petition Clause. Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) prohibiting the parties from: (a) taking legal action against the purchaser or another person; or (b) commencing an insolvency proceeding against the purchaser or another person?

Since the right to commence legal proceedings can be seen as a fundamental right, it is unlikely that a court in India would uphold such a contractual provision, especially where the purchaser is in default.

7.6 Priority of Payments "Waterfall". Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) distributing payments to parties in a certain order specified in the contract?

Such a contract should be enforceable, however, in the event of the winding up of the entity to whom these monies belong to, preferred statutory payments will also have to be made.

7.7 Independent Director. Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) or a provision in a party's organisational documents prohibiting the directors from taking specified actions (including commencing an insolvency proceeding) without the affirmative vote of an independent director?

If this is included in the organisational documents, Indian courts should recognise such a contractual provision.

7.8 Location of Purchaser. Is it typical to establish the purchaser in your jurisdiction or offshore? If in your jurisdiction, what are the advantages to locating the purchaser in your jurisdiction? If offshore, where are purchasers typically located for securitisations in your jurisdiction?

Typically, the purchaser is established onshore as setting up the same in an offshore jurisdiction would require additional approvals under applicable foreign exchange laws. However, the RBI has permitted Foreign Portfolio Investors ("**FPIs**"), to participate as investors in securitisation transactions and therefore, the ultimate beneficiaries of the Securitisation Trusts set up in India, could be located in offshore jurisdictions. Given that FPIs have not made many investments in securitisation transactions, there is not enough data available to make an assessment on which is a preferred jurisdiction.

8 Regulatory Issues

8.1 Required Authorisations, etc. Assuming that the purchaser does no other business in your jurisdiction, will its purchase and ownership or its collection and enforcement of receivables result in its being required to qualify to do business or to obtain any licence or its being subject to regulation as a financial institution in your jurisdiction? Does the answer to the preceding question change if the purchaser does business with more than one seller in your jurisdiction?

Other than compliance with foreign exchange laws, a purchaser will not be required to obtain any licence solely on the account of purchasing receivables. However, if the purchaser is engaged in other business also, then it will have to be analysed whether registration as an NBFC is required and whether the purchaser is a factor governed by the Factoring Regulation Act, 2011. The test for determining whether an entity is an NBFC is whether the entity has assets in the form of financial assets which exceed 50% of the total assets and income from financial assets which exceed 50% of the total income. The test for determining whether an entity is a factor is whether the entity is in the business of acquisition of receivables of an assignor (i.e. owner of receivables), unless it is only carrying out securitisation transactions or other exempt business under the provisions of the Factoring Regulation Act, 2011.

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8.2 Servicing. Does the seller require any licences, etc., in order to continue to enforce and collect receivables following their sale to the purchaser, including to appear before a court? Does a third-party replacement servicer require any licences, etc., in order to enforce and collect sold receivables?

There are no specific licences required for acting as a servicing agent, however, given the number of people employed and the offices used for performing such services, general licences and registrations related to employment and business would have to be looked into.

8.3 Data Protection. Does your jurisdiction have laws restricting the use or dissemination of data about or provided by obligors? If so, do these laws apply only to consumer obligors or also to enterprises?

While the Information Technology Act 2000 does impose damages for any misuse of personal data, there are no specific laws pertaining to the use or dissemination of data about or provided by obligors. Further, the RBI has also issued detailed guidelines regarding the use of customer information.

8.4 Consumer Protection. If the obligors are consumers, will the purchaser (including a bank acting as purchaser) be required to comply with any consumer protection law of your jurisdiction? Briefly, what is required?

Not specifically, other than the general principle that unless a consumer is notified of an assignment he cannot be held responsible for the performance towards the seller. Further, all rights available to a consumer against the original creditor will also be available against the purchaser.

8.5 Currency Restrictions. Does your jurisdiction have laws restricting the exchange of your jurisdiction's currency for other currencies or the making of payments in your jurisdiction's currency to persons outside the country?

Yes, this is governed by the Foreign Exchange Management Act, 1999.

8.6 Risk Retention. Does your jurisdiction have laws or regulations relating to "risk retention"? How are securitisation transactions in your jurisdiction usually structured to satisfy those risk retention requirements?

The RBI securitisation guidelines prescribe a minimum retention requirement of 5–10% of the assets being securitised, where the seller is a bank or an NBFC. There is no law or regulation requiring risk retention for other securitisation transactions.

The choice is left to the seller to fulfil risk retention requirement either through investment in the securities issued by the SPV or through the provision of credit enhancement. Normally, this is met through the provision of first loss credit enhancement and if that is not sufficient, by subscribing to senior tranches.

8.7 Regulatory Developments. Have there been any regulatory developments in your jurisdiction which are likely to have a material impact on securitisation transactions in your jurisdiction?

Apart from the evolution of jurisprudence around the IBC, given that it was introduced only in 2016, there are no regulatory developments which can materially impact securitisation transactions. The indirect tax regime in India has been overhauled in July 2017 and the goods and services tax ("**GST**") has been introduced which could impact the pricing of the receivables contract itself (between non-financial entities).

9 Taxation

9.1 Withholding Taxes. Will any part of payments on receivables by the obligors to the seller or the purchaser be subject to withholding taxes in your jurisdiction? Does the answer depend on the nature of the receivables, whether they bear interest, their term to maturity, or where the seller or the purchaser is located? In the case of a sale of trade receivables at a discount, is there a risk that the discount will be recharacterised in whole or in part as interest? In the case of a sale of trade receivables where a portion of the purchase price is payable upon collection of the receivable, is there a risk that the deferred purchase price will be recharacterised in whole or in part as interest? If withholding taxes might apply, what are the typical methods for eliminating or reducing withholding taxes?

All payments of interest in respect of receivables could be subject to withholding taxes which have to be deducted at the source in respect of the income of the payee. These taxes would not affect principal payments. In relation to payments made to securitisation trusts, there are currently exemptions given regarding withholding tax *vis-à-vis* payments made to the trust, however, when the trust is making payment to the investors, the trust is required to deduct tax at the source at the rates specified.

In relation to receivables sold at a discount, the discount should not be recharacterised as interest, as interest under tax laws in India has been defined to mean payment made in respect of the sums borrowed.

Deferred purchase consideration is not permissible under the RBI securitisation guidelines governing the securitisation of standard assets, however, if such a deferred payment structure is adopted, then the deferred price should not normally be recharacterised as interest, in whole or in part.

The only exemptions available in relation to withholding taxes, when payments are being made by securitisation trusts to investors, are payments made to entities like mutual fund houses, where there is no requirement under Indian tax laws to deduct tax at the source for payments made to such entities.

9.2 Seller Tax Accounting. Does your jurisdiction require that a specific accounting policy is adopted for tax purposes by the seller or purchaser in the context of a securitisation?

There is no separate accounting requirement for the purposes of taxation, however, the RBI securitisation guidelines and the Indian Accounting Standards set out provisions relating to the manner of accounting in relation to securitisation transactions.

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9.3 Stamp Duty, etc. Does your jurisdiction impose stamp duty or other transfer or documentary taxes on sales of receivables?

Yes, under Indian law, parties will have to be aware of both stamp duty and registration fees. Both differ from state to state and very rarely are laws governing the same under two different state-stamp acts found to have similar provisions.

In relation to exemptions for an ARC's acquisition of financial assets, please see our response to question 7.2 above.

Most of the securitisations today, which are not in favour of ARCs, take place in the states of Maharashtra, Delhi, Rajasthan and West Bengal because of the stamp duty-friendly notifications which govern securitisation transactions.

The stamp duty would also be dependent on the nature of the underlying security interest as mortgage debt is normally considered to be immovable property; the stamp duty for transfer of immovable property could be different from transfer of movable property.

9.4 Value Added Taxes. Does your jurisdiction impose value added tax, sales tax or other similar taxes on sales of goods or services, on sales of receivables or on fees for collection agent services?

In respect of any fee earned in such a transaction, including for providing collection agent services, service tax would be due and payable. There is some confusion, arising because of the recently introduced GST, as to whether the assignment of secured debt could be subject to GST; however, the market view appears to be that these transactions would continue to be exempt from taxation as this would be treated as a transaction in money.

9.5 Purchaser Liability. If the seller is required to pay value-added tax, stamp duty or other taxes upon the sale of receivables (or on the sale of goods or services that give rise to the receivables) and the seller does not pay, then will the taxing authority be able to make claims for the unpaid tax against the purchaser or against the sold receivables or collections?

The only time when the tax authorities would have a claim to the sold assets for liabilities of the seller would be when the sale itself is successfully challenged on, *inter alia*, grounds set out under question 6.3 above. However, if the tax in question is a documentary charge like stamp duty/registration fees, both the seller and the purchaser could be held liable for such documentary charges.

9.6 Doing Business. Assuming that the purchaser conducts no other business in your jurisdiction, would the purchaser's purchase of the receivables, its appointment of the seller as its servicer and collection agent, or its enforcement of the receivables against the obligors, make it liable to tax in your jurisdiction?

It could, especially if the domicile of the purchaser can be established to be India or the business of collection and recovery being conducted by the purchaser, is established to have an India nexus.

9.7 Taxable Income. If a purchaser located in your jurisdiction receives debt relief as the result of a limited recourse clause (see question 7.3 above), is that debt relief liable to tax in your jurisdiction?

There are no separate taxation provisions governing debt relief obtained by a purchaser, however, one must analyse whether any income accrues to the purchaser due to the limited recourse clause and accordingly determine the tax applicable on the debt relief. For example, where the debt relief available to the purchaser is equal to the losses suffered by the purchaser because of non-realisations from the underlying borrowers, then the income from debt relief will be set off by the loss on recovery.

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Indonesia

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Freddy Karyadi

1 Receivables Contracts

1.1 Formalities. In order to create an enforceable debt obligation of the obligor to the seller: (a) is it necessary that the sales of goods or services are evidenced by a formal receivables contract; (b) are invoices alone sufficient; and (c) can a binding contract arise as a result of the behaviour of the parties?

Generally, agreements in Indonesia can be made either in writing or verbally. However, for a debt that arises from a loan agreement, Article 1756 of the Indonesian Civil Code ("**ICC**") stipulates that the payment of a debt shall only be limited to the amount stated in the agreement. Thus, receivables shall be made in an agreement in order to provide clarity. Further, pursuant to Article 1457 of the ICC, a sale and purchase is an agreement where one party binds itself to provide goods and the other party pays the agreed price. Article 1513 of the Indonesian Civil Code further stipulates that the main obligation of the buyer is to pay the purchase price in the place, and at the time, agreed in the agreement. If there is no agreement on the place and time of payment, Article 1514 of the Indonesian Civil Code further regulates that the buyer has to pay at the time of the handover of the goods (levering). Based on this, it can be concluded that for the sale and purchase, the payment for the good/services has to be made at the agreed time or at the time of the levering. Such payment cannot be made in instalments, since it has to be paid at the levering.

Invoices alone are sufficient to be deemed as a binding agreement, as long as the recipient of the invoices has made the payment to the issuer of the invoice. Hence, the recipient of the invoices is deemed to provide his consent to the invoices. Indonesian law also recognises the concept of consent by conduct under Article 1347 of the ICC which stipulates that customary stipulation shall be deemed to be implied in the agreement, notwithstanding that these have not been expressed.

As previously explained, a receivables contract, the nature of which can be deemed as a debt or loan agreement, shall be made based on a binding agreement. Hence, it cannot be deemed to exist as a result of the behaviour of the parties. However, as for other agreements which entitle the seller to receive payment aside from the loan agreement, we believe that a contract might be deemed to exist as a result of the behaviour of the parties (please also refer to our explanation above in relation to Article 1347 of the ICC).

1.2 Consumer Protections. Do your jurisdiction's laws: (a) limit rates of interest on consumer credit, loans or other kinds of receivables; (b) provide a statutory right to interest on late payments; (c) permit consumers to cancel receivables for a specified period of time; or (d) provide other noteworthy rights to consumers with respect to receivables owing by them?

Generally, there are no restrictions on interest on consumer credit, loans or other kinds of receivables. Parties may determine the interest rate mutually. However, it should be noted that in Indonesia a usury law (the "*Woekerordonantie*") is still in force. In addition, save for a credit card, Bank Indonesia limits the interest to a maximum of 2.95% per month. Aside from the limitation of interest, Bank Indonesia (the Indonesian central bank) has imposed significant restrictions on new offshore financing arrangements entered into by non-banking institutions in Indonesia, as stipulated under BI Regulation No. 16/21/PBI/2014 on Prudential Principles in the Management of Offshore Borrowing for Non-Bank Institutions as amended by BI Regulation No. 18/4/PBI/2016 dated 21 April 2016 ("**BI Regulation 18/2016**"), which require Indonesian non-bank borrowers to satisfy certain minimum hedging and liquidity ratios in relation to their external indebtedness.

There is no statutory interest rate on late payments.

There are no noteworthy rights of consumers under the Consumer Protection Law with respect to the receivables that they owe.

1.3 Government Receivables. Where the receivables contract has been entered into with the government or a government agency, are there different requirements and laws that apply to the sale or collection of those receivables?

Yes, additional requirements may apply to the sale or collection of government assets. Article 46 of Law No. 1 of 2004 on State Treasury stipulates that any transfer of a government asset shall obtain approval from the House of Representatives, the president, or the minister of finance. Such approval is determined based on the value of the asset. As for government assets other than land and buildings valued at: (i) more than Rp100 billion shall obtain approval from the House of Representatives; (ii) Rp10 billion up to Rp100 billion shall obtain approval from the president; and (iii) below Rp10 billion shall obtain approval from the minister of finance.

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2 Choice of Law – Receivables Contracts

2.1 No Law Specified. If the seller and the obligor do not specify a choice of law in their receivables contract, what are the main principles in your jurisdiction that will determine the governing law of the contract?

Indonesia acknowledges the concept of the "most characteristic connection" in order to determine the governing law of a contract that does not stipulate a choice of law provision.

2.2 Base Case. If the seller and the obligor are both resident in your jurisdiction, and the transactions giving rise to the receivables and the payment of the receivables take place in your jurisdiction, and the seller and the obligor choose the law of your jurisdiction to govern the receivables contract, is there any reason why a court in your jurisdiction would not give effect to their choice of law?

No, there should be no reason.

2.3 Freedom to Choose Foreign Law of Non-Resident Seller or Obligor. If the seller is resident in your jurisdiction but the obligor is not, or if the obligor is resident in your jurisdiction but the seller is not, and the seller and the obligor choose the foreign law of the obligor/seller to govern their receivables contract, will a court in your jurisdiction give effect to the choice of foreign law? Are there any limitations to the recognition of foreign law (such as public policy or mandatory principles of law) that would typically apply in commercial relationships such as that between the seller and the obligor under the receivables contract?

Generally, Indonesian courts will recognise the parties' choice of law in an agreement as long as it is not contrary to public policy or existing laws and regulations. However, to the extent there is an Indonesian party, an Indonesian court has the right to invalidate the agreement if it is deemed to violate Indonesian law.

3 Choice of Law – Receivables Purchase Agreement

3.1 Base Case. Does your jurisdiction's law generally require the sale of receivables to be governed by the same law as the law governing the receivables themselves? If so, does that general rule apply irrespective of which law governs the receivables (i.e., your jurisdiction's laws or foreign laws)?

No, it does not.

3.2 Example 1: If (a) the seller and the obligor are located in your jurisdiction, (b) the receivable is governed by the law of your jurisdiction, (c) the seller sells the receivable to a purchaser located in a third country, (d) the seller and the purchaser choose the law of your jurisdiction to govern the receivables purchase agreement, and (e) the sale complies with the requirements of your jurisdiction, will a court in your jurisdiction recognise that sale as being effective against the seller, the obligor and other third parties (such as creditors or insolvency administrators of the seller and the obligor)?

Yes, it should recognise the sale. Generally, an agreement must fulfil the requirements under Article 1320 of the ICC to be deemed valid, which are as follows:

1. there must be consent of the individuals who are bound thereby;
2. there must be capacity to conclude an agreement;
3. there must be a specific subject; and
4. there must be an admissible cause.

However, in relation to the transfer of receivables, the following requirements must be made in order to give effect to such transfer: (i) there is an underlying agreement to the sale and purchase; (ii) there is a delivery of the object, in the form of deed of transfer/assignment from the seller to the purchaser; and (iii) there is notice and acknowledgment of the obligor to such transfer of receivables.

3.3 Example 2: Assuming that the facts are the same as Example 1, but either the obligor or the purchaser or both are located outside your jurisdiction, will a court in your jurisdiction recognise that sale as being effective against the seller and other third parties (such as creditors or insolvency administrators of the seller), or must the foreign law requirements of the obligor's country or the purchaser's country (or both) be taken into account?

Please see the answer to question 3.2. An Indonesian court should uphold the choice of Indonesian law by the parties.

3.4 Example 3: If (a) the seller is located in your jurisdiction but the obligor is located in another country, (b) the receivable is governed by the law of the obligor's country, (c) the seller sells the receivable to a purchaser located in a third country, (d) the seller and the purchaser choose the law of the obligor's country to govern the receivables purchase agreement, and (e) the sale complies with the requirements of the obligor's country, will a court in your jurisdiction recognise that sale as being effective against the seller and other third parties (such as creditors or insolvency administrators of the seller) without the need to comply with your jurisdiction's own sale requirements?

Yes. Indonesian law recognises the concept of freedom of contract, which the Indonesian party may freely enter into, to the extent it does not violate the public order. Therefore, if the nexus of the agreement is valid, the court might acknowledge the perfection of the sale and purchase, as regulated by the requirement under the prevailing laws of the chosen governing law.

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3.5 Example 4: If (a) the obligor is located in your jurisdiction but the seller is located in another country, (b) the receivable is governed by the law of the seller's country, (c) the seller and the purchaser choose the law of the seller's country to govern the receivables purchase agreement, and (d) the sale complies with the requirements of the seller's country, will a court in your jurisdiction recognise that sale as being effective against the obligor and other third parties (such as creditors or insolvency administrators of the obligor) without the need to comply with your jurisdiction's own sale requirements?

Yes. Please see the answer to question 3.4 above.

3.6 Example 5: If (a) the seller is located in your jurisdiction (irrespective of the obligor's location), (b) the receivable is governed by the law of your jurisdiction, (c) the seller sells the receivable to a purchaser located in a third country, (d) the seller and the purchaser choose the law of the purchaser's country to govern the receivables purchase agreement, and (e) the sale complies with the requirements of the purchaser's country, will a court in your jurisdiction recognise that sale as being effective against the seller and other third parties (such as creditors or insolvency administrators of the seller, any obligor located in your jurisdiction and any third party creditor or insolvency administrator of any such obligor)?

Yes. Please see the answer to question 3.4 above.

4 Asset Sales

4.1 Sale Methods Generally. In your jurisdiction what are the customary methods for a seller to sell receivables to a purchaser? What is the customary terminology – is it called a sale, transfer, assignment or something else?

The seller and the purchaser will enter into a sale and purchase agreement. The customary terminology for a sale of receivables is "a true sale".

4.2 Perfection Generally. What formalities are required generally for perfecting a sale of receivables? Are there any additional or other formalities required for the sale of receivables to be perfected against any subsequent good faith purchasers for value of the same receivables from the seller?

Please refer to our explanation to question 3.2 above.

4.3 Perfection for Promissory Notes, etc. What additional or different requirements for sale and perfection apply to sales of promissory notes, mortgage loans, consumer loans or marketable debt securities?

Promissory notes

The sales of a promissory note can only be perfected by way of endorsement.

Mortgage loans

A loan secured by a mortgage may be sold in the form of a sale and purchase agreement or an assignment agreement.

Consumer loans

A transfer of a consumer loan can be made in the form of a sale and purchase agreement.

Marketable debt securities

Marketable debt securities ("**MDS**") (which are issued in scripless form), must be transferred from the securities account of the seller to the securities account of the purchaser to be perfected. On the other hand, as for MDS issued in physical form, the perfection shall be made by way of endorsement upon physical delivery.

4.4 Obligor Notification or Consent. Must the seller or the purchaser notify obligors of the sale of receivables in order for the sale to be effective against the obligors and/or creditors of the seller? Must the seller or the purchaser obtain the obligors' consent to the sale of receivables in order for the sale to be an effective sale against the obligors? Whether or not notice is required to perfect a sale, are there any benefits to giving notice – such as cutting off obligor set-off rights and other obligor defences?

Yes. The seller or the purchaser must notify obligors of the sale of receivables in order for the sale to be effective against the obligors.

Article 613 of the ICC stipulates that the assignment or transfer of receivables should be notified to the debtor, or agreed and acknowledged in writing by the debtor.

4.5 Notice Mechanics. If notice is to be delivered to obligors, whether at the time of sale or later, are there any requirements regarding the form the notice must take or how it must be delivered? Is there any time limit beyond which notice is ineffective – for example, can a notice of sale be delivered after the sale, and can notice be delivered after insolvency proceedings have commenced against the obligor or the seller? Does the notice apply only to specific receivables or can it apply to any and all (including future) receivables? Are there any other limitations or considerations?

There is no specific requirement of notice regarding the time or how it must be delivered. However, in order to perfect the sale of receivables and make the transfer binding, the obligor shall be informed promptly that a sale of receivables has taken place.

As for an insolvency proceeding and execution of security, notice to the obligors is provided by the bailiff.

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4.6 Restrictions on Assignment – General Interpretation. Will a restriction in a receivables contract to the effect that "None of the [seller's] rights or obligations under this Agreement may be transferred or assigned without the consent of the [obligor]" be interpreted as prohibiting a transfer of receivables by the seller to the purchaser? Is the result the same if the restriction says "This Agreement may not be transferred or assigned by the [seller] without the consent of the [obligor]" (i.e., the restriction does not refer to rights or obligations)? Is the result the same if the restriction says "The obligations of the [seller] under this Agreement may not be transferred or assigned by the [seller] without the consent of the [obligor]" (i.e., the restriction does not refer to rights)?

Yes, the above provisions can be interpreted that any transfer or assignment of rights or obligations shall obtain consent from the non-transferring party.

4.7 Restrictions on Assignment; Liability to Obligor. If any of the restrictions in question 4.6 are binding, or if the receivables contract explicitly prohibits an assignment of receivables or "seller's rights" under the receivables contract, are such restrictions generally enforceable in your jurisdiction? Are there exceptions to this rule (e.g., for contracts between commercial entities)? If your jurisdiction recognises restrictions on sale or assignment of receivables and the seller nevertheless sells receivables to the purchaser, will either the seller or the purchaser be liable to the obligor for breach of contract or tort, or on any other basis?

Since Indonesia honours the freedom of contract, such restrictions will be acknowledged and enforceable in Indonesia (since it has been agreed by the parties to the contract).

If the seller sells the receivables to the purchaser without any consent from the obligor (not in compliance with the provisions of the contract), the seller shall be liable to the obligor for breach of contract.

4.8 Identification. Must the sale document specifically identify each of the receivables to be sold? If so, what specific information is required (e.g., obligor name, invoice number, invoice date, payment date, etc.)? Do the receivables being sold have to share objective characteristics? Alternatively, if the seller sells *all* of its receivables to the purchaser, is this sufficient identification of receivables? Finally, if the seller sells *all* of its receivables *other than* receivables owing by one or more specifically identified obligors, is this sufficient identification of receivables?

Article 1320 paragraph 3 of the ICC stipulates that an agreement must set out a specific object. Nonetheless, there is no provision or guidance regarding the details of receivables.

However, we believe that the details should include: (i) the name of the obligor; (ii) the amount of receivables; (iii) the underlying agreement of the receivables mentioning the parties, the date of agreement and the number of the agreement (if any); (iv) the payment date; and (v) other specific information, in order to distinguish each of the receivables. This will also apply if the seller sells all of his receivables. The seller should break down which receivables to be sold.

4.9 Recharacterisation Risk. If the parties describe their transaction in the relevant documents as an outright sale and explicitly state their intention that it be treated as an outright sale, will this description and statement of intent automatically be respected or is there a risk that the transaction could be characterised by a court as a loan with (or without) security? If recharacterisation risk exists, what characteristics of the transaction might prevent the transfer from being treated as an outright sale? Among other things, to what extent may the seller retain any of the following without jeopardising treatment as an outright sale: (a) credit risk; (b) interest rate risk; (c) control of collections of receivables; (d) a right of repurchase/redemption; (e) a right to the residual profits within the purchaser; or (f) any other term?

As previously explained, Indonesian law recognises the concept of "freedom of contract". Hence, if the agreement has been duly signed and there are no outstanding conditions that need to be fulfilled, and such agreement has complied with Article 1320 of the ICC, the agreement is binding on the parties to such agreement.

However, for a more sophisticated transaction (i.e. REPO), in the event of a dispute, a court may categorise a REPO transaction as a loan transaction. Therefore, the seller may retain a credit risk and a right of repurchase/redemption.

4.10 Continuous Sales of Receivables. Can the seller agree in an enforceable manner to continuous sales of receivables (i.e., sales of receivables as and when they arise)? Would such an agreement survive and continue to transfer receivables to the purchaser following the seller's insolvency?

Yes. However, the notice and acknowledgment by the debtor still remains.

4.11 Future Receivables. Can the seller commit in an enforceable manner to sell receivables to the purchaser that come into existence after the date of the receivables purchase agreement (e.g., "future flow" securitisation)? If so, how must the sale of future receivables be structured to be valid and enforceable? Is there a distinction between future receivables that arise prior to *versus* after the seller's insolvency?

Yes, the seller can commit; however, once the receivable exists, the sale and purchase agreement should be executed and have the details of the receivable.

As for the distinction in relation to the insolvency event, please refer to question 6.5 below.

4.12 Related Security. Must any additional formalities be fulfilled in order for the related security to be transferred concurrently with the sale of receivables? If not all related security can be enforceably transferred, what methods are customarily adopted to provide the purchaser the benefits of such related security?

Practically, security in Indonesia is made in three forms, depending on the type of assets involved.

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Mortgage

A mortgage is created over an immovable asset. If the receivable is secured by a mortgage and it is transferred, the transferee should register it at the land office and the mortgage certificate should be amended to state the name of the transferee.

Pledge

A pledge is a security interest over tangible or intangible property. If the receivable is secured by a pledge and it is transferred, a notification to the pledgor is necessary to be made in favour of the transferee.

Fiduciary security

A fiduciary security is a security right over movable (tangible or intangible) and immovable property which cannot be secured by a mortgage. If a receivable is secured by a fiduciary security and it is transferred, the transferee should register it at the fiduciary registration office.

4.13 Set-Off; Liability to Obligor. Assuming that a receivables contract does not contain a provision whereby the obligor waives its right to set-off against amounts it owes to the seller, do the obligor's set-off rights terminate upon its receipt of notice of a sale? At any other time? If a receivables contract does not waive set-off but the obligor's set-off rights are terminated due to notice or some other action, will either the seller or the purchaser be liable to the obligor for damages caused by such termination?

In the event a set-off right is not waived in an agreement, such right still remains valid upon the receipt of notice of a sale. As such, a borrower may implement its right to set-off against any amount it owes to the purchaser.

4.14 Profit Extraction. What methods are typically used in your jurisdiction to extract residual profits from the purchaser?

The proceeds of collection less all costs (purchase price + cost of capital + other relevant costs).

5 Security Issues

5.1 Back-up Security. Is it customary in your jurisdiction to take a "back-up" security interest over the seller's ownership interest in the receivables and the related security, in the event that an outright sale is deemed by a court (for whatever reason) not to have occurred and have been perfected (see question 4.9 above)?

It is not common in Indonesia to take a "back-up" security interest, to the extent the sale of receivables and the related security have been perfected.

5.2 Seller Security. If it is customary to take back-up security, what are the formalities for the seller granting a security interest in receivables and related security under the laws of your jurisdiction, and for such security interest to be perfected?

It is not common to take a "back-up" security interest as stipulated in question 5.1.

A security interest in receivables in Indonesia is secured under a fiduciary security. Execution of a deed of fiduciary security and registration to the fiduciary registration office are needed in order to perfect the security.

5.3 Purchaser Security. If the purchaser grants security over all of its assets (including purchased receivables) in favour of the providers of its funding, what formalities must the purchaser comply with in your jurisdiction to grant and perfect a security interest in purchased receivables governed by the laws of your jurisdiction and the related security?

Commonly, receivables are secured under a fiduciary. A fiduciary over receivables should be registered to the fiduciary registration office in order to be perfected.

5.4 Recognition. If the purchaser grants a security interest in receivables governed by the laws of your jurisdiction, and that security interest is valid and perfected under the laws of the purchaser's jurisdiction, will the security be treated as valid and perfected in your jurisdiction or must additional steps be taken in your jurisdiction?

To the extent the purchaser is located in Indonesia, the receivable can be encumbered with fiduciary security then registered and perfected under Indonesian law. Otherwise, the receivable cannot be used as a security under Indonesian laws.

5.5 Additional Formalities. What additional or different requirements apply to security interests in or connected to insurance policies, promissory notes, mortgage loans, consumer loans or marketable debt securities?

Insurance policies

Acknowledgment by the insurer is needed in order to perfect a security interest on insurance policies. In addition, a banker's clause can also be an option for a security interest connected to insurance policies.

Promissory notes

Please see the answer to question 4.3 above.

Mortgage loans

Please see the answer to question 4.3 above.

Consumer loans

Please see the answer to question 4.3 above.

Marketable debt securities

Please see the answer to question 4.3 above.

5.6 Trusts. Does your jurisdiction recognise trusts? If not, is there a mechanism whereby collections received by the seller in respect of sold receivables can be held or be deemed to be held separate and apart from the seller's own assets (so that they are not part of the seller's insolvency estate) until turned over to the purchaser?

The concept of a trust is not recognised under Indonesian law since Indonesian law does not recognise the concept of splitting up ownership (i.e. between ownership of record and beneficial ownership).

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5.7 Bank Accounts. Does your jurisdiction recognise escrow accounts? Can security be taken over a bank account located in your jurisdiction? If so, what is the typical method? Would courts in your jurisdiction recognise a foreign law grant of security (for example, an English law debenture) taken over a bank account located in your jurisdiction?

Yes, escrow accounts are recognised in Indonesia and are usually structured under an escrow agreement.

Yes, security can be taken over a bank account. The typical method of a security over a bank account is a pledge. However, the Fiduciary Registration Office has expressed the view that a bank account cannot be subject to 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 in practice to secure a bank account with a pledge over a bank account.

Yes, an Indonesian court should recognise a foreign law grant of security taken over a bank account.

5.8 Enforcement over Bank Accounts. If security over a bank account is possible and the secured party enforces that security, does the secured party control all cash flowing into the bank account from enforcement forward until the secured party is repaid in full, or are there limitations? If there are limitations, what are they?

Please see the answer to question 5.7.

In practice, a pledge of a bank account is supplemented with a power of attorney to manage a bank account which grants authorisation to the attorney to manage and control all cash flowing into the bank account. The secured party may control all cash flowing into the bank account from enforcement forward until the secured party is repaid in full. However, it should be noted that perfection and enforcement of a pledge of a bank account shall be acknowledged by the bank in advance.

5.9 Use of Cash Bank Accounts. If security over a bank account is possible, can the owner of the account have access to the funds in the account prior to enforcement without affecting the security?

In practice, to access or take action with regard to the pledged account, prior consent from the pledgee shall be obtained.

6 Insolvency Laws

6.1 Stay of Action. If, after a sale of receivables that is otherwise perfected, the seller becomes subject to an insolvency proceeding, will your jurisdiction's insolvency laws automatically prohibit the purchaser from collecting, transferring or otherwise exercising ownership rights over the purchased receivables (a "stay of action")? If so, what generally is the length of that stay of action? Does the insolvency official have the ability to stay collection and enforcement actions until he determines that the sale is perfected? Would the answer be different if the purchaser is deemed to only be a secured party rather than the owner of the receivables?

In relation to the sale of receivables under Indonesian law, the sale of receivables will be deemed as valid if it has fulfilled certain aspects. Please refer to our answer to question 3.2 above.

Normally, there is no stay of action if the seller becomes subject to an insolvency proceeding after the sale of receivable has been perfected. The sale of the receivable may be annulled if the seller commits fraudulent conveyances when it sold the receivable. The cancellation can be done if the seller is aware that the sale of the receivable would damage the interest of the creditor of the seller. In the event the sale happens within the last 12 months before the bankruptcy status of the seller is issued by the commercial court, the seller would be deemed aware of the consequences in question.

If the purchaser is deemed to only be a secured party rather than the owner of the receivables, then the answer will be different. Article 56 of IBL regulates that the right of the secured party to execute its right pursuant to a security agreement is stayed for a period of 90 days as of the announcement of the bankruptcy decision.

6.2 Insolvency Official's Powers. If there is no stay of action, under what circumstances, if any, does the insolvency official have the power to prohibit the purchaser's exercise of its ownership rights over the receivables (by means of injunction, stay order or other action)?

Please refer to our responses to questions 6.1 and 6.3. These relate to fraudulent conveyances.

6.3 Suspect Period (Clawback). Under what facts or circumstances could the insolvency official rescind or reverse transactions that took place during a "suspect" or "preference" period before the commencement of the seller's insolvency proceedings? What are the lengths of the "suspect" or "preference" periods in your jurisdiction for (a) transactions between unrelated parties, and (b) transactions between related parties? If the purchaser is majority-owned or controlled by the seller or an affiliate of the seller, does that render sales by the seller to the purchaser "related party transactions" for purposes of determining the length of the suspect period? If a parent company of the seller guarantee's the performance by the seller of its obligations under contracts with the purchaser, does that render sales by the seller to the purchaser "related party transactions" for purposes of determining the length of the suspect period?

As briefly mentioned earlier, fraudulent conveyances are regulated under the IBL and the ICC.

The IBL states that only the receiver could request for the nullification of a preferential transfer transaction conducted by the debtor before its bankruptcy if such transaction was considered detrimental to the creditors and met the following requirements:

- the preferential transfer was performed by the debtor before it was declared bankrupt;
- the debtor was not obligated by contract (existing obligation) or by law to perform the preferential transfer;
- the preferential transfer prejudiced the creditors' interests; and
- the debtor and such third party had or should have had knowledge that the preferential transfer would prejudice the creditors' interests.

However, in addition to the above, the ICC provides the right of any creditor to request the nullification of preferential transfer. The ICC stipulates that the right exists within a period of five years starting

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from the date when the creditor knew, or should have known, the preferential transfer prejudiced the creditor's interests. Meanwhile, the IBL stipulates that a legal act taken by the debtor up to one year prior to the issuance of a bankruptcy decision which prejudices the rights of the creditors (while such legal act is not compulsory to be carried out by the debtor) could be deemed detrimental to the creditors. However, the IBL does not clearly define any time difference on the length for a "suspect" or "preference" period for a transaction entered into by related or unrelated parties to the bankrupt debtor.

Notwithstanding the above, please be advised that the ICC and the IBL protect a good faith purchaser from a preferential claim. As such, even if the preferential transfer claim on an asset was accepted and the transaction was nullified, purchasing the asset in good faith should be a valid defence for the purchaser to protect the asset from seizure in relation to a preferential transfer claim made by a receiver or creditor.

6.4 Substantive Consolidation. Under what facts or circumstances, if any, could the insolvency official consolidate the assets and liabilities of the purchaser with those of the seller or its affiliates in the insolvency proceeding? If the purchaser is owned by the seller or by an affiliate of the seller, does that affect the consolidation analysis?

There is no consolidation concept in Indonesian bankruptcy law.

6.5 Effect of Insolvency on Receivables Sales. If insolvency proceedings are commenced against the seller in your jurisdiction, what effect do those proceedings have on (a) sales of receivables that would otherwise occur after the commencement of such proceedings, or (b) on sales of receivables that only come into existence after the commencement of such proceedings?

For the purposes of answering this question, we assume that the commencement of proceedings here means the date when the seller is declared bankrupt.

Sales of receivables that would occur after the commencement of the proceeding

After the debtor has been declared bankrupt, all assets of the debtor will be managed by the receiver and the debtor will not have any access to its assets again. Therefore, we believe that it is unlikely that the sale of receivables will be made after the debtor is declared to be bankrupt. However, this will be up to the discretion of the receiver. If the receiver believes that continuing the sale will benefit the other creditors of the bankrupt debtor, then the receiver may continue with the sale.

Sales of receivables that only come into existence after the commencement of the proceeding

Under this scenario, there is a commitment to sell future receivables which has not existed, however, the seller is subsequently declared bankrupt before the receivable exists. Pursuant to Article 36 of IBL, if the declaration of bankruptcy is announced and there is a reciprocal agreement which has not been executed, the counterparty of the debtor may request a certainty on the continuation of the agreement after the declaration of bankruptcy of the debtor. If the receiver has not provided a certainty after a certain period which has been: (a) agreed by the receiver and the counterparty; or (b) assigned by the supervisory judge, then the agreement will be deemed as terminated and the counterparty may claim damages as an unsecured creditor of the bankrupt debtor. Once the receiver believes that continuing the agreement will be beneficial to the other creditors of the bankrupt debtor, then he/she may decide to continue the agreement.

6.6 Effect of Limited Recourse Provisions. If a debtor's contract contains a limited recourse provision (see question 7.3 below), can the debtor nevertheless be declared insolvent on the grounds that it cannot pay its debts as they become due?

The IBL regulates that the requirements for a debtor to be declared bankrupt are: (i) having two creditors or more; and (ii) failing to pay at least one debt which has matured and become payable. The IBL further regulates that the petition for bankruptcy shall be granted if the facts or circumstances summarily prove the fulfilment of the requirement as mentioned above. As such, if the requirements have been fulfilled, we believe that the limited recourse provision should not have any effect on the bankruptcy proceeding. However, this will be subject to the discretion of the panel of judges in the proceeding, who might have their own view as to the nature of the case.

7 Special Rules

7.1 Securitisation Law. Is there a special securitisation law (and/or special provisions in other laws) in your jurisdiction establishing a legal framework for securitisation transactions? If so, what are the basics? Is there a regulatory authority responsible for regulating securitisation transactions in your jurisdiction?

Yes. There are several regulations in Indonesia in relation to securitisation transactions. Below are the regulations in relation to securitisation transactions in capital markets and banking.

Capital market

In a capital market, the regulations in relation to securitisation transactions are as below:

- OJK Regulation No. 65/Pojk.04/2017 dated 21 December 2017 on Guidelines of Issuance and reporting of Monthly Report of Asset-backed Securities ("**EBA**") Collective Investment Contracts;
- OJK Regulation No. 23/POJK.04/2014 dated 19 November 2014 on Guidelines of Issuance and Reporting of EBA in the Form of Participation Letter in the Context of Secondary House Financing; and
- OJK Regulation No. 20/POJK.04/2015 dated 3 November 2015 on Issuance and Requirement of Sharia EBA.

In Indonesia, EBA is issued under an EBA Collective Investment Contract ("**KIK-EBA**"). A KIK-EBA is entered by, and between, an investment manager and a custodian bank of which the investment manager will manage the portfolio and the custodian bank will provide custodian services to the investment manager.

Aside from the investment manager and custodian bank, there are other parties involved, for example, a servicer (usually this role is conducted by the initial creditor (originator)) and a credit enhancer.

Banking

In banking, regulations relating to securitisation are governed by Bank Indonesia Regulation No. 7/4/PBI/2005 on Prudential Principles in Asset Securitisation for Commercial Banks.

This regulation generally governs criteria and requirements of financial assets that can be transferred in relation to the securitisation asset and the function of a bank in securitisation transactions.

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ICC

Article 584 of the ICC stipulates the following:

"*Ownership of assets cannot be acquired in any manner other than by appropriation, attachment, prescription, legal or testamentary succession, and by delivery pursuant to a transfer of legal title, originating from the individual who was entitled to dispose of the property.*"

Article 613 of the ICC stipulates the following:

"*The transfer of registered debts and other intangible assets, shall be effected by using an authentic or private deed, in which the rights to such objects shall be transferred to another individual. Such transfer shall have no consequences with respect to the debtor, until he has been notified thereof, or if he has accepted the transfer in writing or has acknowledged it.*"

Securitisation transactions are regulated and supervised by the Financial Services Authority and Indonesian Central Bank.

7.2 Securitisation Entities. Does your jurisdiction have laws specifically providing for establishment of special purpose entities for securitisation? If so, what does the law provide as to: (a) requirements for establishment and management of such an entity; (b) legal attributes and benefits of the entity; and (c) any specific requirements as to the status of directors or shareholders?

There is no specific regulation for the establishment of a special purpose entity for securitisation; such establishment will generally comply with the Indonesian Company Law.

7.3 Location and form of Securitisation Entities. Is it typical to establish the special purpose entity in your jurisdiction or offshore? If in your jurisdiction, what are the advantages to locating the special purpose entity in your jurisdiction? If offshore, where are special purpose entities typically located for securitisations in your jurisdiction? What are the forms that the special purpose entity would normally take in your jurisdiction and how would such entity usually be owned?

Typically the special purpose entity is established in our jurisdiction. Please note that under the Indonesian law, securitisation is structured under the collective investment contract ("**CIC**") that shall be made before the notary. Based on this structure, the investment manager will purchase the underlying assets from the originator (the one who has the underlying assets). Further, based on the CIC, the investment manager as the one that purchases the assets will issue and offer the EBA to the investor. There are no specific advantages to locating the special purpose entity in our jurisdiction, other than the rules on EBA only regulate the establishment of EBA in our jurisdiction.

7.4 Limited-Recourse Clause. Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) limiting the recourse of parties to that agreement to the available assets of the relevant debtor, and providing that to the extent of any shortfall the debt of the relevant debtor is extinguished?

Normally yes, to the extent there is an Indonesian party or other legal nexus which relates to Indonesia.

7.5 Non-Petition Clause. Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) prohibiting the parties from: (a) taking legal action against the purchaser or another person; or (b) commencing an insolvency proceeding against the purchaser or another person?

Please see the answer to question 7.4 above.

7.6 Priority of Payments "Waterfall". Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) distributing payments to parties in a certain order specified in the contract?

Please see the answer to question 7.4 above.

7.7 Independent Director. Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) or a provision in a party's organisational documents prohibiting the directors from taking specified actions (including commencing an insolvency proceeding) without the affirmative vote of an independent director?

Please see the answer to question 7.4 above.

7.8 Location of Purchaser. Is it typical to establish the purchaser in your jurisdiction or offshore? If in your jurisdiction, what are the advantages to locating the purchaser in your jurisdiction? If offshore, where are purchasers typically located for securitisations in your jurisdiction?

The purchaser is typically established in our jurisdiction for a securitisation transaction. The main benefit to having the purchaser in Indonesia is that it results in an easier process for collecting the receivable as well as lowering withholding tax upon interest paid by the obligor *vis-à-vis* withholding tax upon interest paid to an offshore purchaser.

8 Regulatory Issues

8.1 Required Authorisations, etc. Assuming that the purchaser does no other business in your jurisdiction, will its purchase and ownership or its collection and enforcement of receivables result in its being required to qualify to do business or to obtain any licence or its being subject to regulation as a financial institution in your jurisdiction? Does the answer to the preceding question change if the purchaser does business with more than one seller in your jurisdiction?

No licences are required to the extent that the purchaser is (i) solely purchasing and holding the receivables, and (ii) not established as a permanent legal entity in Indonesia.

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8.2 Servicing. Does the seller require any licences, etc., in order to continue to enforce and collect receivables following their sale to the purchaser, including to appear before a court? Does a third-party replacement servicer require any licences, etc., in order to enforce and collect sold receivables?

Please see the answer to question 8.1 above. A third-party replacement servicer is not required to hold any licences in order to enforce and collect sold receivables to the extent it is solely purchasing and holding the receivables and does not intend to establish a permanent legal entity in Indonesia.

8.3 Data Protection. Does your jurisdiction have laws restricting the use or dissemination of data about or provided by obligors? If so, do these laws apply only to consumer obligors or also to enterprises?

Indonesia does not have specific regulations regarding data protection. However, Law No. 7 of 1992 on Banking as amended by Law No. 10 of 1998 provides that a bank has bank secrecy obligations which require it to keep the confidentiality of any information regarding the depositor and his deposit. Meanwhile, information concerning debt is not deemed as confidential information and may be released.

Further, if the utilisation of information relating to personal data is made through electronic media, Law No. 11 of 2008 on Information and Electronic Transaction will apply where it requires such utilisation to be based on approval by the respective person.

8.4 Consumer Protection. If the obligors are consumers, will the purchaser (including a bank acting as purchaser) be required to comply with any consumer protection law of your jurisdiction? Briefly, what is required?

To the extent the agreement has been duly signed and has complied with the prevailing regulations and no continuing obligations need to be fulfilled, we believe that consumer protection law should not have any impact on the agreement.

8.5 Currency Restrictions. Does your jurisdiction have laws restricting the exchange of your jurisdiction's currency for other currencies or the making of payments in your jurisdiction's currency to persons outside the country?

There are no restrictions or requirements which limit the availability or transfer of foreign currency except that, pursuant to Regulation of Bank Indonesia number 18/18/PBI/2016 dated 5 September 2016 on Foreign Exchange Transactions Against Rupiah between Banks and Domestic Parties, the conversion of Indonesian Rupiah to foreign currencies or the purchase of foreign currency in the amount of more than US$100,000 per month (or its equivalent) per customer (including the purchase of foreign currencies for derivative transactions) must be based on an underlying transaction, with a maximum amount required under the underlying transaction. In addition, the party purchasing the above-stated foreign currencies is required to submit the following documents to the bank making the conversion:

(i) a copy of the underlying agreement that can be accounted for, both the final and estimated form;

(ii) supporting documents in the form of a copy of customer's ID and Tax Registration Number for Indonesian parties (known as NPWP); and

(iii) a written statement from the party purchasing the foreign currencies which contains information on: (i) the authenticity and validity of the underlying transaction and the utilisation of underlying transaction documents, for the purpose of foreign currencies against Rupiah, shall not exceed the nominal value of the underlying transaction in the banking system in Indonesia; and (ii) the total needs, purpose of utilisation, and date of foreign currencies utilisation, in case the underlying transaction documents is in estimated form.

8.6 Risk Retention. Does your jurisdiction have laws or regulations relating to "risk retention"? How are securitisation transactions in your jurisdiction usually structured to satisfy those risk retention requirements?

There is no specific law that regulates "risk retention". Please see our answer to question 7.3 above on the structure of securitisation in Indonesia.

8.7 Regulatory Developments. Have there been any regulatory developments in your jurisdiction which are likely to have a material impact on securitisation transactions in your jurisdiction?

No, there have been no such regulatory developments.

9 Taxation

9.1 Withholding Taxes. Will any part of payments on receivables by the obligors to the seller or the purchaser be subject to withholding taxes in your jurisdiction? Does the answer depend on the nature of the receivables, whether they bear interest, their term to maturity, or where the seller or the purchaser is located? In the case of a sale of trade receivables at a discount, is there a risk that the discount will be recharacterised in whole or in part as interest? In the case of a sale of trade receivables where a portion of the purchase price is payable upon collection of the receivable, is there a risk that the deferred purchase price will be recharacterised in whole or in part as interest? If withholding taxes might apply, what are the typical methods for eliminating or reducing withholding taxes?

(a) If the obligors are Indonesian tax residents, the interest portion of the receivables would be subject to withholding tax.

(b) It does not depend on the nature of the receivables or the location of the seller or the purchaser.

(c) Yes, there is.

(d) Yes, there is.

9.2 Seller Tax Accounting. Does your jurisdiction require that a specific accounting policy is adopted for tax purposes by the seller or purchaser in the context of a securitisation?

Yes, it does.

9.3 Stamp Duty, etc. Does your jurisdiction impose stamp duty or other transfer or documentary taxes on sales of receivables?

Yes, it does.

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9.4 Value Added Taxes. Does your jurisdiction impose value added tax, sales tax or other similar taxes on sales of goods or services, on sales of receivables or on fees for collection agent services?

Yes, it does.

9.5 Purchaser Liability. If the seller is required to pay value-added tax, stamp duty or other taxes upon the sale of receivables (or on the sale of goods or services that give rise to the receivables) and the seller does not pay, then will the taxing authority be able to make claims for the unpaid tax against the purchaser or against the sold receivables or collections?

No, it will not.

9.6 Doing Business. Assuming that the purchaser conducts no other business in your jurisdiction, would the purchaser's purchase of the receivables, its appointment of the seller as its servicer and collection agent, or its enforcement of the receivables against the obligors, make it liable to tax in your jurisdiction?

No, unless the withholding tax is imposed by the seller upon the sale.

9.7 Taxable Income. If a purchaser located in your jurisdiction receives debt relief as the result of a limited recourse clause (see question 7.3 above), is that debt relief liable to tax in your jurisdiction?

Yes, it is.

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Mr. Freddy Karyadi joined ABNR as Senior Associate in July 2007 and became a Partner on 1 January 2012. He read law at the University of Indonesia (1998) and Leiden University, majoring in International Tax Law (2002). He also graduated *cum laude* in 1997 from the Faculty of Economics of Trisakti University in Jakarta. He has participated in various training and seminars in Indonesia and abroad. Prior to joining ABNR, he worked for a number of years in other prominent law firms in Jakarta. In 2010, he was seconded to Loyens & Loeffs, Amsterdam Office, a prominent Dutch law firm. His special practice areas are capital market, M&A, taxation, banking and corporate finance matters. He has represented numerous financial institutions, banks, private equity and funds, and multinational companies.

He is a member of the editorial board of Derivatives and Financial Instrument Journal, International Bureau of Fiscal Documentation, the Netherlands and is the regional correspondent for the Indonesia jurisdiction for Tax Notes International of Virginia, United States. He also contributes articles to the *International Financial Law Review* and a number of national tax magazines, teaches in several universities and is a regular speaker at seminars and training. In addition to being an advocate and tax attorney, he is also a registered accountant (Ak) and a licensed tax consultant (brevet C).

Ali Budiardjo, Nugroho, Reksodiputro (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 ground-breaking 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).

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Ireland

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1 Receivables Contracts

1.1 Formalities. In order to create an enforceable debt obligation of the obligor to the seller: (a) is it necessary that the sales of goods or services are evidenced by a formal receivables contract; (b) are invoices alone sufficient; and (c) can a binding contract arise as a result of the behaviour of the parties?

To be enforceable against the obligor, a debt obligation need not be evidenced by a formal written contract, but must be evidenced as a matter of contract or deed. Contracts may be written, oral or partly written and partly oral. An invoice could itself constitute the contract between the seller and obligor if the standard elements of a contract are present. Where a contract is oral, evidence of the parties' conduct may be used in determining the terms of the contract. A "binding contract" may also be implied based on a course of conduct or dealings between the parties.

1.2 Consumer Protections. Do your jurisdiction's laws: (a) limit rates of interest on consumer credit, loans or other kinds of receivables; (b) provide a statutory right to interest on late payments; (c) permit consumers to cancel receivables for a specified period of time; or (d) provide other noteworthy rights to consumers with respect to receivables owing by them?

Consumer credit agreements are regulated by the Consumer Credit Act 1995 (as amended) (the **CCA**) and the European Communities (Consumer Credit Agreements) Regulations 2010 (as amended) (the **CCA Regulations**).

There is no statutory interest rate cap, but under the CCA if the cost of credit under a credit agreement is excessive it may be unenforceable. In addition, pursuant to Section 149 of the CCA a "credit institution" (as defined under the CCA) must notify the Central Bank of Ireland (the **CBI**) of any increase of any existing charge it imposes on its customers (or any new charge not previously notified to the CBI) and the CBI may direct the credit institution to refrain from imposing or changing the charge.

There is no statutory right to interest on late payments, but contractual "default interest" may be imposed (as long as the rate of such default interest is not so high as to constitute a penalty).

If a consumer credit agreement does not comply with the requirements of the CCA, the creditor may not be able to enforce it. Certain clauses in a receivables contract with a consumer could be also found to be unfair under the European Communities (Unfair Terms in Consumer Contracts) Regulations 1995 (the **UTCCR Regulations**) and hence unenforceable.

The Consumer Protection Code (the **CPC**) of the CBI also imposes obligations on "regulated entities" in their dealings with their "customers". The Consumer Protection Act 2007 contains a general prohibition on unfair, misleading, aggressive and prohibited trading practices that could result in a contract with a consumer being rendered void or unenforceable.

1.3 Government Receivables. Where the receivables contract has been entered into with the government or a government agency, are there different requirements and laws that apply to the sale or collection of those receivables?

Under the Prompt Payments of Accounts Act 1997, all Irish public bodies and contractors on public sector contracts must pay amounts due to their suppliers promptly (i.e. on or before the due date in the contract or, if there is no due date (or no written contract), within 45 days of receipt of the invoice or delivery of the global servicers).

In certain circumstances, enforceability of receivables contracts with the government/a government agency could potentially be an issue as a result of the law of sovereign immunity.

2 Choice of Law – Receivables Contracts

2.1 No Law Specified. If the seller and the obligor do not specify a choice of law in their receivables contract, what are the main principles in your jurisdiction that will determine the governing law of the contract?

Contracts entered into on or after 17 December 2009 will be governed by Regulation (EC) 593/2008 of 17 June 2008 (**Rome I**). Contracts entered into prior to 17 December 2009 will be subject to the Contractual Obligations (Applicable Law) Act 1991, pursuant to which the Rome convention on the law applicable to contractual obligations (the **Rome Convention**) was enacted in Ireland.

Under Rome I in the absence of an express choice of law in a contract, the applicable law of the contract will be that of the country with which it has the "closest connection", which is the country where the party who is to perform the contract has its habitual residence or its central administration (unless the contract is within one of a number of defined classes for which specific rules apply, or is manifestly more closely connected with the law of a different country, or if it is sufficiently certain from the terms or circumstances of the contract which law the parties intended to apply).

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Similarly, under the Rome Convention the applicable law of a contract is presumed to be that of the country with which the contract has the "closest connection" (i.e. the country where the party performing the contract has its habitual residence or its central administration). However, if the contract is a commercial or professional contract, the applicable law will be the law of the place in which the principal place of business of the party performing the contract is situated or, where performance is to be effected through a place of business other than the principal place of business of that party, the country in which that other place of business is situated.

If the contract falls outside the scope of Rome I or the Rome Convention, Irish common law principles will determine the applicable law by reference to the parties' intentions. If the parties' intention cannot be established, the applicable law will be the law with which the contract has its "closest and most real connection".

2.2 Base Case. If the seller and the obligor are both resident in your jurisdiction, and the transactions giving rise to the receivables and the payment of the receivables take place in your jurisdiction, and the seller and the obligor choose the law of your jurisdiction to govern the receivables contract, is there any reason why a court in your jurisdiction would not give effect to their choice of law?

In those circumstances the Irish courts should give effect to the choice of Irish law.

2.3 Freedom to Choose Foreign Law of Non-Resident Seller or Obligor. If the seller is resident in your jurisdiction but the obligor is not, or if the obligor is resident in your jurisdiction but the seller is not, and the seller and the obligor choose the foreign law of the obligor/seller to govern their receivables contract, will a court in your jurisdiction give effect to the choice of foreign law? Are there any limitations to the recognition of foreign law (such as public policy or mandatory principles of law) that would typically apply in commercial relationships such as that between the seller and the obligor under the receivables contract?

As discussed above, Rome I and the Rome Convention provide that the parties to a contract may freely choose the law of their contract and that choice is generally only overridden if it conflicts with mandatory rules or public policy. Contracts falling outside the scope of Rome I or the Rome Convention will be subject to standard Irish common law principles which also generally support the parties' right to choose the governing law of their contract and will only displace their choice in exceptional circumstances.

3 Choice of Law – Receivables Purchase Agreement

3.1 Base Case. Does your jurisdiction's law generally require the sale of receivables to be governed by the same law as the law governing the receivables themselves? If so, does that general rule apply irrespective of which law governs the receivables (i.e., your jurisdiction's laws or foreign laws)?

Irish law does not require the sale of receivables to be governed by the law governing the receivables themselves. Whether under Rome I, the Rome Convention or general principles of Irish common law, the parties to a contract can (subject to certain exceptions) choose the law of any country to govern the contract, irrespective of the law governing the receivable.

However, whether a receivable has been validly sold and whether such sale has been perfected will generally be a matter for the law governing the receivable and not the law governing the receivables sale agreement. Furthermore, the enforceability of the receivables against the obligor may be determined by the law of the jurisdiction in which the obligor is located.

3.2 Example 1: If (a) the seller and the obligor are located in your jurisdiction, (b) the receivable is governed by the law of your jurisdiction, (c) the seller sells the receivable to a purchaser located in a third country, (d) the seller and the purchaser choose the law of your jurisdiction to govern the receivables purchase agreement, and (e) the sale complies with the requirements of your jurisdiction, will a court in your jurisdiction recognise that sale as being effective against the seller, the obligor and other third parties (such as creditors or insolvency administrators of the seller and the obligor)?

Yes, it should.

3.3 Example 2: Assuming that the facts are the same as Example 1, but either the obligor or the purchaser or both are located outside your jurisdiction, will a court in your jurisdiction recognise that sale as being effective against the seller and other third parties (such as creditors or insolvency administrators of the seller), or must the foreign law requirements of the obligor's country or the purchaser's country (or both) be taken into account?

See section 2 and question 3.1 above. In addition, under Rome I and the Rome Convention, laws other than the governing law of the receivables purchase agreement may sometimes be taken into account. For instance, where a contract is governed by Irish law but will be performed in a place other than Ireland, the Irish courts might apply certain mandatory provisions of the law of the country where the contract is to be performed (if the contract would be otherwise rendered unlawful in that country).

3.4 Example 3: If (a) the seller is located in your jurisdiction but the obligor is located in another country, (b) the receivable is governed by the law of the obligor's country, (c) the seller sells the receivable to a purchaser located in a third country, (d) the seller and the purchaser choose the law of the obligor's country to govern the receivables purchase agreement, and (e) the sale complies with the requirements of the obligor's country, will a court in your jurisdiction recognise that sale as being effective against the seller and other third parties (such as creditors or insolvency administrators of the seller) without the need to comply with your jurisdiction's own sale requirements?

As per Section 2 and questions 3.1 and 3.3 above, under Rome I and the Rome Convention where there is an express choice of law by the parties to a contract, the Irish courts should recognise the choice of law and assess the validity of the contract in accordance with the law chosen by the parties.

However, certain mandatory principles of Irish law cannot be disapplied and the courts might not apply the parties' chosen law to the extent it conflicted with those mandatory principles.

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3.5 Example 4: If (a) the obligor is located in your jurisdiction but the seller is located in another country, (b) the receivable is governed by the law of the seller's country, (c) the seller and the purchaser choose the law of the seller's country to govern the receivables purchase agreement, and (d) the sale complies with the requirements of the seller's country, will a court in your jurisdiction recognise that sale as being effective against the obligor and other third parties (such as creditors or insolvency administrators of the obligor) without the need to comply with your jurisdiction's own sale requirements?

Yes. See section 2 and questions 3.1, 3.3 and 3.4 above.

3.6 Example 5: If (a) the seller is located in your jurisdiction (irrespective of the obligor's location), (b) the receivable is governed by the law of your jurisdiction, (c) the seller sells the receivable to a purchaser located in a third country, (d) the seller and the purchaser choose the law of the purchaser's country to govern the receivables purchase agreement, and (e) the sale complies with the requirements of the purchaser's country, will a court in your jurisdiction recognise that sale as being effective against the seller and other third parties (such as creditors or insolvency administrators of the seller, any obligor located in your jurisdiction and any third party creditor or insolvency administrator of any such obligor)?

Yes. See section 2 and questions 3.1, 3.3, 3.4 and 3.5 above.

4 Asset Sales

4.1 Sale Methods Generally. In your jurisdiction what are the customary methods for a seller to sell receivables to a purchaser? What is the customary terminology – is it called a sale, transfer, assignment or something else?

In Ireland receivables are most commonly sold by way of equitable (or legal) assignment. Other methods which are more rarely used include: a declaration of trust over the receivables (or over the proceeds of the receivables), a sub-participation or a novation. An outright sale of receivables may be described as a "sale", a "transfer" or an "assignment", although "assignment" often indicates a transfer of the rights in respect of the receivables (and not the obligations), while a "transfer" often indicates a transfer of both rights and obligations by way of novation. The phrase "security assignment" is often used to distinguish a transfer by way of security from an outright assignment.

4.2 Perfection Generally. What formalities are required generally for perfecting a sale of receivables? Are there any additional or other formalities required for the sale of receivables to be perfected against any subsequent good faith purchasers for value of the same receivables from the seller?

A sale of receivables by way of an outright legal assignment is perfected by the delivery of notice in writing of the sale to the obligor(s) of the relevant receivables in accordance with the requirements of Section 28(6) of the Supreme Court of Judicature (Ireland) Act 1877 (the **Judicature Act**). The provision of notice does not in itself result in the transfer becoming a legal (as opposed to an equitable) assignment as certain other formalities are also required; namely, the assignment must be: (i) in writing under the hand of the assignor; (ii) of the whole of the debt; and (iii) absolute and not by way of charge. If the assignment does not fulfil all these requirements, it will likely take effect as an equitable assignment so that any subsequent assignment effected by the seller which is fully compliant with the Judicature Act requirements will take priority, if notified to the obligor prior to the date on which the original assignment is notified to the obligor.

A novation of receivables (i.e. of both the rights and obligations in respect of such receivables) requires the written consent of the obligor, the seller and the purchaser.

4.3 Perfection for Promissory Notes, etc. What additional or different requirements for sale and perfection apply to sales of promissory notes, mortgage loans, consumer loans or marketable debt securities?

The transfer requirements for promissory notes (as well as other negotiable instruments) are governed by the Bills of Exchange Act 1882, which provides that they are transferable by delivery (or delivery and endorsement).

Mortgage loans and their related mortgages may be transferred by way of assignment. For a mortgage over real property in order to effect a full legal (rather than just equitable) assignment, the transfer will need to be registered at the Land Registry or the Registry of Deeds (depending on whether the land is registered or unregistered). Most residential mortgage-backed securitisation transactions are structured as an equitable assignment of mortgage loans and their related mortgages to avoid having to give notice to the underlying mortgagors and to register the transfer. Under the CBI's Code of Conduct on the Transfer of Mortgages (if applicable), a loan secured by a mortgage of residential property may not be transferred without the written consent of the borrower (the relevant consent is usually obtained under the mortgage origination documentation).

Questions 8.3 and 8.4 below outline some of the regulatory requirements in relation to consumer loans. Under the CCA Regulations, a consumer must be provided with notice of any transfer by the creditor of its loan, except where the original creditor continues to service the credit. Under the CPC where part of a regulated business is transferred by a regulated entity (including a transfer of consumer loans) at least two months' notice must be provided to affected consumers if the transfer is to another regulated entity (and one month if it is not).

Marketable debt securities in bearer form may be transferred by delivery and endorsement; in registered form, by registration of the transferee in the relevant register. Dematerialised marketable securities may be transferred by debiting the clearing system account of the purchaser (or its custodian or nominee/intermediary).

4.4 Obligor Notification or Consent. Must the seller or the purchaser notify obligors of the sale of receivables in order for the sale to be effective against the obligors and/or creditors of the seller? Must the seller or the purchaser obtain the obligors' consent to the sale of receivables in order for the sale to be an effective sale against the obligors? Whether or not notice is required to perfect a sale, are there any benefits to giving notice – such as cutting off obligor set-off rights and other obligor defences?

A seller or purchaser need not notify the obligors to effect a valid equitable sale of the receivables (which would be effective against

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the seller). However, in order for a legal sale of the receivables to be effected (enforceable against both the seller and the underlying obligor) written notice would need to be provided to the underlying obligor. Ideally, from an evidentiary perspective, the underlying obligor would acknowledge the notice, but the obligors' consent is not required for the sale to be effective against them.

If notice is not provided, the assignment will only be equitable and: (i) obligors can discharge their debts by paying the seller; (ii) obligors may set off claims against the seller even if they accrue after the assignment; (iii) a subsequent assignee without notice of the prior assignment would take priority over the claims of the initial purchaser; and (iv) the purchaser cannot sue the obligor in its own name, but must join the seller as co-plaintiff.

4.5 Notice Mechanics. If notice is to be delivered to obligors, whether at the time of sale or later, are there any requirements regarding the form the notice must take or how it must be delivered? Is there any time limit beyond which notice is ineffective – for example, can a notice of sale be delivered after the sale, and can notice be delivered after insolvency proceedings have commenced against the obligor or the seller? Does the notice apply only to specific receivables or can it apply to any and all (including future) receivables? Are there any other limitations or considerations?

See also the response above to question 4.3.

Notice must be in writing and given to the obligor at the time of, or after the sale (preferably after), but there is no particular form specified. The notice should clearly state that the obligor must pay the assignee (the purchaser) from then on.

There is no specific time limit for the giving of notices set down in the Judicature Act and notice can be given to obligors post-insolvency of the obligor or the seller (including pursuant to an irrevocable power of attorney granted by the seller). The notice should only apply to specific receivables.

4.6 Restrictions on Assignment – General Interpretation. Will a restriction in a receivables contract to the effect that "None of the [seller's] rights or obligations under this Agreement may be transferred or assigned without the consent of the [obligor]" be interpreted as prohibiting a transfer of receivables by the seller to the purchaser? Is the result the same if the restriction says "This Agreement may not be transferred or assigned by the [seller] without the consent of the [obligor]" (i.e., the restriction does not refer to rights or obligations)? Is the result the same if the restriction says "The obligations of the [seller] under this Agreement may not be transferred or assigned by the [seller] without the consent of the [obligor]" (i.e., the restriction does not refer to rights)?

Either of the first two formulations would likely be interpreted by an Irish court as prohibiting a transfer of relevant receivables by the seller to the purchaser (see our response to question 4.7 below).

In the last instance, the seller will implicitly have the authority to assign its rights to a purchaser (but not its obligations), as in the absence of an express contractual prohibition on the assignment of rights, the receivables may be assigned without the obligor's consent.

4.7 Restrictions on Assignment; Liability to Obligor. If any of the restrictions in question 4.6 are binding, or if the receivables contract explicitly prohibits an assignment of receivables or "seller's rights" under the receivables contract, are such restrictions generally enforceable in your jurisdiction? Are there exceptions to this rule (e.g., for contracts between commercial entities)? If your jurisdiction recognises restrictions on sale or assignment of receivables and the seller nevertheless sells receivables to the purchaser, will either the seller or the purchaser be liable to the obligor for breach of contract or tort, or on any other basis?

Restrictions on assignment or transfers of receivables are generally enforceable in Ireland. As noted in question 4.6 above, if a contract is silent on the question of assignment, then it (and the receivables arising thereunder) will normally be freely assignable. If an assignment is effected in breach of a contractual prohibition on assignment, it will be ineffective as between the obligor, the seller and the purchaser, but should still be effective as between the seller and purchaser.

4.8 Identification. Must the sale document specifically identify each of the receivables to be sold? If so, what specific information is required (e.g., obligor name, invoice number, invoice date, payment date, etc.)? Do the receivables being sold have to share objective characteristics? Alternatively, if the seller sells *all* of its receivables to the purchaser, is this sufficient identification of receivables? Finally, if the seller sells *all* of its receivables *other than* receivables owing by one or more specifically identified obligors, is this sufficient identification of receivables?

The sale document must specify the receivables being sold with sufficient clarity that they are identifiable and distinguishable from the rest of the seller's assets. The receivables being sold need not share objective characteristics but normally a portfolio of receivables being sold is all of the same type. To our knowledge, the scenario has not been considered by the Irish courts but a purported sale of all of a seller's receivables other than those owing by specifically identified obligors might be effective if the contract sufficiently identifies the receivables not being sold.

4.9 Recharacterisation Risk. If the parties describe their transaction in the relevant documents as an outright sale and explicitly state their intention that it be treated as an outright sale, will this description and statement of intent automatically be respected or is there a risk that the transaction could be characterised by a court as a loan with (or without) security? If recharacterisation risk exists, what characteristics of the transaction might prevent the transfer from being treated as an outright sale? Among other things, to what extent may the seller retain any of the following without jeopardising treatment as an outright sale: (a) credit risk; (b) interest rate risk; (c) control of collections of receivables; (d) a right of repurchase/redemption; (e) a right to the residual profits within the purchaser; or (f) any other term?

If a transaction is expressed to be an outright sale and the sale agreement (and other documents) purports to effect an outright sale, but this does not reflect the actual agreement between the parties, the purported sale could be recharacterised as a secured loan.

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Irrespective of the label given to a transaction by the parties, the court will look at its substance (including the particular economic characteristics of the transaction) and will examine whether it creates rights and obligations consistent with a sale.

English case law (for example, *Re: George Inglefield, [1933] Ch. 1, as considered and applied by the English Court of Appeal in Welsh Development Agency v. Export Finance Co Ltd, [1992] BCC 270*) has established a number of key questions which must be considered when determining whether a transaction is a sale rather than a secured loan:

(i) Is the transaction a "sham" (i.e. do the transaction documents accurately reflect the intention of the parties or is there some other agreement or agreements that constitute the real transaction between the parties)?

(ii) Does the seller have the right to reacquire the receivables?

(iii) Does the purchaser have to account for any profit made by it on the sale of the receivables?

(iv) Is the seller required to compensate the purchaser if it ultimately realises the acquired receivables for an amount less than the amount paid?

The principles set out in the above English case law were recently confirmed by the Irish High Court in *Bank of Ireland v. Eteams International Ltd [2017] IEHC 393*.

Although it will depend on the particular circumstances, the fact that the seller remains as servicer/collection agent of the receivables post-sale, or retains some degree of credit risk in respect of the receivables post-sale, is not considered to be inconsistent with the transfer being treated as a sale (rather than a secured loan).

There is no Irish case law on the point, but a right of repurchase/redemption for the seller would likely be inconsistent with the transaction being one of true sale. However, if the seller has only a right to ask the purchaser to sell the receivables back, such an arrangement might not be inconsistent with a true sale.

If the sale is recharacterised as a secured loan, the assets "sold" will remain on the seller's balance sheet and the loan will be shown as a liability of the seller. In addition, as it is not the practice in Ireland to make "back-up" security filings, the security may not have been registered and may be void in an insolvency of the seller for lack of registration.

In addition to recharacterisation, sale transactions are also vulnerable under certain provisions of the Irish Companies Act 2014 (the **Companies Act**) such as Section 443 (*power of court to order the return of assets improperly transferred*), Section 604 (*unfair preferences*) and Section 608 (*power of court to order return of assets which have been improperly transferred*).

4.10 Continuous Sales of Receivables. Can the seller agree in an enforceable manner to continuous sales of receivables (i.e., sales of receivables as and when they arise)? Would such an agreement survive and continue to transfer receivables to the purchaser following the seller's insolvency?

Yes. However, the sale of the receivables would need to be by way of an equitable assignment (an agreement whereby a seller purports to sell receivables on a continuous basis will generally take effect as an agreement to assign); the receivables will then be automatically equitably assigned as and when they come into existence.

See question 6.5 for the effect the seller's insolvency could have on such an agreement to assign.

4.11 Future Receivables. Can the seller commit in an enforceable manner to sell receivables to the purchaser that come into existence after the date of the receivables purchase agreement (e.g., "future flow" securitisation)? If so, how must the sale of future receivables be structured to be valid and enforceable? Is there a distinction between future receivables that arise prior to *versus* after the seller's insolvency?

Yes. See question 4.10 above — an assignment of a receivable not in existence at the time of the agreement, but which will be ascertainable in the future, is treated as an agreement to assign and should give rise to an equitable assignment as soon as the receivable comes into existence. See question 6.5 for the effect the seller's insolvency could have on such an agreement to assign.

4.12 Related Security. Must any additional formalities be fulfilled in order for the related security to be transferred concurrently with the sale of receivables? If not all related security can be enforceably transferred, what methods are customarily adopted to provide the purchaser the benefits of such related security?

Related security will typically be capable of being assigned in the same manner as the receivables themselves. It is important, however, to ensure that the assignment provisions are consistent. The transfer or assignment of certain types of security may require additional formalities (some of which are referred to in question 4.3 above).

4.13 Set-Off; Liability to Obligor. Assuming that a receivables contract does not contain a provision whereby the obligor waives its right to set-off against amounts it owes to the seller, do the obligor's set-off rights terminate upon its receipt of notice of a sale? At any other time? If a receivables contract does not waive set-off but the obligor's set-off rights are terminated due to notice or some other action, will either the seller or the purchaser be liable to the obligor for damages caused by such termination?

Until notice of the sale of the receivables contract is provided to the relevant underlying obligor, the obligor will be entitled to exercise any rights of set-off against the purchaser even if they accrue after the date of the sale. It would likely depend on the circumstances, but if an obligor's set-off rights were terminated due to notice or for some other valid reason, the seller or purchaser should not be liable to the obligor for damages caused as a result.

4.14 Profit Extraction. What methods are typically used in your jurisdiction to extract residual profits from the purchaser?

A number of methods of profit extraction are commonly used in Ireland including:

(i) the SPV making loan payments on subordinated loans by the originator; and

(ii) the originator holding a majority of a junior class of notes issued by the purchaser and being paid interest on the notes.

Other profit extraction methods used include:

(i) the originator taking fees for:

- administering the receivables contracts and collecting the receivables;

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- arranging or managing the portfolio of receivables; and/or
- acting as a swap counterparty;

(ii) the purchaser paying the originator deferred consideration on the receivables purchased;

(iii) originating, providing and receiving a fee from the purchaser for credit enhancement arrangements; and

(iv) the originator holding equity securities in the purchaser.

The type of profit extraction method used in any given securitisation transaction will depend on a number of factors, including:

- the nature of the assets in the pool;
- the type of credit enhancement used;
- rating agency and timing considerations; and
- accounting and regulatory capital treatment which may be applied.

5 Security Issues

5.1 Back-up Security. Is it customary in your jurisdiction to take a "back-up" security interest over the seller's ownership interest in the receivables and the related security, in the event that an outright sale is deemed by a court (for whatever reason) not to have occurred and have been perfected (see question 4.9 above)?

It is not customary in Ireland to take such a "back-up" security when the intention is to effect an outright sale of the relevant receivable.

5.2 Seller Security. If it is customary to take back-up security, what are the formalities for the seller granting a security interest in receivables and related security under the laws of your jurisdiction, and for such security interest to be perfected?

See question 5.3 (below).

5.3 Purchaser Security. If the purchaser grants security over all of its assets (including purchased receivables) in favour of the providers of its funding, what formalities must the purchaser comply with in your jurisdiction to grant and perfect a security interest in purchased receivables governed by the laws of your jurisdiction and the related security?

Security is most commonly taken over receivables by way of a legal (or equitable) assignment or a charge over book debts.

Receivables assigned by way of security will create a mortgage over the receivables, either legal (if the requirements of the Judicature Act are followed – see question 4.2 above) or (in the absence of these requirements) equitable. Prior to the perfection of an equitable mortgage by notice to the obligor, the assignee's security will be subject to prior equities (such as rights of set-off and other defences), and will rank behind a later assignment (where the later assignee has no notice of the earlier assignment and has itself given notice to the obligor). In addition, the obligor will be able to discharge its debt by continuing to pay the assignor (as described in questions 4.4 and 4.5 above).

Alternatively, a fixed or floating charge could be granted over the receivables. In comparison to a mortgage (which is a transfer of title together with a condition for re-assignment on redemption), a charge is a mere encumbrance on the receivables, giving the chargee a preferential right to payment out of the receivables in priority to other creditors of the relevant company.

A fixed charge is typically granted over specific receivables and attaches to those receivables upon the creation of the fixed charge. In comparison, a floating charge is normally granted over a class of assets (both present and future) which, prior to the occurrence of a "crystallisation event", can continue to be managed in the ordinary course of the chargor's business. On the occurrence of a crystallisation event, the floating charge will attach to the particular class of the chargor's assets, effectively becoming a fixed charge over those assets. The chargee's degree of control over the receivable is the determining factor in distinguishing a fixed from floating charge (and in that regard the Irish courts look at the substance of the security created, rather than how it is described or named).

In terms of perfection, if an Irish company grants security over certain types of assets (including receivables constituting book debts) (i.e. it creates a "registrable charge" for the purposes of the Companies Act), it must register short particulars of the security created with the Irish Registrar of Companies (the **Registrar of Companies**) within 21 days of its creation (see below for outline of the new priority register under the Companies Act).

Section 408(1) of the Companies Act specifically excludes security interests over the following assets from the registration requirement:

(a) cash;

(b) money credited to an account of a financial institution, or any other deposits;

(c) shares, bonds or debt instruments;

(d) units in collective investment undertakings or money market instruments; or

(e) claims and rights (such as dividends or interest) in respect of anything referred to in any of paragraphs (b) to (d).

The expression "charge" (which now excludes the assets referred to in Section 408(1) above) was drafted to give effect to recommendations of the Irish Company Law Review Group, the group involved with drafting the Companies Act and in accordance with the exceptions to the registration requirements envisaged under Directive 2002/47/EC on Financial Collateral Arrangements as implemented in Ireland by way of the European Communities (Financial Collateral Arrangements) Regulations 2010 (as amended) (the **Financial Collateral Regulations**). It should be noted that "cash" has not been defined in the Companies Act but is defined in the Financial Collateral Regulations as "money credited to an account" or a claim for the repayment of money (for example, money market deposits).

The Companies Act created a new priority register so that the priority of charges is now linked to the date of receipt by the Registrar of Companies of the particulars of the charge, rather than the date of creation of the charge (which determined priority of charges under the old Irish Companies Acts 1963 to 2013). Practically speaking this means that filing in the Companies Registration Office should be effected immediately after closing or as soon as possible thereafter.

Failure to register a registrable security interest within 21 days of its creation will result in that security interest being void as against the liquidator and any creditors of the company which created the registrable charge. However, an unregistered charge will still be valid as against the chargor, provided the chargor is not in liquidation.

5.4 Recognition. If the purchaser grants a security interest in receivables governed by the laws of your jurisdiction, and that security interest is valid and perfected under the laws of the purchaser's jurisdiction, will the security be treated as valid and perfected in your jurisdiction or must additional steps be taken in your jurisdiction?

The relevant security must be valid and perfected under the laws of Ireland and under the governing law of the security, in order for

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it to be given effect by the Irish courts. If the security over the receivables is created by a purchaser which is an Irish company and the receivables are situated in Ireland, details of the security will generally need to be filed with the Registrar of Companies within 21 days of its creation (see question 5.3 above).

Since the enactment of the Companies Act, details of security over the receivables created by a purchaser which is a foreign company where the receivables are situated in Ireland, do not need to be filed with the Registrar of Companies. Only charges submitted against an Irish or external company already registered with the Companies Registration Office will be accepted.

5.5 Additional Formalities. What additional or different requirements apply to security interests in or connected to insurance policies, promissory notes, mortgage loans, consumer loans or marketable debt securities?

A security assignment is usually taken over insurance policies.

Security over mortgage or consumer loans will be created by mortgage or charge. An equitable mortgage is typically created over the mortgage securing a mortgage loan.

The type of security over marketable debt securities depends on whether the relevant securities are bearer or registered, certificated, immobilised or dematerialised and/or directly-held or indirectly held: (i) directly-held and certificated debt securities, where registered, are generally secured by legal mortgage (by entry of the mortgagee on the relevant register) or by equitable mortgage or charge (by security transfer or by agreement for transfer or charge); (ii) security over bearer securities may be created by mortgage or pledge (by delivery together with a memorandum of deposit) or charge (by agreement to charge); and (iii) security may be created over indirectly-held certificated debt securities by legal mortgage (by transfer, either to an account of the mortgagee at the same intermediary or by transfer to the mortgagee's intermediary or nominee via a common intermediary) or by equitable mortgage or charge (by agreement of the intermediary to operate a relevant securities account in the name of the mortgagor containing the debt securities to the order/control of the chargee).

Section 408 of the Companies Act specifically excludes security interests over shares, bonds or debt instruments from the security interest registration requirement. If the security interest contributes a "security financial collateral arrangement", the Financial Collateral Regulations may apply (see question 5.3 above).

5.6 Trusts. Does your jurisdiction recognise trusts? If not, is there a mechanism whereby collections received by the seller in respect of sold receivables can be held or be deemed to be held separate and apart from the seller's own assets (so that they are not part of the seller's insolvency estate) until turned over to the purchaser?

Ireland recognises trusts, and a trust over collections received by the seller in respect of sold receivables should be recognised under the laws of Ireland (provided it is validly constituted).

5.7 Bank Accounts. Does your jurisdiction recognise escrow accounts? Can security be taken over a bank account located in your jurisdiction? If so, what is the typical method? Would courts in your jurisdiction recognise a foreign law grant of security (for example, an English law debenture) taken over a bank account located in your jurisdiction?

Ireland recognises the concept of money held in escrow in a bank account. Security may be taken over a bank account in Ireland and is typically taken by way of a charge or security assignment. Security over a credit balance granted by a depositor in favour of the bank at which such deposit is held can only be achieved by way of charge (not by assignment). If the security constitutes a "security financial collateral arrangement" over "financial collateral" within the meaning of the Financial Collateral Regulations, then those regulations should apply (as to which, see question 5.3 above).

Foreign law-governed security over an Irish situated bank account must be valid under both Irish law and the foreign law in order for it to be given effect by the Irish courts (see question 5.4 above).

5.8 Enforcement over Bank Accounts. If security over a bank account is possible and the secured party enforces that security, does the secured party control all cash flowing into the bank account from enforcement forward until the secured party is repaid in full, or are there limitations? If there are limitations, what are they?

Normally, notice of the creation of security over the account is provided to the bank with which the account is held, and an acknowledgment sought that the bank will, *inter alia*, (upon notification that the security has become enforceable) act in accordance with the instructions of the secured party. If such an acknowledgment has been obtained, once the secured party enforces its security over the relevant bank account, the bank should follow its instructions in respect of all cash in (or flowing into) the account until the obligations owed to the secured party are discharged in full.

However, this control is conferred on the secured party by contract – the bank could refuse to act in accordance with the secured party's instructions. Furthermore, rights of set-off (under statute, common law or contract) might be exercisable in respect of the cash in the account to the detriment of the secured party. Finally, under the Central Bank (Supervision and Enforcement) Act 2013, the CBI has powers to direct the activities of Irish credit institutions in certain circumstances, and the exercise of such powers could interfere with the secured party's control over the bank account.

5.9 Use of Cash Bank Accounts. If security over a bank account is possible, can the owner of the account have access to the funds in the account prior to enforcement without affecting the security?

This depends on the type of security granted over the account/account balance. If a floating charge is granted, the fact the owner of the account may access funds in the account should not affect the validity of the floating charge. However, if the security granted purports to be a fixed charge, the more freely the owner can access the funds in the account, and the less likely it is that the Irish courts would treat it as a fixed charge and the more likely it would be recharacterised as being a floating charge.

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6 Insolvency Laws

6.1 Stay of Action. If, after a sale of receivables that is otherwise perfected, the seller becomes subject to an insolvency proceeding, will your jurisdiction's insolvency laws automatically prohibit the purchaser from collecting, transferring or otherwise exercising ownership rights over the purchased receivables (a "stay of action")? If so, what generally is the length of that stay of action? Does the insolvency official have the ability to stay collection and enforcement actions until he determines that the sale is perfected? Would the answer be different if the purchaser is deemed to only be a secured party rather than the owner of the receivables?

The appointment of a liquidator or an examiner to an insolvent Irish company imposes an automatic stay of action against the entity, but if the receivables have been transferred by legal assignment, the sale will have already been perfected, and the stay should not affect the purchaser's ability to enforce its rights in the receivables.

In the event that a winding up order is issued against the seller and a liquidator is appointed, a plaintiff will need the leave of the court to continue or commence proceedings against the seller.

As regards examinership, a stay of action can be imposed for up to 100 calendar days where the seller goes into examinership (an examiner's appointment is initially for 70 days, but may be extended by another 30 days with the sanction of the court).

If the seller has been appointed as the servicer of the receivables, the stay of action could block the purchaser from enforcing the servicing contract, and any amounts held by the servicer in respect of the receivables (if not held on trust for the purchaser under a valid and binding trust arrangement) could be deemed to form part of the insolvency estate of the servicer, rather than being the property of the purchaser.

If only an equitable assignment has been effected (i.e. no notice has been given to an obligor), an obligor may continue to pay the seller. Normally, the seller will hold any such amounts on trust for the purchaser, but if no such trust has been created, such amounts will likely form part of the seller's insolvency estate and the purchaser would be an unsecured creditor of the seller in respect of those amounts.

6.2 Insolvency Official's Powers. If there is no stay of action, under what circumstances, if any, does the insolvency official have the power to prohibit the purchaser's exercise of its ownership rights over the receivables (by means of injunction, stay order or other action)?

See question 6.1 above. Assuming the receivables have been sold by legal assignment or by means of a subsequently perfected equitable assignment, an Irish insolvency official appointed over the seller should not be able to prohibit the purchaser's exercise of its ownership rights over the receivables (unless there has been a fraudulent preference or an improper transfer of company assets, as described in our response to question 6.3 below).

6.3 Suspect Period (Clawback). Under what facts or circumstances could the insolvency official rescind or reverse transactions that took place during a "suspect" or "preference" period before the commencement of the seller's insolvency proceedings? What are the lengths of the "suspect" or "preference" periods in your jurisdiction for (a) transactions between unrelated parties, and (b) transactions between related parties? If the purchaser is majority-owned or controlled by the seller or an affiliate of the seller, does that render sales by the seller to the purchaser "related party transactions" for purposes of determining the length of the suspect period? If a parent company of the seller guarantee's the performance by the seller of its obligations under contracts with the purchaser, does that render sales by the seller to the purchaser "related party transactions" for purposes of determining the length of the suspect period?

Under Section 443 of the Companies Act, if a liquidator can show that any company property was disposed of and the effect was to "perpetrate a fraud" on either the company, its creditors or its members, the High Court may, if just and equitable, order any person who appears to have "use, control or possession" of the property or the proceeds of the sale or development thereof, to deliver it or pay a sum in respect of it to the liquidator on such terms as the High Court sees fit.

Section 604(2) of the Companies Act provides that any conveyance, mortgage, delivery of goods, payment, execution or other act relating to property made or done by or against a company, which is unable to pay its debts as they become due to any creditor, within six months of the commencement of a winding up of the company with a view to giving such creditor (or any surety or guarantor of the debt due to such creditor) a preference over its other creditors, will be invalid. Case law (under the equivalent provision of the previous Irish Companies Act 1963) indicates that a "dominant intent" must be shown on the part of the entity concerned to prefer a creditor over other creditors. Furthermore, Section 604 is only applicable if at the time of the conveyance, mortgage or other relevant act, the company was already insolvent. Where the conveyance, mortgage, etc. is in favour of a "connected person", the six-month period is extended to two years.

If the purchaser is majority-owned or controlled by the seller or an affiliate of the seller, the purchaser will be considered a "connected person" under Section 604. If a parent company of the seller guarantees the performance by the seller of its obligations under contracts with the purchaser, the question of whether or not the purchaser would be considered a "connected person" under Section 604 depends on the relationship between the purchaser and the seller. For example, if the purchaser was a "related company" (for example, if the purchaser was a subsidiary of the seller or if the purchaser was a company controlled by the seller) then it would be considered a "connected person" and the six-month period would be extended to two years.

Section 597 of the Companies Act renders invalid (except to the extent of monies actually advanced or paid, or the actual price or value of goods or services sold or supplied, to the company at the time of or subsequently to the creation of, and in consideration for the charge, or to interest on that amount at the appropriate rate) floating charges on the property of a company created within 12 months before the commencement of the winding up of that company (unless the company was solvent immediately after the creation of the charge). Where the floating charge is created in favour of a "connected person", the 12-month period is extended to two years.

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6.4 Substantive Consolidation. Under what facts or circumstances, if any, could the insolvency official consolidate the assets and liabilities of the purchaser with those of the seller or its affiliates in the insolvency proceeding? If the purchaser is owned by the seller or by an affiliate of the seller, does that affect the consolidation analysis?

Irish law gives an Irish court the power, in certain circumstances, to treat the assets and liabilities of one company as though they were assets and liabilities of another company.

An Irish court may exercise its equitable jurisdiction and treat two or more companies as a single entity if this conforms to the economic and commercial realities of the situation and the justice of the case so requires.

Furthermore, if an Irish company goes into liquidation or examination, the Companies Act specifies particular scenarios where an Irish court has the power to "make such order as it thinks fit" in respect of transactions entered into by that company to restore the position to what it would have been if it had not entered into the transaction. In addition, in certain limited instances, a court may "pierce the corporate veil".

Also, depending on the particular case, a court may: (i) order that the appointment of an examiner to a company be extended to a "related company" of the company in examination; (ii) (if it is just and equitable to do so) order that any related company of a company being liquidated pay some or all of the debts of the company in liquidation (a "contribution order"); or (iii) provide that where two or more "related companies" are being wound up (and it is just and equitable to do so), both companies be wound up together as if they were one company (a "pooling order"). Each of the above "related company" orders may apply where the purchaser is owned by the seller or by an affiliate of the seller.

However, case law suggests that the above powers/orders will only be exercised/granted in exceptional circumstances.

6.5 Effect of Insolvency on Receivables Sales. If insolvency proceedings are commenced against the seller in your jurisdiction, what effect do those proceedings have on (a) sales of receivables that would otherwise occur after the commencement of such proceedings, or (b) on sales of receivables that only come into existence after the commencement of such proceedings?

If a true sale of the receivables (including future receivables) has already been effected, the purchase price for the receivables has been paid (subject to the matters described in questions 6.1 and 6.3 above), and no further action is required by the seller, the seller's insolvency should not of itself affect the purchaser's rights as purchaser of the receivable.

If a receivables purchase agreement has been entered into, but the purchase price is not paid prior to the seller's insolvency, the purchaser will be left as an unsecured creditor of the seller.

6.6 Effect of Limited Recourse Provisions. If a debtor's contract contains a limited recourse provision (see question 7.3 below), can the debtor nevertheless be declared insolvent on the grounds that it cannot pay its debts as they become due?

A contractual provision limiting the recourse of the creditors of the debtor (as specified in question 7.3 below) is likely to be valid as a matter of Irish law (although such provisions have not yet been adjudicated upon by the Irish courts). Accordingly, if all of the debtor's contracts contain a limited recourse provision whereby its creditors agree to limit their recourse to the debtor (and assuming the limited recourse provisions operate correctly), it should not be possible for the debtor to be declared insolvent on grounds that it cannot pay its debts as they become due.

7 Special Rules

7.1 Securitisation Law. Is there a special securitisation law (and/or special provisions in other laws) in your jurisdiction establishing a legal framework for securitisation transactions? If so, what are the basics? Is there a regulatory authority responsible for regulating securitisation transactions in your jurisdiction?

Yes. Section 110 of the Taxes Consolidation Act 1997 (the **TCA**) allows for the special treatment of Irish companies (**Section 110 SPVs**) under which securitisations and other structured transactions can be effected. Section 110 SPVs can either be private limited companies (**CLS**) or designated activity companies (**DAC**) incorporated under the Companies Act which, if they meet the conditions set out in Section 110, have their profits calculated for Irish tax purposes as if they were carrying on a trade. Where it is envisaged that a Section 110 SPV will issue debt securities it must be registered as a DAC.

This enables Section 110 SPVs to make deductions for all expenditure (subject to certain limitations/restrictions), in particular, interest payments that must be made on the debt instruments issued by them. This ensures that there is very little or no Irish tax payable by Section 110 SPVs. This legislative regime has facilitated the development of securitisation in Ireland, and Section 110 SPVs have been used in numerous cross-border securitisations.

There are also generous exemptions available from Irish withholding tax on payments of interest made by Section 110 SPVs which are structured to fall within the securitisation legislation (these are discussed in more detail in question 9.1 below). One clear advantage for Section 110 SPVs is that they can make payments of "profit dependent" interest without any negative implications and can use straight "pass through" structures, for example, collateralised debt obligations.

In order to avail of the relief under Section 110, the company must be a "qualifying company"; i.e.:

(i) it must be resident in Ireland;

(ii) it must acquire "qualifying assets";

(iii) it must carry on in Ireland a business of holding, managing, or both the holding and management of, qualifying assets;

(iv) it must, apart from activities ancillary to that business, carry on no other activities;

(v) the market value of the qualifying assets is not less than EUR 10 million on the day on which they are first acquired; and

(vi) it must have notified the Revenue Commissioners that it is or intends to be a Section 110 company.

The notice referred to in item (vi) above must be delivered in the prescribed form to the Revenue Commissioners within eight weeks of the 'qualifying company' meeting the requirements outlined in the definition above.

A company shall not be a qualifying company if any transaction or arrangement is entered into by it otherwise than by way of a bargain made at arm's length.

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The definition of "qualifying assets" is non-exhaustive and includes shares, bonds, receivables, other securities, futures, etc. Please note, however, that a Section 110 SPV may not hold real estate assets directly (albeit it may hold shares in a property holding company). In addition, where the qualifying assets derive some or all of their value from real estate located in Ireland, particular care must be taken to ensure strict compliance with Section 110.

Section 110 SPVs are unregulated entities and as such there is no regulatory authority responsible for regulating securitisation transactions in Ireland. As noted in item (iv) above, however, the Revenue Commissioners must be notified that the Section 110 SPV is a "qualifying company" for the purpose of Section 110, and the Central Bank should be notified that it is a "financial vehicle corporation" for the purpose of Regulation (EU) No. 1075/2013 (ECB/2013/40) concerning statistics on the assets and liabilities of financial vehicles corporations engaged in securitisation transactions (the **FVC Regulation**).

7.2 Securitisation Entities. Does your jurisdiction have laws specifically providing for establishment of special purpose entities for securitisation? If so, what does the law provide as to: (a) requirements for establishment and management of such an entity; (b) legal attributes and benefits of the entity; and (c) any specific requirements as to the status of directors or shareholders?

Irish law does not specifically provide for the establishment of special purpose entities for securitisation transactions, but see question 7.1 above.

7.3 Location and form of Securitisation Entities. Is it typical to establish the special purpose entity in your jurisdiction or offshore? If in your jurisdiction, what are the advantages to locating the special purpose entity in your jurisdiction? If offshore, where are special purpose entities typically located for securitisations in your jurisdiction? What are the forms that the special purpose entity would normally take in your jurisdiction and how would such entity usually be owned?

Typically where the underlying assets being securitised are situated in Ireland, the Section 110 SPVs will be incorporated in Ireland. This is subject to any specific legal, commercial, regulatory, tax or administrative reasons and/or any structural practicalities which could require a securitisation entity to be incorporated outside Ireland.

Ireland is considered one of the more attractive jurisdictions in which to establish Section 110 SPVs to effect securitisation transactions. Ireland has a favourable tax regime applicable to Section 110 SPVs and the tax treatment afforded by Section 110 is a key advantage of using an Irish Section 110 SPVs (whether the underlying securitised assets are situated in Ireland or not). The special purpose entity is often incorporated in Ireland (as opposed to other jurisdictions) because investors and market participants are familiar with the established legal framework and tax relief in relation to interest available, due to Ireland's double taxation treaty network.

The main benefits/advantages include:

(i) A highly regarded onshore location. Ireland is a member of the EU and Organisation for Economic Co-operation and Development (**OECD**).

(ii) A trusted and transparent tax regime (Section 110).

(iii) An extensive tax treaty regime. Ireland has 73 double taxation treaties with other countries (72 in effect) which offer an Irish resident Section 110 SPV significant advantages over offshore locations.

(iv) Clear VAT rules. In general, the activities of a Section 110 SPV which is a "qualifying company" under Section 110 are exempt activities for VAT purposes. Management services provided to a Section 110 SPV are also exempt from VAT in Ireland.

(v) An exemption from Irish stamp duty. No Irish stamp duty is payable on the issue of transfer of the notes issued by an Irish Section 110 SPV, provided that the finance raised by the issue of the notes is used in the course of the business of the Section 110 SPV.

(vi) An efficient listing mechanism. The Irish Stock Exchange has extensive experience in the listing of specialist debt securities, and offers a turnaround time of maximum three working days.

(vii) A common law jurisdiction. The Irish legal system derives from the English legal system.

(viii) An infrastructure of experienced professionals: corporate administrators, lawyers, auditors and other service providers.

(ix) A European passport. Securities issued by an Irish Section 110 SPV can, once the prospectus has been approved by the CBI, be accepted throughout the EU for public offers and/or admission to trading on regulated markets under the EU Prospectus Directive.

(x) A public or private limited company structure. A private limited company can be used for most securitisation transactions, meaning that the Section 110 SPV can be incorporated with share capital of just EUR 1 and in just five days (as noted below, public limited companies are typically used for "public offers" of securities).

An Irish Section 110 SPV is usually incorporated under the Companies Act as one of the following:

(i) A private company limited by shares (**LTD**).

(ii) A "designated activity company", being a private company limited by shares (**DAC**).

(iii) A public limited company (**PLC**).

Depending on whether the Section 110 SPV will be listing notes/debentures, the typical structure under Irish law is now a LTD or a DAC. Section 110 SPVs are usually structured as orphan entities, the shares of which are usually held by a professional share trustee on trust for charitable purposes.

Each of the three types of Section 110 SPVs can be incorporated with just a single member.

An LTD has no objects stated in its constitution and can issue unlisted notes/debentures which fall within one of the "excluded offer" exemptions under Directive 2003/71/EC (as amended) to trading (**Prospectus Directive**), for example, where the debt securities the subject of the offer have a minimum denomination of EUR 100,000.

A DAC has specific objects stated in its constitution and can also issue and list notes/debentures which fall within an "excluded offer" under the Prospectus Directive. If the Section 110 SPV intends to list securities other than notes/debentures (such as shares), or to offer listed or unlisted notes/debentures to the public (that is, outside one of the "excluded offer" exemptions under the Prospectus Directive), it must be established as a PLC.

While an LTD is not required to have an authorised share capital, a DAC must have an authorised share capital (although there is no minimum capitalisation requirement). The minimum capitalisation of a PLC is EUR 25,000 of which a quarter must be paid up.

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7.4 Limited-Recourse Clause. Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) limiting the recourse of parties to that agreement to the available assets of the relevant debtor, and providing that to the extent of any shortfall the debt of the relevant debtor is extinguished?

A contractual provision limiting the recourse of the creditors of an entity to its available funds is likely to be valid under Irish law (whether the contract's governing law is Irish or the law of another country – see question 6.6 above).

7.5 Non-Petition Clause. Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) prohibiting the parties from: (a) taking legal action against the purchaser or another person; or (b) commencing an insolvency proceeding against the purchaser or another person?

Although there is little authority in Irish law, it is likely that an Irish court would give effect to contractual provisions (whether governed by Irish law or the law of another country) prohibiting the parties to the relevant contract from taking legal action (or commencing an insolvency proceeding) against the purchaser or another person.

It is possible that an Irish court would consider an insolvency winding up petition even if it were presented in breach of a non-petition clause. A party may have statutory or constitutional rights to take legal action against the purchaser/another person, which may not be contractually disapplied and a court could hold that the non-petition clause was contrary to Irish public policy on the grounds referred to above (i.e. ousting of court jurisdiction and/or Irish insolvency laws).

7.6 Priority of Payments "Waterfall". Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) distributing payments to parties in a certain order specified in the contract?

An Irish court should generally give effect to a contractual provision (whether the contract's governing law is Irish or the law of another country) distributing payments to an Irish company's creditors in a certain order. However, in an insolvency of an Irish company certain creditors are given preferential status by statute and so the contractual priority of payments provision could be altered.

7.7 Independent Director. Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) or a provision in a party's organisational documents prohibiting the directors from taking specified actions (including commencing an insolvency proceeding) without the affirmative vote of an independent director?

A CLS has full and unlimited capacity under its constitution i.e. no provision in its constitution can restrict the directors from taking specified actions. On the other hand, the constitution of a DAC has an objects clause by which the directors can be restricted from taking specified actions. An Irish court should give effect to such a provision in a DAC's constitution.

The Irish courts should give effect to a contractual provision which prohibits the directors from taking specified actions. However, any provision which purports to restrict or limit the directors' ability to bring insolvency proceedings may be invalid on public policy grounds or as incompatible with the directors' statutory duties.

7.8 Location of Purchaser. Is it typical to establish the purchaser in your jurisdiction or offshore? If in your jurisdiction, what are the advantages to locating the purchaser in your jurisdiction? If offshore, where are purchasers typically located for securitisations in your jurisdiction?

Typically where the underlying assets being securitised are situated in Ireland, the purchaser will be incorporated in Ireland. This is subject to any specific legal, commercial, regulatory, tax or administrative reasons and/or any structural practicalities which could require a purchaser to be incorporated outside Ireland.

As specified in question 7.3 above, the purchaser is often incorporated in Ireland (as opposed to other jurisdictions) because investors and market participants are familiar with the established legal framework and largely tax neutral treatment of profits arising in the purchaser established as a Section 110 qualifying company.

See question 7.3 above for a list of the main benefits/advantages.

8 Regulatory Issues

8.1 Required Authorisations, etc. Assuming that the purchaser does no other business in your jurisdiction, will its purchase and ownership or its collection and enforcement of receivables result in its being required to qualify to do business or to obtain any licence or its being subject to regulation as a financial institution in your jurisdiction? Does the answer to the preceding question change if the purchaser does business with more than one seller in your jurisdiction?

If the underlying obligors are consumers, the CCA (and the other consumer protection legislation and codes discussed in question 1.2 above and question 8.4 below) may be applicable (irrespective of whether the purchaser is dealing with one or more sellers in Ireland). The CCA provides for the licensing of three categories of activity, acting as: (i) a moneylender; (ii) a credit intermediary; or (iii) a mortgage intermediary. If the underlying obligors are natural persons and there is any form of credit being provided, consideration should be had to the retail credit firm authorisation requirements of the CBI under the Central Bank Acts 1942 to 2015 (the **CBA**). In addition, under current Irish data protection legislation, the purchaser might need to register with the Irish Data Protection Commissioner as a "data controller" or a "data processor". This requirement will, however, fall away once the EU General Data Protection Regulation (EU) 2016/679 (**GDPR**) becomes effective on 25th May 2018. See the response below at question 8.7.

If a purchaser holds the legal title to a credit and (i) where that credit was advanced by an Irish bank or a EU regulated entity authorised to provide credit in Ireland, (ii) is advanced to one or more natural persons within the state or with certain micro, small or medium-sized enterprises, and (iii) chooses to service the loan itself, it may be required to be authorised as a "credit servicing firm" as defined in the Consumer Protection (Regulation of Credit Servicing Firms) Act 2015 (the **Credit Servicing Act**) by the CBI and will be subject to the CBI's various codes (as discussed in question 1.2 above and question 8.4 below). If, however, the relevant purchaser appoints a credit servicer who is either (i) a regulated financial services

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provider authorised to provide credit in Ireland, or (ii) an authorised "credit servicing firm" itself (whether incorporated in Ireland or elsewhere within the EEA) to service the loans/credit, the purchaser will not be required to be authorised under the Credit Servicing Act.

8.2 Servicing. Does the seller require any licences, etc., in order to continue to enforce and collect receivables following their sale to the purchaser, including to appear before a court? Does a third-party replacement servicer require any licences, etc., in order to enforce and collect sold receivables?

The seller does not need a licence in order to continue to enforce and collect receivables following their sale to the purchaser, as debt collection is not a specifically licensed activity in Ireland. However, with respect to any credit agreement it continues to service, it will be required to be authorised as a "credit servicing firm" as defined in the Credit Servicing Act (see question 8.1 above) and comply with applicable Irish consumer protection legislation (e.g. the CPC). Up until 25th May 2018, the seller would also need to be registered with the Data Protection Commissioner. Where the seller continues to act as servicer with respect to residential mortgage loans, it will need to be authorised to perform such role by the CBI. Any standby or replacement servicer would require the same licences and authorisations.

8.3 Data Protection. Does your jurisdiction have laws restricting the use or dissemination of data about or provided by obligors? If so, do these laws apply only to consumer obligors or also to enterprises?

The Irish Data Protection Act, 1988 and the Irish Data Protection (Amendment) Act 2003 (the **DPAs**) restrict the use and dissemination of personal data in relation to "data subjects", which are "individuals" (i.e. natural persons and not corporate entities).

The DPAs regulate the collection, processing, use and disclosure of data and provide, *inter alia*, that such data must be kept for one or more specified and lawful purposes only, that it must be used and disclosed only in ways compatible with those purposes, and be kept safe and secure.

The GDPR will come into force on the 25th May 2018, replacing the existing data protection framework under the EU Data Protection Directive. Data subjects will have more control over the processing of their personal data once GDPR comes into force. The GDPR imposes direct statutory obligations on data processors, which means they will be subject to direct enforcement by supervisory authorities, fines, and compensation claims by data subjects. Data transfers to countries outside the EEA continue to be prohibited unless that country ensures an adequate level of protection. The GDPR retains existing transfer mechanisms, and provides for additional mechanisms, including approved codes of conduct and certification schemes. The GDPR prohibits any non-EU court, tribunal or regulator from ordering the disclosure of personal data from EU companies unless it requests such disclosure under an international agreement, such as a mutual legal assistance treaty. See question 8.7 below.

8.4 Consumer Protection. If the obligors are consumers, will the purchaser (including a bank acting as purchaser) be required to comply with any consumer protection law of your jurisdiction? Briefly, what is required?

If the obligors are "consumers" then a bank acting as purchaser will need to comply with the terms of its authorisation and the applicable codes of conduct/advertising rules (e.g. the CPC) or other Irish consumer protection laws, including the CCA, the CCA Regulations and the UTCCR Regulations.

The CCA imposes a number of obligations on credit intermediaries and also provides protections to consumers (e.g. by regulating the advertising of consumer credit, and by bestowing a "cooling-off" period in favour of the consumer after signing an agreement).

The CCA Regulations apply to loans to consumers where the amount lent is between EUR 200 and EUR 75,000. The main provisions of the CCA relate to, *inter alia*: (i) standardisation of the information to be contained in a credit agreement; (ii) standardisation of pre-contractual information; and (iii) a full 14-day "right of withdrawal" for consumers from the relevant credit agreement.

Where there is a significant imbalance in the parties' rights and obligations under a consumer contract to the detriment of the consumer, the UTCCR Regulations may apply. The UTCCR Regulations contain a non-exhaustive list of terms which will be deemed "unfair" and the list includes terms which attempt to exclude or limit the legal liability of a seller in the event of the death of, or personal injury to, a consumer due to an act or omission by the seller, or, require any consumer who fails to fulfil his obligation to pay a disproportionately high sum in compensation. If a term is unfair it will not be binding on the consumer. However, the contract should continue to bind the parties, if it is capable of continuing in existence without the unfair term.

The CPC imposes general obligations on "regulated entities" dealing with "customers" in Ireland (primarily "consumers"), to act honestly, fairly and professionally and with due skill, care and diligence in the best interests of their customers and to avoid conflicts of interest.

If there is no obligation on a non-bank purchaser to provide any funding to a consumer, then it should not need to be licensed, but might still need to comply with the CCA, the UTCCR Regulations, the CPC and the CCA Regulations (if applicable).

8.5 Currency Restrictions. Does your jurisdiction have laws restricting the exchange of your jurisdiction's currency for other currencies or the making of payments in your jurisdiction's currency to persons outside the country?

Ireland does not have any exchange control laws. Certain financial transfer orders in place from time to time may restrict payments to certain countries, groups and individuals subject to UN sanctions.

8.6 Risk Retention. Does your jurisdiction have laws or regulations relating to "risk retention"? How are securitisation transactions in your jurisdiction usually structured to satisfy those risk retention requirements?

The European-wide regime for risk retention is set out in:

- Articles 404 to 410 of Regulation (EU) No. 575/2013 (the **CRR**), the associated regulatory technical standards (**RTS**) and implementing technical standards.
- Corresponding provisions in Directive 2011/61/EU, the Alternative Investment Fund Managers (**AIFM Directive**) and Commission Delegated Regulation (EU) No 231/2013 referred to as the Alternative Investment Fund Manager Regulation (the **AIFMR**).
- Commission Delegated Regulation (EU) 2015/35 supplementing Directive 2009/138/EC of the European Parliament and of the Council on the taking-up and pursuit of the business of Insurance and Reinsurance (**Solvency II**).

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The CRR is directly applicable in Ireland but the European Union (Capital Requirements) (No. 2) Regulations 2014 give effect to a number of technical requirements to ensure the CRR operates effectively in Irish law.

The CRR prohibits an institution, other than when acting as an originator, a sponsor or original lender, from becoming exposed to the credit risk of a securitisation position unless the originator, sponsor or original lender has explicitly disclosed to the institution that it will retain, on an ongoing basis, a material net economic interest in the credit risk of the securitisation position which, in any event, must be at least 5%.

Often such interest will be comprised of an interest in the first loss tranche, as contemplated by each of Article 405(1)(d) of the CRR, Article 51(1)(d) of AIFMR and paragraph 2(d) of Article 254 of the Solvency II.

8.7 Regulatory Developments. Have there been any regulatory developments in your jurisdiction which are likely to have a material impact on securitisation transactions in your jurisdiction?

(i) The GDPR is a directly effective regulation which will be immediately effective across the EU from 25 May 2018. The GDPR significantly changes data protection law in Europe. The GDPR will strengthen the rights of individuals in relation to their personal information and increase the obligations of organisations which hold that information. It aims to give control to EU citizens over their personal data and simplify the regulatory environment for international business by unifying regulation within the EU. Data subjects will have more control over the processing of their personal data. The GDPR applies to both controllers and processors established in the EU, and those outside the EU, who offer goods or services to, or monitor EU data subjects. As of 25 May 2018, the DPA's will be replaced by GDPR as the new data protection legislation applicable in Ireland.

(ii) The legal developments arising from regulation affecting the securitisation market generally in Europe will be relevant to securitisations in Ireland. In January 2018 two regulations, namely Regulation (EU) 2017/2042 (the **STS Regulation**) and the associated Regulation (EU) 2017/2401 (the **Securitisation Prudential Regulation**, and together with the STS Regulation, the **Securitisation Regulations**) came into force establishing a new framework for European securitisations. The majority of the Securitisation Regulations will apply to securitisations on or after 1 January 2019.

(iii) The Irish Parliament (the **Oireachtas**) is currently considering a proposed bill entitled 'Consumer Protection (Regulation of Credit Servicing Firms) (Amendment) Bill 2018' (the **Bill**). The proposed Bill seeks to amend the Credit Servicing Act, the Central Bank (Supervision and Enforcement) Act 2013, the Central Bank Act 1942 and the Central Bank Act 1997. The Bill is at an early stage of consideration and there is no clarity on when, and in what form, the Bill will be enacted into law and how it will co-exist with the regime introduced under the Credit Servicing Act. The purpose of the Bill is to (i) extend the requirement to being regulated to "credit agreement owners" of mortgage loans and SME loans and (ii) introduce certain other protections for the borrowers under such credit agreements. The current draft of the Bill helpfully seeks to carve out entities which purchase credit agreements where such purchase "is made by way of securitisation" from its application but "securitisation" is not currently defined in the Bill. The Bill is expected to be subject to amendments at committee stage before coming before the Oireachtas again. It is expected that any amendments will seek to clarify, amongst other things, that the provisions will not adversely affect securitisation special purpose entities involved in certain securitisation transactions.

(iv) As noted above, the "true sale" principles set out in the English cases of *Re: George Inglefield and Welsh Development Agency* have been confirmed by the Irish High Court in *Bank of Ireland v. Eteams International Ltd [2017] IEHC 393*.

(v) The Credit Reporting Act 2013 (the **CRA**) imposes certain reporting obligations on lenders in respect of the provision of credit in circumstances in which the CRA applies. The CRA establishes a central database for credit information, which will enable the Central Bank to create a complete credit report for relevant borrowers. It will also provide lenders with a greater level of information to assist them in assessing credit applications. Key provisions of the CRA have taken effect from 30 June 2017. From this date, most lenders will begin submitting information to the new Central Credit Register (the **Register**) operated by the CBI. The information collection will be implemented on a phased basis between 2017 and 2018, with an initial focus on collecting information relating to consumer lending, followed by obtaining information relating to business lending.

9 Taxation

9.1 Withholding Taxes. Will any part of payments on receivables by the obligors to the seller or the purchaser be subject to withholding taxes in your jurisdiction? Does the answer depend on the nature of the receivables, whether they bear interest, their term to maturity, or where the seller or the purchaser is located? In the case of a sale of trade receivables at a discount, is there a risk that the discount will be recharacterised in whole or in part as interest? In the case of a sale of trade receivables where a portion of the purchase price is payable upon collection of the receivable, is there a risk that the deferred purchase price will be recharacterised in whole or in part as interest? If withholding taxes might apply, what are the typical methods for eliminating or reducing withholding taxes?

It is usually possible to structure a securitisation (especially when using a Section 110 SPV) so that payments on receivables are not subject to Irish withholding tax.

There is a general obligation to withhold tax from any payment of yearly interest made by an Irish company. The rate of withholding is currently 20%. Therefore, in principle, if the debtor is an Irish person and the receivable has a maturity of more than one year it is likely this withholding obligation will arise. Interest paid by Irish debtors to a Section 110 SPV should come within an exemption from interest withholding tax.

Exemptions also exist for interest payments made by a Section 110 SPV. There is an exemption for interest paid by a Section 110 SPV to a person who is resident for the purpose of tax in an EU Member State (other than Ireland) or in a country with which Ireland has a double tax treaty (except in a case where the person is a company where such interest is paid to the company in connection with a trade or a business which is carried on in Ireland by the company through a branch or agency).

There is also an exemption for interest paid on a quoted eurobond, where either:

(a) the person by or through whom the payment is made is not in Ireland, i.e. non-Irish paying agent; or

(b) the payment is made by or through a person in Ireland, and either:

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(i) the quoted eurobond is held in a recognised clearing system (Euroclear and Clearstream SA are so recognised); or

(ii) the person who is a beneficial owner of the quoted eurobond and who is beneficially entitled to the interest is not resident in Ireland and has made a declaration to this effect.

A quoted eurobond means a security which:

(a) is issued by a company;

(b) is quoted on a recognised stock exchange; and

(c) carries a right to interest.

In the case of a sale of trade receivables, deferred purchase price should not be recharacterised in whole, or in part, as interest. It should be considered to be a payment made for the acquisition of the receivables, and not a payment of interest. Likewise, a sale of receivables at a discount should not of itself result in amounts subsequently paid on the receivables being treated as annual interest subject to withholding tax.

Given extensive domestic tax exemptions, withholding tax is unlikely to apply. However, where one of the above-mentioned exemptions does not apply in relation to payments of interest by a Section 110 SPV, it may be possible to still avoid Irish withholding tax if the securities issued by the Section 110 SPV can be constituted as wholesale debt instruments (broadly being debt instruments recognising an obligation to pay a stated amount which are interest bearing (or issued at a premium or discount) and which mature within two years of issue).

9.2 Seller Tax Accounting. Does your jurisdiction require that a specific accounting policy is adopted for tax purposes by the seller or purchaser in the context of a securitisation?

A company qualifying for the favourable Irish tax treatment provided for by Section 110 of the TCA will be, subject to certain adjustments required by law, subject to Irish corporation tax on its profit according to its profit and loss account prepared in accordance with generally accepted commercial accounting principles in Ireland as at 31 December 2004 (i.e. before the introduction of IFRS), unless it elects otherwise.

9.3 Stamp Duty, etc. Does your jurisdiction impose stamp duty or other transfer or documentary taxes on sales of receivables?

An agreement for the sale of, or an instrument effecting the sale of, debt having an Irish legal *situs* may be chargeable to Irish stamp duty absent an exemption. An instrument effecting the transfer of debt having a non-Irish *situs* may also be chargeable to Irish stamp duty, absent an exemption, if it is executed in Ireland or if it relates to something done or to be done in Ireland. There are certain exemptions from Irish stamp duty that may be relevant, such as the debt factoring exemption or loan capital exemption. A transfer by way of novation should not give rise to stamp duty.

9.4 Value Added Taxes. Does your jurisdiction impose value added tax, sales tax or other similar taxes on sales of goods or services, on sales of receivables or on fees for collection agent services?

Ireland does apply VAT on the sale of goods and services. The standard rate of VAT is 23%.

A purchaser will be required to register and account, on a reverse charge basis, for Irish VAT at the rate of 23% on the receipt by it of vatable services from persons established outside Ireland. These services would include legal, accounting, consultancy and rating agency services and also financial services to the extent that those financial services are not exempt from Irish VAT.

The sale of receivables should be exempt from VAT. The services of a collection agent would normally qualify for exemption.

Where a purchaser would not be engaged in making VAT taxable supplies in the course of its business, it would not be able to recover VAT (1) payable by it in respect of the receipt of services outlined in the paragraph above, or (2) charged to it by suppliers of VAT-taxable services (e.g. the provision of legal, accounting and audit services).

9.5 Purchaser Liability. If the seller is required to pay value-added tax, stamp duty or other taxes upon the sale of receivables (or on the sale of goods or services that give rise to the receivables) and the seller does not pay, then will the taxing authority be able to make claims for the unpaid tax against the purchaser or against the sold receivables or collections?

Regarding VAT, if the supply is made by an Irish supplier, the supplier is the party responsible for payment of the VAT liability to the VAT authority, and the VAT authorities cannot pursue the liability from the purchaser or any other. However, in the case of reverse charge, VAT liabilities in respect of the receipt of rateable services from outside of Ireland the purchaser is the party responsible for payment of the VAT liability to the VAT authorities. In an arm's length transaction, stamp duty should be for the account of the purchaser only.

9.6 Doing Business. Assuming that the purchaser conducts no other business in your jurisdiction, would the purchaser's purchase of the receivables, its appointment of the seller as its servicer and collection agent, or its enforcement of the receivables against the obligors, make it liable to tax in your jurisdiction?

Liability to Irish corporation tax may arise if the purchaser is "carrying on a trade" in Ireland. The term "trade" is a case law-derived concept and there is no useful statutory definition of the term. However, in general, the purchase, collection and enforcement of the receivable should not be considered as "trading" under Irish law and the purchaser should not incur any Irish tax liabilities.

9.7 Taxable Income. If a purchaser located in your jurisdiction receives debt relief as the result of a limited recourse clause (see question 7.3 above), is that debt relief liable to tax in your jurisdiction?

The purchaser should be able to claim a tax deduction in respect of a debt which is proven to the satisfaction of the Irish tax authorities to be bad. A tax deduction is not available for general provisions for bad debt. If the purchaser claims a tax deduction for a bad debt, which is subsequently recovered, that amount will be treated as taxable income of the purchaser.

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Italy

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Ugo De Vivo

1 Receivables Contracts

1.1 Formalities. In order to create an enforceable debt obligation of the obligor to the seller: (a) is it necessary that the sales of goods or services are evidenced by a formal receivables contract; (b) are invoices alone sufficient; and (c) can a binding contract arise as a result of the behaviour of the parties?

(i) Under a general principle of Italian law, the relevant parties can freely choose the form of their contracts, except as otherwise (expressly) provided by the law.

According to certain provisions of Italian law (*e.g.* Article 1350 of the Italian Civil Code), only the validity of certain specific contracts (*e.g.* contracts that involve the transfer of ownership of a property) requires written form (otherwise the contract is considered null and void).

In addition, in relation to certain agreements expressly identified by the law (*e.g.* Article 1888 of the Italian Civil Code in relation to the insurance agreement), the written form can be required to prove the existence of such relevant agreement between the parties.

(ii) Invoices can be considered written evidence of a commercial agreement between the parties, but – according to the majority of Italian case law – they are not sufficient to prove the existence of a valid contract.

However, according to Article 633 *et seq.* of the Italian Civil Procedure Code, a creditor, under certain conditions expressly provided therein, may use the invoice as an instrument in order to obtain from the relevant Court an injunction to pay against the debtor.

(iii) In light of paragraph (i) above, a contract can arise as a result of certain behaviour of the parties. However, it should be considered that (i) certain sales of receivable contracts require the written form to be valid (*e.g.* the contracts entered into with public administration entities or factoring agreements), and (ii) binding contracts are generally proved by written documents. For these reasons – in the context of Italian transactions – receivables transfer agreements are made in written form. In relation to the main features of receivables transfer agreements, please refer to section 4 below.

In addition, pursuant to Article 1362 of the Italian Civil Code, the overall behaviour of the parties is considered a criterion of interpretation for an Italian court, in order to understand the common intention of the parties in respect of the relevant contract.

1.2 Consumer Protections. Do your jurisdiction's laws: (a) limit rates of interest on consumer credit, loans or other kinds of receivables; (b) provide a statutory right to interest on late payments; (c) permit consumers to cancel receivables for a specified period of time; or (d) provide other noteworthy rights to consumers with respect to receivables owing by them?

(i) Under Italian law, the rate of interest payable under any credit agreement that is higher than a certain threshold provided by law – as set quarterly by the Italian Ministry of Economy and Finance, in agreement with Bank of Italy, on the basis of, amongst other things, the average overall effective rate (*Tasso Effettivo Globale Medio*) charged by banks and other financial institutions in the context of similar transactions – is considered usurious and, therefore, the relevant interest clause is null and void and no interest is due by the relevant debtor in accordance with Article 1815, paragraph 2 of the Italian Civil Code.

When the interest is considered usurious, criminal sanctions may apply in accordance with Article 644 of the Italian Criminal Code.

(ii) Italian legal framework provides for a specific regime in relation to interest on late payments.

According to Article 1224 of the Italian Civil Code, interest on late payments is due by the relevant debtor for pecuniary obligations – starting from the default – at the statutory rate (currently at 0.3%). However, the parties may agree on higher default interest in cases of late payment.

In addition, Legislative Decree No. 231/2002 provides for specific provisions in relation to interest on late payments in commercial transactions.

(iii) Under Italian law, a right to withdraw is recognised both under the Italian Civil Code and under certain special laws.

In general, if the parties have agreed that one of them has the right to withdraw from the contract, such right can be exercised as long as the relevant obligations (*e.g.* the object of the agreement) have not been performed. In contracts for continuous or periodic performance (*contratti a esecuzione continuata o periodica*), such a right can be exercised also at a later stage, but the withdrawal has no effect in relation to the activities which have been already carried out (Article 1373 of the Italian Civil Code).

In relation to consumers contracts, Legislative Decree No. 206 of 6 September 2005 (the "**Italian Consumers' Code**") provides for additional withdrawal rights. The consumer has a right of withdrawal, *inter alia*, from distance or off-premises contracts without any justification (and without

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incurring any further costs) for a period of 14 calendar days from the date of the agreement, as specified in Article 52 *et seq.* of the Italian Consumers' Code.

In addition, Legislative Decree No. 385 of 1 September 1993 (the "**Italian Consolidated Banking Law**") provides for specific provisions on credit to consumers. In particular, pursuant to Article 125-*ter* of the Italian Consolidated Banking Law, the consumer may withdraw from the relevant contract (and, as a consequence, any ancillary services) within 14 days from the date of the execution of such contract or from the date it has received all the relevant information required by the law.

(iv) The Italian Consumers' Code provides for a specific chapter (Article 45 *et seq.*) entitled "*Consumer rights in contracts*" which includes certain rules that have to be applied to any contract concluded by a consumer.

The Italian Civil Code provides for certain provisions that apply to consumers (*e.g.* on transparency in banking and credit agreements and insurance contracts).

In addition, as specified in paragraph (iii) above, the Italian Consolidated Banking Law (Article 121 *et seq.*) provides for specific provisions on credit to consumers which include, *inter alia*, provisions on transfers of receivables (Article 125-*septies* provides that (i) in case of transfer of receivables and in derogation from the provisions of the Italian Civil Code, the consumer may oppose to the transferee the same objections it could raise *vis-à-vis* the transferor, including any set-off right; and (ii) the consumer/debtor shall be informed of the assignment of the relevant receivables).

1.3 Government Receivables. Where the receivables contract has been entered into with the government or a government agency, are there different requirements and laws that apply to the sale or collection of those receivables?

Italian law provides for a particular regime in relation to receivables arising from contracts entered into with government, government agencies or other public entities (the "**Government Receivables**").

The assignment of Government Receivables is mainly regulated by (i) the Royal Decree No. 2440 of 24 November 1923 (the "**Royal Decree 2440**"), and (ii) the Legislative Decree No. 50 of 2016 concerning public procurement (the "**Public Procurement Code**").

In particular, according to Articles 69 and 70 of the Royal Decree 2440 the assignment of Government Receivables shall comply with, *inter alia*, the following requirements:

(i) the transfer shall be executed by way of a public deed (*atto pubblico*) or notarised private deed (*scrittura privata autenticata*), and a public deed or notarised private deed shall be executed for each public entity;

(ii) the assignment must be notified to the assigned debtor/public entity through a court bailiff; and

(iii) in case of assignment of receivables deriving from ongoing public procurement, the assignment must be approved by the assigned debtor.

Pursuant to Article 106, paragraph 13, of the Public Procurement Code, the assignment of the receivables arising from a procurement agreement shall comply with, *inter alia*, the following requirements:

(a) the provisions of Law No. 52 of 21 February 1991 (the "**Italian Factoring Law**") shall apply;

(b) the transfer shall be executed by way of a public deed (*atto pubblico*) or notarised private deed (*scrittura privata autenticata*);

(c) the assignment must be notified to the assigned debtor/public entity;

(d) the assignment is valid and effective towards the public entity if it is not rejected by the public entity within 45 days from receipt of the relevant notification; and

(e) in any case the public entity which has received the relevant notification may oppose to the transferee the same objections it could raise *vis-à-vis* the transferor deriving from the relevant agreement.

It should be noted that, in relation to the transfer of receivables carried out in the context of Italian securitisation transactions, Law No. 130 of 30 April 1999 ("**Italian Securitisation Law**") provides that (i) Articles 69 and 70 of Royal Decree 2440 and (ii) other provisions which require different or further formalities than those set out under the Italian Securitisation Law, do not apply (Article 4, par. 4-*bis* of the Italian Securitisation Law).

It shall be noted that, according to Article 48-*bis* of the Italian Presidential Decree No. 602/1973, a public entity, before making any payment to its creditor for an amount higher than EUR 5,000, shall verify whether or not such creditor has unpaid tax.

2 Choice of Law – Receivables Contracts

2.1 No Law Specified. If the seller and the obligor do not specify a choice of law in their receivables contract, what are the main principles in your jurisdiction that will determine the governing law of the contract?

In Italy, private international law is governed by the Law No. 218/1995 (the "**Italian Private International Law**"). According to Article 57 of the Italian Private International Law, contractual obligations shall be governed in all cases by the Rome Convention of 19 June 1980 (which has been superseded by Regulation (EC) No. 593/2008 (the "**Rome I Regulation**") in relation to all Member States excluding Denmark).

According to Article 4, paragraph 1 of Rome I Regulation, in case the parties have not specified the law applicable to the contract, the applicable law is determined also by taking into account the type of contract (*e.g.* for sale of goods, the law of the country of habitual residence of the seller applies). If none or more than one of paragraph 1 rules apply to a contract, the contract shall be governed by the law of the country where the party required to effect the characteristic performance of the contract has its habitual residence. In addition, where it is clear from all the circumstances of the case that the contract is manifestly more closely connected with a country other than that identified with the criteria above, the law of that other country shall apply. The same law applies when no applicable law can be determined.

In case one of the parties is not placed in a Member State (and the parties have not specified a choice of law in their contract), the choice of law will depend on the multilateral and/or bilateral international convention in force between Italy and the country where the other party is placed.

2.2 Base Case. If the seller and the obligor are both resident in your jurisdiction, and the transactions giving rise to the receivables and the payment of the receivables take place in your jurisdiction, and the seller and the obligor choose the law of your jurisdiction to govern the receivables contract, is there any reason why a court in your jurisdiction would not give effect to their choice of law?

In the proposed scenario, an Italian Court will give effect to the

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choice of law of the parties. In particular, according to Article 3 of Rome I Regulation, a contract shall be governed by the law chosen by the parties.

2.3 Freedom to Choose Foreign Law of Non-Resident Seller or Obligor. If the seller is resident in your jurisdiction but the obligor is not, or if the obligor is resident in your jurisdiction but the seller is not, and the seller and the obligor choose the foreign law of the obligor/seller to govern their receivables contract, will a court in your jurisdiction give effect to the choice of foreign law? Are there any limitations to the recognition of foreign law (such as public policy or mandatory principles of law) that would typically apply in commercial relationships such as that between the seller and the obligor under the receivables contract?

In accordance with Rome I Regulation, Italian courts will generally give effect to the choice of a foreign law. Pursuant to Article 3 of Rome I Regulation, the obligor and the seller are permitted to choose the law governing their receivables contract (that can be also amended by the parties, if it does not affect the rights of third parties).

However, Rome I Regulation sets out certain limitations to the general application of a law chosen by the parties, including:

(i) where all of the relevant elements in the contract are located in one or more Member State (or in a country other than the country whose law has been chosen), the choice of the parties regarding the applicable law may not prejudice the application of mandatory provisions under EU law (or under the law of that other country);

(ii) the choice of the parties shall not restrict the application of the overriding mandatory provisions of the law of the relevant forum; and

(iii) the application of a provision of the law chosen by the parties may be refused if such application is manifestly incompatible with the public policy (*ordre public*) of the relevant forum.

Similarly, it should be noted that Italian Private International Law also provides for the following limitations:

(i) the foreign law of referral shall not apply if its effects are "contrary to public order" (*ordine pubblico*) (usually meaning the "international public order"); and

(ii) the Italian mandatory provisions ("*norme di applicazione necessaria*") shall at all times prevail.

3 Choice of Law – Receivables Purchase Agreement

3.1 Base Case. Does your jurisdiction's law generally require the sale of receivables to be governed by the same law as the law governing the receivables themselves? If so, does that general rule apply irrespective of which law governs the receivables (i.e., your jurisdiction's laws or foreign laws)?

Italian law does not require the sale of receivables to be governed by the same law governing the receivables.

According to Article 3 of Rome I Regulation, the seller and the purchaser are free to choose the applicable law for the sale of receivables (please refer to questions 2.2 and 2.3 above).

However, please note that in relation to assignments of receivables:

(i) in accordance with Article 14, paragraph 2, of Rome I Regulation, the law governing the assigned receivables determines: (a) their assignability; (b) the relationship between the assignee and the debtor; (c) the conditions under which the assignment or subrogation can be invoked against the debtor; and (d) whether the debtor's obligations have been discharged; and

(ii) according to Article 27 of Rome I Regulation, the European Commission issued (a) on September 2016 a report on the effectiveness of an assignment or subrogation of a claim against third parties and the priority of the assigned or subrogated claim over a right of another person, and (b) in March 2018 a proposal for a regulation on the law applicable to the third-party effects of assignments of claims.

3.2 Example 1: If (a) the seller and the obligor are located in your jurisdiction, (b) the receivable is governed by the law of your jurisdiction, (c) the seller sells the receivable to a purchaser located in a third country, (d) the seller and the purchaser choose the law of your jurisdiction to govern the receivables purchase agreement, and (e) the sale complies with the requirements of your jurisdiction, will a court in your jurisdiction recognise that sale as being effective against the seller, the obligor and other third parties (such as creditors or insolvency administrators of the seller and the obligor)?

In the envisaged scenario, Italian Courts will recognise the sale of receivables as being effective against the seller and the obligor.

In this respect, please also refer to question 3.1 above.

3.3 Example 2: Assuming that the facts are the same as Example 1, but either the obligor or the purchaser or both are located outside your jurisdiction, will a court in your jurisdiction recognise that sale as being effective against the seller and other third parties (such as creditors or insolvency administrators of the seller), or must the foreign law requirements of the obligor's country or the purchaser's country (or both) be taken into account?

On the basis of Article 14, paragraph 2, of Rome I Regulation – described in question 3.1. above – the law governing the assigned or subrogated claim shall determine its assignability, the relationship between the assignee and the debtor, the conditions under which the assignment or subrogation can be invoked against the debtor, and whether the debtor's obligations have been discharged.

In this case, assuming that the provisions of the Rome I Regulation are applicable, the Italian court should recognise the sale of receivables as being effective against the seller.

3.4 Example 3: If (a) the seller is located in your jurisdiction but the obligor is located in another country, (b) the receivable is governed by the law of the obligor's country, (c) the seller sells the receivable to a purchaser located in a third country, (d) the seller and the purchaser choose the law of the obligor's country to govern the receivables purchase agreement, and (e) the sale complies with the requirements of the obligor's country, will a court in your jurisdiction recognise that sale as being effective against the seller and other third parties (such as creditors or insolvency administrators of the seller) without the need to comply with your jurisdiction's own sale requirements?

In the envisaged scenario, an Italian court will recognise the receivables contract as being effective against the seller, without the

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need to comply with Italian sale requirements, assuming that the chosen applicable law to the receivables contract is compliant with the relevant provisions of the Rome I Regulation.

However, please consider the limitations to the general application of a law chosen by the parties described in question 2.3 above.

3.5 Example 4: If (a) the obligor is located in your jurisdiction but the seller is located in another country, (b) the receivable is governed by the law of the seller's country, (c) the seller and the purchaser choose the law of the seller's country to govern the receivables purchase agreement, and (d) the sale complies with the requirements of the seller's country, will a court in your jurisdiction recognise that sale as being effective against the obligor and other third parties (such as creditors or insolvency administrators of the obligor) without the need to comply with your jurisdiction's own sale requirements?

On the basis of the provisions described in questions 3.1 and 3.2 above, and provided that the sale contract complies with all the requirements of the chosen applicable law (the law of the seller's country), an Italian court would recognise that sale as being effective against the obligor, without the need to comply with the Italian sale requirements.

However, please consider the limitations to the general application of a law chosen by the parties described in question 2.3 above.

3.6 Example 5: If (a) the seller is located in your jurisdiction (irrespective of the obligor's location), (b) the receivable is governed by the law of your jurisdiction, (c) the seller sells the receivable to a purchaser located in a third country, (d) the seller and the purchaser choose the law of the purchaser's country to govern the receivables purchase agreement, and (e) the sale complies with the requirements of the purchaser's country, will a court in your jurisdiction recognise that sale as being effective against the seller and other third parties (such as creditors or insolvency administrators of the seller, any obligor located in your jurisdiction and any third party creditor or insolvency administrator of any such obligor)?

On the basis of the provisions described in questions 3.1 and 3.2 above, and provided that the sale contract complies with all the requirements of the chosen applicable law (the law of the purchaser's country), an Italian court would recognise that sale as being effective against the seller.

However, please consider the limitations to the general application of a law chosen by the parties described in question 2.3 above.

4 Asset Sales

4.1 Sale Methods Generally. In your jurisdiction what are the customary methods for a seller to sell receivables to a purchaser? What is the customary terminology – is it called a sale, transfer, assignment or something else?

In Italy, receivables are generally transferred by means of a transfer agreement entered into between the seller and the purchaser in written form.

The Italian Civil Code (Article 1260 *et seq.*) provides for the general rules governing the assignment of receivables.

In addition, in the context of certain finance transactions and subject to the relevant conditions being met, receivables can be transferred pursuant to the provisions of (i) the Italian Factoring Law, and (ii) the Italian Securitisation Law.

The customary terminology for the transfer of receivables is "*cessione*" (*e.g.* assignment or transfer).

4.2 Perfection Generally. What formalities are required generally for perfecting a sale of receivables? Are there any additional or other formalities required for the sale of receivables to be perfected against any subsequent good faith purchasers for value of the same receivables from the seller?

Pursuant to Article 1264 of the Italian Civil Code, a transfer of receivables is enforceable against the assigned debtor either by (i) giving notice of such assignment to the debtor, or (ii) acceptance of such assignment by the debtor. According to Article 1265 of the Italian Civil Code, in the case where the same receivable has been transferred, through following assignments, to different transferees, then the first assignment in respect of which the assigned debtor has been notified, or which the assigned debtor has accepted and having a date certain in law (*data certa*), shall prevail in respect of the other assignments.

Further formalities could be required by specific provisions of law (*e.g.* the contracts entered into with public administration entities).

In the context of securitisation transactions, the perfection formalities set out in Article 4 of the Italian Securitisation Law shall apply and, accordingly, assignments of receivables are enforceable against the relevant debtors following (i) the publication in the Italian Official Gazette of the notice of assignment, and (ii) the registration of the notice of assignment in the relevant Companies' Register. Any other provisions which require different or further formalities than those set out under the Italian Securitisation Law do not apply.

In the context of securitisation transactions involving trade receivables, the parties can also decide to apply the provisions set out in the Italian Factoring Law.

4.3 Perfection for Promissory Notes, etc. What additional or different requirements for sale and perfection apply to sales of promissory notes, mortgage loans, consumer loans or marketable debt securities?

In Italy, the sale of promissory notes shall comply with the specific provisions set out in the Royal Decree No. 1669 of 14 December 1933, which require the delivery and endorsement of such notes in favour of the purchaser.

In relation to assignments of mortgage loans, Article 2843 of the Italian Civil Code requires that such assignments should be noted "on the margin of the registration of the mortgage" ("a *margine dell'iscrizione dell'ipoteca*") and the relevant copy must be delivered to the competent land register office.

There are not specific provisions on the sale of consumer loans.

In relation to transfer of debt securities, it should be noted that:

(i) bearer securities require the delivery of such securities (Article 2003 of the Italian Civil Code);

(ii) registered securities require double annotation of the transfer on the security itself and on the issuer's register (Article 2021 of the Italian Civil Code);

(iii) order securities require the endorsement of such securities (Article 2008 *et seq.* of the Italian Civil Code);

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(iv) according to Article 83-*bis et seq.* of the Legislative Decree No. 58 of 24 February 1998 (the "**Italian Consolidated Financial Law**"), the securities regulated by Italian law admitted to trading or traded in an Italian (or EU) trading venue are generally issued in dematerialised form and, therefore, are subject to a particular transfer regime; and

(v) the transfer requirements for debt securities may also vary on the basis of the corporate type of the issuer (*e.g.* please refer to Article 2483, paragraph 2, of the Italian Civil Code in relation to Italian limited liability companies (*società a responsabilità limitata*)).

4.4 Obligor Notification or Consent. Must the seller or the purchaser notify obligors of the sale of receivables in order for the sale to be effective against the obligors and/or creditors of the seller? Must the seller or the purchaser obtain the obligors' consent to the sale of receivables in order for the sale to be an effective sale against the obligors? Whether or not notice is required to perfect a sale, are there any benefits to giving notice – such as cutting off obligor set-off rights and other obligor defences?

In relation to the notification of the assignment to the debtor or the debtor's acceptance of the assignment, please refer to question 4.2. above.

The assigned obligor's consent is not generally required. However, (i) the debtor's consent may be required in case of contractual limitation to the transfer of the receivables, and (ii) the notification to, or the acceptance by, the assigned debtor of the assignment may have some consequences in relation to its set-off rights. In this respect, please refer to question 4.13 below.

4.5 Notice Mechanics. If notice is to be delivered to obligors, whether at the time of sale or later, are there any requirements regarding the form the notice must take or how it must be delivered? Is there any time limit beyond which notice is ineffective – for example, can a notice of sale be delivered after the sale, and can notice be delivered after insolvency proceedings have commenced against the obligor or the seller? Does the notice apply only to specific receivables or can it apply to any and all (including future) receivables? Are there any other limitations or considerations?

In relation to the time limit beyond which a notice is ineffective, there is no specific provision under Italian law.

However, please consider that:

(i) in case the receivables are assigned to more than one transferee, please refer to question 4.2 above;

(ii) according to Article 2914 of the Italian Civil Code, the assignments of receivables notified to or accepted by the relevant obligor after the foreclosure (*pignoramento*) are ineffective in prejudice of the foreclosing creditor; and

(iii) Royal Decree No. 267 of 16 March 1942 (the "**Italian Bankruptcy Law**") provides for certain provisions in relation to the time limit of a transaction in the insolvency context. In addition to "suspect period" provisions of Articles 65 and 67 (in this respect, please refer to question 6.3 below), Article 45 of the Italian Bankruptcy Law specifies that any formality that is necessary to make a transaction enforceable *vis-à-vis* third parties shall have no effect against the creditors if completed after the date of declaration of bankruptcy.

To the extent that more than one receivable or future receivables are assigned, an assignment notice may be given for all the relevant assigned receivables. In case of future receivables, the relevant notice shall be delivered once the relevant deed of assignment has been entered into and the relevant receivables have arisen. In addition, please consider that specific rules regarding the assignment of future receivables are set out in the Italian Factoring Law as specified in question 4.11 below.

4.6 Restrictions on Assignment – General Interpretation. Will a restriction in a receivables contract to the effect that "None of the [seller's] rights or obligations under this Agreement may be transferred or assigned without the consent of the [obligor]" be interpreted as prohibiting a transfer of receivables by the seller to the purchaser? Is the result the same if the restriction says "This Agreement may not be transferred or assigned by the [seller] without the consent of the [obligor]" (i.e., the restriction does not refer to rights or obligations)? Is the result the same if the restriction says "The obligations of the [seller] under this Agreement may not be transferred or assigned by the [seller] without the consent of the [obligor]" (i.e., the restriction does not refer to rights)?

According to Article 1260, paragraph 2, of the Italian Civil Code, the parties may prevent the assignment of the receivables; however, such clause is enforceable against the assignee only if it can be proved that such assignee was aware of such limitation clause at the time of the assignment.

Generally, prohibitions on assigning the agreement do not necessarily prevent the assigning of the receivables; however, a case-by-case analysis should be carried out.

In addition, Article 1260 of the Italian Civil Code provides for additional restrictions on transfer of receivables ((i) the assignment of receivables should not be forbidden by law or (ii) the receivables should not be of a strictly personal nature (*carattere strettamente personale*)).

4.7 Restrictions on Assignment; Liability to Obligor. If any of the restrictions in question 4.6 are binding, or if the receivables contract explicitly prohibits an assignment of receivables or "seller's rights" under the receivables contract, are such restrictions generally enforceable in your jurisdiction? Are there exceptions to this rule (e.g., for contracts between commercial entities)? If your jurisdiction recognises restrictions on sale or assignment of receivables and the seller nevertheless sells receivables to the purchaser, will either the seller or the purchaser be liable to the obligor for breach of contract or tort, or on any other basis?

When the seller sells the receivables to a purchaser in breach of a contractual clause preventing the assignment of such receivables, the seller would generally be liable for any damages deriving from such breach (also *vis-à-vis* the assigned debtor if the contractual provisions required the consent of such debtor).

In this respect, please also refer to question 4.6 above.

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4.8 Identification. Must the sale document specifically identify each of the receivables to be sold? If so, what specific information is required (e.g., obligor name, invoice number, invoice date, payment date, etc.)? Do the receivables being sold have to share objective characteristics? Alternatively, if the seller sells *all* of its receivables to the purchaser, is this sufficient identification of receivables? Finally, if the seller sells *all* of its receivables *other than* receivables owing by one or more specifically identified obligors, is this sufficient identification of receivables?

Under a general principle of Italian law, the object (*oggetto*) is an essential requirement of each contract, and must be identified or identifiable. As a consequence, certain information relating to the receivables is typically provided in assignment agreements (*e.g.* including the details on the assigned debtors, the contracts from which the receivables are originated, the purchase price, the payment date and any security interests).

In addition, according to Article 1262 of the Italian Civil Code, the transferor shall deliver to the transferee any document in its possession evidencing the receivables.

In the context of securitisation transactions, the receivables shall be identified as a pool (*individuabili in blocco*) (*e.g.* common elements of identification (so-called "criteria") must be specified in the transfer agreement), when they consist of a plurality of claims identified as credits, in accordance with Article 58 of the Italian Consolidated Banking Law and the provisions set out by the Bank of Italy.

4.9 Recharacterisation Risk. If the parties describe their transaction in the relevant documents as an outright sale and explicitly state their intention that it be treated as an outright sale, will this description and statement of intent automatically be respected or is there a risk that the transaction could be characterised by a court as a loan with (or without) security? If recharacterisation risk exists, what characteristics of the transaction might prevent the transfer from being treated as an outright sale? Among other things, to what extent may the seller retain any of the following without jeopardising treatment as an outright sale: (a) credit risk; (b) interest rate risk; (c) control of collections of receivables; (d) a right of repurchase/redemption; (e) a right to the residual profits within the purchaser; or (f) any other term?

Under a general principle of Italian law, the courts are not bound by the qualification given by the parties. However, the common intention of the parties (also resulting from their overall behaviour) is a criterion of interpretation to be taken into account by Italian courts.

Therefore, in the envisaged scenario, assuming that the receivables purchase price is fair (or not excessively low) and that the relevant assignment agreement has all the features which are customary for these transactions, the Italian Courts would consider the transaction as an outright sale.

Following the perfection of the assignment, the seller may still have certain connections with the receivables (*e.g.* retaining credit or rate interest risks (by a derivative agreement), controlling of collections of receivables (by a servicing agreement), or may have a right of repurchase) which generally do not jeopardise the outright sale if all the conditions required by the law for a valid assignment were previously met. However, a case-by-case analysis should be carried out.

4.10 Continuous Sales of Receivables. Can the seller agree in an enforceable manner to continuous sales of receivables (i.e., sales of receivables as and when they arise)? Would such an agreement survive and continue to transfer receivables to the purchaser following the seller's insolvency?

In Italy: (1) the parties (a) can freely determine the contents of the contract in compliance with the law, (b) are free to enter into a contract different from those specifically set out by the Italian Civil Code, provided that the contract aims to regulate interests that are worthy of protection; and (2) future receivables can be transferred (please refer to question 4.11 below). Therefore, the seller may agree to the continuous sale of receivables.

However, a seller's insolvency can affect the enforceability of such continuous sales of receivables. In particular:

(i) according to Article 72 of the Italian Bankruptcy Law, if a contract has not yet been carried out or not been completed by both parties when one of the parties is declared bankrupt, the execution of the contract remains suspended until the insolvency official (*curatore*), with authorisation from the creditors' committee, decides alternatively to (A) replace the bankrupt party in the contract, assuming all the obligations arising therefrom, or (B) terminate the contract;

(ii) according to Article 74 of the Italian Bankruptcy Law, if the insolvency official replaces a party in a continuous or periodic execution contract, it must also fully pay the price for the services already provided; and

(iii) clawback action should be also considered (please refer to question 6.3 below).

4.11 Future Receivables. Can the seller commit in an enforceable manner to sell receivables to the purchaser that come into existence after the date of the receivables purchase agreement (e.g., "future flow" securitisation)? If so, how must the sale of future receivables be structured to be valid and enforceable? Is there a distinction between future receivables that arise prior to *versus* after the seller's insolvency?

Under Italian law, the seller can commit in an enforceable manner to sell future receivables, provided that the receivables transfer agreement has been validly entered into between the parties and the receivables are identified or identifiable at the date of the agreement. The future receivables will be transferred to the purchaser only when they will come into existence.

In addition, please consider that:

(i) under the Italian Securitisation Law, securitisation of future receivables is expressly permitted; and

(ii) the Italian Factoring Law expressly states that: (a) the receivables can be assigned also prior to the conclusion of the relevant agreement from which they will derive; and (b) the assignment of future receivables in mass (*in massa*) shall take place only in relation to the receivables that will derive from contracts to be executed no later than 24 months from the date of the transfer agreement.

Please consider that, subject to certain limitations set forth under the Italian Factoring Law, assignments of future receivables shall not be effective and enforceable against the purchaser in the case of bankruptcy of the seller.

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4.12 Related Security. Must any additional formalities be fulfilled in order for the related security to be transferred concurrently with the sale of receivables? If not all related security can be enforceably transferred, what methods are customarily adopted to provide the purchaser the benefits of such related security?

According to Article 1263 of the Italian Civil Code, in the case of assignment of a receivable, any privilege, guarantee, security interest or other ancillary right is simultaneously transferred to the assignee.

In addition, pursuant to Italian Securitisation Law and Article 58 of the Italian Consolidated Banking Law, any privilege or security interests related to the assigned receivables are transferred to the assignee and preserve their validity and rank for the benefit of the assignee without the need of any additional formalities or annotation.

4.13 Set-Off; Liability to Obligor. Assuming that a receivables contract does not contain a provision whereby the obligor waives its right to set-off against amounts it owes to the seller, do the obligor's set-off rights terminate upon its receipt of notice of a sale? At any other time? If a receivables contract does not waive set-off but the obligor's set-off rights are terminated due to notice or some other action, will either the seller or the purchaser be liable to the obligor for damages caused by such termination?

In relation to the assigned debtor's set-off rights, according to Article 1248 of the Italian Civil Code: (i) if the debtor has accepted the assignment, it cannot exercise any set-off right *vis-à-vis* the assignee (that it could have exercised *vis-à-vis* the assignor), and (ii) if the assignment has been notified to (but not accepted by) the debtor, the debtor cannot exercise the set-off right *vis-à-vis* the assignee in relation to the receivables arisen after the date of the notification.

In the context of securitisation transactions, the limit referred to in sub-paragraph (ii) above applies from the date of the publication of the notice of the assignment in the Official Gazette, or from the date certain at law on which the purchase price has been paid (*e.g.* the assigned debtors cannot exercise any set-off rights between the receivables purchased by the relevant Italian Securitisation Law special purpose vehicle (the "**SPV**") and the receivables owed by such assigned debtors to the seller which have arisen after such date).

4.14 Profit Extraction. What methods are typically used in your jurisdiction to extract residual profits from the purchaser?

According to the Italian Securitisation Law, when the notes issued by the SPV are offered to professional investors, the prospectus shall contain, *inter alia*, estimates of the transaction's profits and the beneficiary of such profits.

In the context of Italian securitisation transactions, the methods typically used to extract residual profits include:

(i) subscription of junior notes;

(ii) payment of a deferred consideration on the receivables; and

(iii) payment of (servicer or swap counterparties) fees to the originator.

5 Security Issues

5.1 Back-up Security. Is it customary in your jurisdiction to take a "back-up" security interest over the seller's ownership interest in the receivables and the related security, in the event that an outright sale is deemed by a court (for whatever reason) not to have occurred and have been perfected (see question 4.9 above)?

Please note that this is not customary in Italy.

5.2 Seller Security. If it is customary to take back-up security, what are the formalities for the seller granting a security interest in receivables and related security under the laws of your jurisdiction, and for such security interest to be perfected?

Please refer to question 5.1 above.

5.3 Purchaser Security. If the purchaser grants security over all of its assets (including purchased receivables) in favour of the providers of its funding, what formalities must the purchaser comply with in your jurisdiction to grant and perfect a security interest in purchased receivables governed by the laws of your jurisdiction and the related security?

As a general note, please note that Article 2800 *et seq.* of the Italian Civil Code set out the provisions in relation to pledges over receivables, providing that, *inter alia*, the relevant priority is effective only when (i) the relevant pledge results from a written deed, and (ii) the creation of such pledge has been notified to the relevant debtor (of the pledged receivable) or has been accepted by it in writing with a document bearing the date certain at law.

5.4 Recognition. If the purchaser grants a security interest in receivables governed by the laws of your jurisdiction, and that security interest is valid and perfected under the laws of the purchaser's jurisdiction, will the security be treated as valid and perfected in your jurisdiction or must additional steps be taken in your jurisdiction?

In accordance with Article 51 of the Italian Private International Law, security interests over assets are governed by the law of the jurisdiction in which the relevant assets are located.

In addition, pursuant to the Rome I Regulation, the relationship between assignor and assignee under a voluntary assignment of a receivable shall be governed by the law that applies to the relevant contract between the assignor and assignee. In accordance with Article 14 of Rome I Regulation, the law governing the assigned receivable shall determine, *inter alia*, its assignability and the relationship between the assignee and the debtor. The concept of assignment also includes outright transfers of receivables, transfers of receivables by way of security and pledges or other security rights over such receivables.

In light of the above, in relation to receivables governed by Italian law, the relevant parties have to create a valid and perfected security interest in accordance with the Italian law provisions.

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5.5 Additional Formalities. What additional or different requirements apply to security interests in or connected to insurance policies, promissory notes, mortgage loans, consumer loans or marketable debt securities?

Please note that there are no specific requirements or additional formalities expressly provided for security interests in or connected to insurance policies, promissory notes, mortgage loans, consumer loans or marketable debt securities and, therefore, the general Italian law provisions on security interests shall apply.

5.6 Trusts. Does your jurisdiction recognise trusts? If not, is there a mechanism whereby collections received by the seller in respect of sold receivables can be held or be deemed to be held separate and apart from the seller's own assets (so that they are not part of the seller's insolvency estate) until turned over to the purchaser?

The trust is a common law institution which – for several years – has not been recognised by the Italian legal framework.

The Republic of Italy has implemented the Hague Convention on the law applicable to trusts and their recognition of 1 July 1985 and, as a consequence, the trusts created under foreign law may also be recognised and enforceable in Italy subject to certain conditions and requirements.

However, it shall be noted that there is no consolidated case law in Italy on the recognition of trusts.

In relation to the segregation principle provided by the Italian Securitisation Law, please refer to question 7.3 below.

5.7 Bank Accounts. Does your jurisdiction recognise escrow accounts? Can security be taken over a bank account located in your jurisdiction? If so, what is the typical method? Would courts in your jurisdiction recognise a foreign law grant of security (for example, an English law debenture) taken over a bank account located in your jurisdiction?

An escrow account may be constituted in Italy typically through the creation of a pledge over the sums credited on such account.

Such a pledge can generally be created in accordance with the provisions of the Italian Civil Code and/or – when the relevant conditions required by the law are met – pursuant to Legislative Decree No. 170 of 21 May 2004 (the "**Decree 170**") (which allows a more efficient management of the pledged assets and provides for certain advantages in relation to the perfection formalities and the enforceability of the pledge).

In relation to bank accounts, another solution that is common in the Italian market practice is the creation of a pledge directly over the bank account (and not over a specific deposited amount). In this case, such a pledge is deemed a pledge over receivables (of the pledgor against the relevant bank) and a particular regime – in relation to notification and perfection formalities, as identified also by the scholars and the courts in case law – shall apply.

In relation to the recognition in Italy of a foreign law grant of security taken over a bank account located in Italy, please refer to question 5.4 above.

5.8 Enforcement over Bank Accounts. If security over a bank account is possible and the secured party enforces that security, does the secured party control all cash flowing into the bank account from enforcement forward until the secured party is repaid in full, or are there limitations? If there are limitations, what are they?

As a general note, following the occurrence of an enforcement event specified in the relevant security documents, the secured creditor may use the pledged amounts or apply the proceeds of the monetary receivables (of the pledgor) arising from the balance of the pledged account towards discharge of the secured obligations and in order to satisfy its credit.

The pledge, and any other security interest, give to the secured creditors a right to be satisfied (over the pledged assets) with priority on the other non-secured creditors.

However, such privileged creditors may be subject to certain limitations relating to the Italian Bankruptcy Law provisions. In particular, as a general rule of Italian insolvency law, the creation of security instruments may be subject to clawback by the insolvency official of the grantor. In this respect, please also refer to question 6.3 below.

In addition, in the event of bankruptcy proceedings commenced against a pledgor:

(i) the secured creditor will be considered a privileged creditor in respect of the amounts credited on the account as of the date of the commencement of the proceedings, but all monetary rights which come into existence after the commencement of the proceedings might be deemed to be part of the pledgor's bankruptcy estate and, therefore, available for distribution to all of its creditors, regardless of the security originally created in favour of the pledgee;

(ii) the pledgee is allowed to enforce the pledge only after: (a) the existence and validity of its claim against the pledgor and of the pledge has been recognised by the judge who is following the relevant insolvency proceeding, and (b) such judge has authorised the sale of the pledged assets; and

(iii) the perfection of the pledge does not prevent any third-party creditor of the pledgor from seeking attachment or execution against the claims over which the pledges have been constituted to satisfy its unpaid claims against the pledgor. Third-party creditors may seek the forced sale of the pledged claims, although the secured creditors would remain entitled to share the proceeds of such sale in accordance with their relative ranking in terms of priority (*diritto di prelazione*) pursuant to applicable law.

Decree 170 sets forth a specific regime applicable to pledges created in accordance with such provisions.

In particular, *inter alia*, Article 4 of Decree 170 specifies that, upon the occurrence of an enforcement event and also in an insolvency scenario, the beneficiary/pledgee may withhold the amount standing on the pledged account to discharge the secured obligations.

Moreover, Article 9 of Decree 170 provides that the security interest created pursuant to such decree cannot be declared ineffective towards the relevant secured creditor upon (and as a consequence of) the commencement of an insolvency procedure.

5.9 Use of Cash Bank Accounts. If security over a bank account is possible, can the owner of the account have access to the funds in the account prior to enforcement without affecting the security?

In standard financing transactions, the owner of the account is usually

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entitled to use the pledged funds in accordance with the terms and conditions (and the instructions) provided for in the relevant deed of pledge, intercreditor agreement or finance documents until the occurrence of an enforcement event or an event or default.

In addition, under Italian law it is also possible to create so-called "irregular pledges" (Article 1851 of the Italian Civil Code), whereby (i) a certain amount is credited by the pledgor on a beneficiary/pledgee's account, (ii) the ownership of such amount is transferred to the pledgee, which may use such amount, (iii) the pledgee has an obligation to give back to the pledgor the pledged amount if no enforcement event occurs.

6 Insolvency Laws

6.1 Stay of Action. If, after a sale of receivables that is otherwise perfected, the seller becomes subject to an insolvency proceeding, will your jurisdiction's insolvency laws automatically prohibit the purchaser from collecting, transferring or otherwise exercising ownership rights over the purchased receivables (a "stay of action")? If so, what generally is the length of that stay of action? Does the insolvency official have the ability to stay collection and enforcement actions until he determines that the sale is perfected? Would the answer be different if the purchaser is deemed to only be a secured party rather than the owner of the receivables?

The Italian Bankruptcy Law does not include specific provisions that automatically prohibit the purchaser from collecting, transferring or otherwise exercising ownership rights over the receivables which have been purchased before the seller becomes subject to an insolvency proceeding.

However, please consider that, in accordance with Chapter III, Section III, of the Italian Bankruptcy Law, the insolvency official may obtain the clawback (*revoca*) of certain transactions (including payments of receivables or granting of security interests) carried out by the bankrupt during the so-called "suspect period" (*periodo sospetto*). In this respect, please refer to question 6.3 below.

6.2 Insolvency Official's Powers. If there is no stay of action, under what circumstances, if any, does the insolvency official have the power to prohibit the purchaser's exercise of its ownership rights over the receivables (by means of injunction, stay order or other action)?

Under the Italian Bankruptcy Law the insolvency official does not have specific powers to prohibit the purchaser exercising its ownership rights over the purchased receivables.

However, as anticipated, please consider that the insolvency official may apply for a clawback action. In this respect, please refer to question 6.3 below.

6.3 Suspect Period (Clawback). Under what facts or circumstances could the insolvency official rescind or reverse transactions that took place during a "suspect" or "preference" period before the commencement of the seller's insolvency proceedings? What are the lengths of the "suspect" or "preference" periods in your jurisdiction for (a) transactions between unrelated parties, and (b) transactions between related parties? If the purchaser is majority-owned or controlled by the seller or an affiliate of the seller, does that render sales by the seller to the purchaser "related party transactions" for purposes of determining the length of the suspect period? If a parent company of the seller guarantee's the performance by the seller of its obligations under contracts with the purchaser, does that render sales by the seller to the purchaser "related party transactions" for purposes of determining the length of the suspect period?

As a general rule, the Italian Bankruptcy Law distinguishes between: (i) acts or transactions which are ineffective *vis-à-vis* creditors by operation of law, and (ii) acts or transactions which are ineffective at the request of the insolvency official, as detailed below:

(i) acts ineffective by operation of law:
   - (a) under Article 64 of the Italian Bankruptcy Law, all transactions entered into for no consideration are ineffective *vis-à-vis* creditors if entered into by the debtor in the two-year period prior to the declaration of bankruptcy; and
   - (b) under Article 65 of the Italian Bankruptcy Law, payments of debts due on the day of the declaration of bankruptcy or thereafter are ineffective *vis-à-vis* creditors if made by the debtor in the two-year period prior to the declaration of bankruptcy;

(ii) acts which could be clawed back (*e.g.* declared ineffective) at the request of the insolvency official (Article 67 of the Italian Bankruptcy Law):
   - (a) the following acts and transactions may be clawed back, unless the other party proves that it had no (actual or constructive) knowledge of the debtor's insolvency:
     - (1) the onerous transactions entered into in the year preceding the declaration of bankruptcy, where the obligations performed or undertaken by the debtor exceed by more than a quarter what the debtor received;
     - (2) payments of debts, due and payable, made by the debtor, which were not paid in cash or by other customary means of payment in the year preceding the declaration of bankruptcy;
     - (3) pledges and mortgages granted by the bankrupt entity in the year preceding the declaration of bankruptcy in order to secure pre-existing debts which are not already due;
     - (4) pledges and mortgages granted by the bankrupt entity in the six months preceding the declaration of bankruptcy, in order to secure debts which are due; and
   - (b) the following acts and transactions may be clawed back if the insolvency official proves that the other party knew that the bankrupt entity was insolvent at the time of the act or transaction:

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(1) the payments of debts that are immediately due and payable and any onerous transactions entered into or made in the six months preceding the declaration of bankruptcy; and

(2) the granting of security interests securing debts (even those of third parties), contextually created, and made in the six months preceding the declaration of bankruptcy.

Please note that Italian Securitisation Law provides for specific exceptions to the general provisions above. In particular, according to Article 4 of the Italian Securitisation Law:

(A) the clawback provisions set forth in Articles 65 and 67 of the Italian Bankruptcy Law will not apply to payments made by the debtors to the relevant SPV in respect of the assigned receivables; and

(B) the one-year and six-month suspect periods as provided by Article 67 of the Italian Bankruptcy Law are reduced, respectively, to six months and three months.

In addition, the lengths of the suspect periods provided by the Italian Bankruptcy Law provisions do not change in case of transactions between unrelated parties and transactions between related parties and, therefore, the general provisions detailed above shall apply.

6.4 Substantive Consolidation. Under what facts or circumstances, if any, could the insolvency official consolidate the assets and liabilities of the purchaser with those of the seller or its affiliates in the insolvency proceeding? If the purchaser is owned by the seller or by an affiliate of the seller, does that affect the consolidation analysis?

The principle of "substantive consolidation" is not recognised by Italian insolvency law and, accordingly, the insolvency of a parent company does not automatically result in or imply the insolvency of its subsidiary. As a consequence, under no circumstances could the insolvency official consolidate the assets and liabilities of the purchaser with those of the seller or its affiliates in the insolvency proceeding, even though the purchaser is owned by the seller or its affiliate.

The fact that the purchaser is owned by the seller or its affiliate may be relevant in case of clawback action under Article 67 of the Italian Bankruptcy Law, since proving that the purchaser had no (actual or constructive) knowledge of the debtor's insolvency might be difficult to demonstrate.

6.5 Effect of Insolvency on Receivables Sales. If insolvency proceedings are commenced against the seller in your jurisdiction, what effect do those proceedings have on (a) sales of receivables that would otherwise occur after the commencement of such proceedings, or (b) on sales of receivables that only come into existence after the commencement of such proceedings?

After a declaration of insolvency, in no circumstances could a sales of receivables occur.

In addition, assignments of future receivables shall not be effective and enforceable against the receiver in the case of bankruptcy of the seller.

6.6 Effect of Limited Recourse Provisions. If a debtor's contract contains a limited recourse provision (see question 7.3 below), can the debtor nevertheless be declared insolvent on the grounds that it cannot pay its debts as they become due?

The limited recourse provision contained in securitisation transactions should be considered an "atypical" contractual provision (and not as a limitation of liability, which is prohibited under Article 2740, paragraph 2 of the Italian Civil Code).

Such provisions should be valid and legally binding under Italian law among the relevant parties of the agreement and, therefore, would give right to a claim for damages in case of breach; however, it is debatable if such provisions can be considered enforceable *vis-à-vis third parties* (*e.g.* the insolvency official).

In relation to the enforceability of limited recourse and non-petition provisions, please refer to questions 7.4 and 7.5 below.

7 Special Rules

7.1 Securitisation Law. Is there a special securitisation law (and/or special provisions in other laws) in your jurisdiction establishing a legal framework for securitisation transactions? If so, what are the basics? Is there a regulatory authority responsible for regulating securitisation transactions in your jurisdiction?

The Italian Securitisation Law is the special law that establishes a specific legal framework for the securitisation transactions carried out in Italy. The Italian Securitisation Law applies to all transactions carried out through the transfer for consideration to an SPV of existing or future monetary receivables identifiable as a pool (*individuabili in blocco*) on the basis of objective criteria specified in the relevant transfer agreement. The purchase price of such receivables will be funded through the issue by the SPV of notes that will be repaid through the collections deriving from the underlying receivables.

The Italian SPVs:

(i) are corporate, typically incorporated as "*società a responsabilità limitata*" under the laws of the Republic of Italy in accordance with Article 3 of the Italian Securitisation Law;

(ii) in case the SPV is incorporated as a "*società a responsabilità limitata*", it has a minimum corporate capital equal to EUR 10,000;

(iii) are enrolled with a special register held by the Bank of Italy (the "**SPV Register**"); and

(iv) have as their sole corporate object the performance of securitisation transactions in accordance with the Italian Securitisation Law.

In addition to the above, under Article 3, paragraph 2, of the Italian Securitisation Law, all receivables related to each securitisation transaction carried out by the relevant SPV, including not only the specific portfolio of receivables purchased by the SPV but also the cash flow arising from the collections of such receivables and all financial activities that have been purchased using such collections, are assets segregated from all other assets of the SPV and from the cash flows generated from any other securitisation transaction.

The Italian Securitisation Law was amended by Law Decree No. 91 of 24 June 2014 with the purpose of making the SPVs eligible to provide loans to entities other than individuals and micro-enterprises, provided that: (i) the borrowers are selected by a bank or financial intermediary enrolled with a special register held by the Bank of Italy pursuant to Article 106 of the Italian Consolidated Banking Law (the "**106 Register**"), which can also act as "*soggetto incaricato per i servizi di riscossione dei crediti ceduti e dei servizi di cassa e di pagamento*" pursuant to Article 2, paragraph 3, letter (c) and paragraph 6 and 6-*bis* of the Italian Securitisation Law, by carrying out all collection activities related to the receivables; (ii) the

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notes issued by the SPV to obtain the financial resources necessary for the provision of the loans are intended for qualified investors, as defined in Article 100 of the Italian Consolidated Financial Law; and (iii) the bank or financial intermediary that identify and assess the borrower retain a "*significant economic interest*" in the transaction, in line with the terms and procedures detailed in the implementing provisions of the Bank of Italy.

On 15 June 2017, the Italian Parliament enacted new measures which amended the Italian Securitisation Law (introducing Article 7.1) and significantly expanding SPVs' operations, in order to facilitate the sale of impaired receivables transferred by banks or financial intermediaries enrolled under the 106 Register having registered office in Italy. In this respect, please refer to question 8.7 below.

The Bank of Italy is the regulatory authority responsible for regulating securitisation transactions carried out in Italy.

7.2 Securitisation Entities. Does your jurisdiction have laws specifically providing for establishment of special purpose entities for securitisation? If so, what does the law provide as to: (a) requirements for establishment and management of such an entity; (b) legal attributes and benefits of the entity; and (c) any specific requirements as to the status of directors or shareholders?

The Italian Securitisation Law provides for establishment of special purpose entities (*SPVs*) for securitisation and, in particular, Article 3 provides specific requirements for its establishment and management.

The Bank of Italy's administrative measure of 7 June 2017 provides for (i) some disclosure requirements and statistical reporting obligations for Italian SPVs pursuant to Regulation (EU) No. 1075/2013 of the European Central Bank, and (ii) measures for the establishment of the SPV Register and the relevant rules for the registration and cancellation of the SPVs therefrom. In particular, immediately upon purchasing a portfolio of receivables from the assignor, newly-established SPVs must apply for registration in the SPV Register.

The Italian Securitisation Law provides for a more favourable regime applicable to the SPVs, including in respect of tax, segregation of assets (please refer to question 7.3 below) and clawback of payments.

Finally, under Italian law there are no specific mandatory requirements as to the status of directors or shareholders of SPVs other than those generally applicable in accordance with the Italian Civil Code.

7.3 Location and form of Securitisation Entities. Is it typical to establish the special purpose entity in your jurisdiction or offshore? If in your jurisdiction, what are the advantages to locating the special purpose entity in your jurisdiction? If offshore, where are special purpose entities typically located for securitisations in your jurisdiction? What are the forms that the special purpose entity would normally take in your jurisdiction and how would such entity usually be owned?

Regarding Italian securitisation transactions, it is typical to establish the SPV under the laws of the Republic of Italy, as a consequence of certain legal and tax advantages from which such an entity benefits.

In particular, the main benefits of locating the SPV in Italy regard the segregation of its assets pursuant to Article 3 of the Italian Securitisation Law and a favourable applicable tax regime.

In relation to the segregation provision, the receivables relating to each of the transactions, the relevant collections and the financial assets purchased through such collections form separate assets from any other asset of the SPV and from those relating to any other transactions. On each separate asset, therefore, no actions are permitted by creditors other than the holders of the notes issued in order to finance the purchase of such receivables. In addition, no actions by entities other than the holders of the notes are permitted in respect of the accounts opened in the name of the SPV, pursuant to the ancillary activities performed under each securitisation transaction or otherwise pursuant to the transaction documents. The amounts credited on such accounts shall be used by the SPV solely for the purpose of discharging the claims due to the holder of the notes, as well as paying the other transaction costs and expenses.

Should any of the proceedings referred to in Title IV of the Italian Consolidated Banking Law or any insolvency proceedings be commenced in respect of the relevant custodian (*depositario*), the amounts deposited in such accounts and those credited during the course of the relevant proceeding shall not be subject to any suspension of payments, and shall be immediately and fully paid back to the SPV without the need to file any petition (*domanda di ammissione al passivo o di rivendica*) and outside of the distribution plans or the sums' repayment plans.

In relation to the favourable tax regime, pursuant to Article 6, paragraph 1, of the Italian Securitisation Law, payments of interest and other proceeds in respect of the notes issued in the context of the securitisation are subject to the fiscal regime set forth by Legislative Decree No. 239 of 1996. With regards to tax regimes, please also refer to question 9 below.

According to Article 3, paragraph 3, of the Italian Securitisation Law and the provisions contained in Title V of the Italian Consolidated Banking Law, an Italian SPV may be incorporated both as a joint stock company or limited liability company, having as its sole corporate object only the realisation of securitisation transactions.

Italian SPVs frequently have a sole quota holder and a sole director (or a board of directors of three or five directors). The quota holder may be an Italian company or, alternatively, in some securitisation transactions, a non-Italian foundation (for instance, a "*stichting*" incorporated under the laws of the Netherlands).

7.4 Limited-Recourse Clause. Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) limiting the recourse of parties to that agreement to the available assets of the relevant debtor, and providing that to the extent of any shortfall the debt of the relevant debtor is extinguished?

A limited recourse clause could be construed as (i) a provision for the determination of the amount actually payable by the debtor on the relevant payment date, in the sense that the amount originally due by the debtor can be reduced correspondingly to the funds available to such debtor on the relevant payment date, or (ii) a covenant (*pactum de non petendo*), under which creditors of the debtor agree not to enforce their obligations for an amount in excess of the liquidity from time to time available to the obligor for the purpose of making the relevant payments. Such provisions should be valid and binding under Italian law, in the sense that they would give right to a claim for damages in case of breach. It should be noted that limited recourse loans are expressly contemplated by Article 2447-*decies* of the Italian Civil Code.

A limited recourse clause contained in the transaction documents related to a securitisation may be recognised as valid and binding

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under Italian law by a court, provided that such clause would not be interpreted in the sense that it constitutes a limitation of liability, which is prohibited under Article 2740, paragraph 2, of the Italian Civil Code, but rather as an "atypical" contractual provision, the legality of which should be evaluated in the light of its conformity to mandatory provisions and general principles of Italian law.

7.5 Non-Petition Clause. Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) prohibiting the parties from: (a) taking legal action against the purchaser or another person; or (b) commencing an insolvency proceeding against the purchaser or another person?

Non-petition clause (pursuant to which a creditor of the SPV agrees not to institute against or adhere in instituting against the SPV any bankruptcy, reorganisation, arrangement, insolvency or liquidation proceedings or join as a party to any such proceeding already instituted) is valid and binding under Italian law, in the sense that such clause would give rise to a claim for damages in case of breach, although it would not necessarily prevent proceedings commenced in breach of such non-petition clause from being deemed to have been validly commenced.

All creditors which have agreed to a non-petition clause would contractually be prevented from commencing such proceedings, provided that no fraud or misconduct has occurred on the part of the SPV's management, or of any party acting on its behalf.

However, under Italian bankruptcy rules, the public prosecutor can commence such proceedings upon its own initiative, without having being solicited by a creditor of the relevant company. Any petition filed by a creditor that has agreed on a non-petition clause would be deemed to have been validly filed notwithstanding non-petition clauses.

7.6 Priority of Payments "Waterfall". Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) distributing payments to parties in a certain order specified in the contract?

The subordination and order of priority clauses contained in the transaction documents related to a securitisation would be valid and binding under Italian law.

Even if there is no case law on this specific matter and, therefore, there is some uncertainty as to the relationship between subordination and the principle of *pari passu* ranking of creditors in any insolvency proceedings, order of priority clauses under which the noteholders agree to subordinate their rights to the rights of other creditors of the SPV would be recognised and enforceable by Italian courts as the benefits of Article 3 of the Italian Securitisation Law may in fact be postponed by the parties in favour of which they are given, *e.g.* by the noteholders (no judicial or other interpretation has yet been given on this matter).

It should be further noted that if a receiver or insolvency official disregards the subordination provisions contained in a transaction document, it should (subject to the provisions of the relevant transaction document) pay all amounts due to all the creditors who are a party to the transaction documents to the relevant representative of the noteholders, who would then be obliged to comply with the applicable priority of payments.

7.7 Independent Director. Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) or a provision in a party's organisational documents prohibiting the directors from taking specified actions (including commencing an insolvency proceeding) without the affirmative vote of an independent director?

In Italy, only in relation to all listed companies, Article 147-*ter*, paragraph 3, of the Italian Consolidated Financial Law requires the appointment of at least an independent director (two if the board of directors is composed of more than seven directors) that must meet the independence requirements for statutory auditors established by Article 148, paragraph 3, of the Italian Consolidated Financial Law.

Regarding all other types of company, the appointment of independent directors is not mandatory. However, the by-laws may provide that for certain reserved matters, the affirmative vote of an independent director is necessary. Therefore, for these reserved matters, a resolution of the board of directors cannot be adopted without the affirmative vote of independent director(s), despite the majorities provided by Article 2388 of the Italian Civil Code.

In light of the above, an Italian court could give effect to those provisions contained in by-laws prohibiting the directors from taking specified actions without the affirmative vote of independent directors.

7.8 Location of Purchaser. Is it typical to establish the purchaser in your jurisdiction or offshore? If in your jurisdiction, what are the advantages to locating the purchaser in your jurisdiction? If offshore, where are purchasers typically located for securitisations in your jurisdiction?

The SPV, as purchaser of a portfolio of receivables, is typically established in Italy due to many advantages provided by the Italian Securitisation Law and a favourable tax regime that the SPVs enjoy.

In this respect, please refer to question 7.3 above.

8 Regulatory Issues

8.1 Required Authorisations, etc. Assuming that the purchaser does no other business in your jurisdiction, will its purchase and ownership or its collection and enforcement of receivables result in its being required to qualify to do business or to obtain any licence or its being subject to regulation as a financial institution in your jurisdiction? Does the answer to the preceding question change if the purchaser does business with more than one seller in your jurisdiction?

According to Article 106 of the Italian Consolidated Banking Law, "granting of loans" (under any form) activities qualify as a reserved activity – and, as such, shall be carried out exclusively by authorised financial intermediaries enrolled in the 106 Register – when it is performed towards the public (*e.g.* when performed towards third parties on a professional basis).

The activities falling within the definition of "granting of loans activity" ("*attività di concessione di finanziamenti*") are specified in the Italian Ministerial Decree No. 53/2015 (the "**MD 53**"), which include, *inter alia*, the "purchase of receivables for a valuable consideration" ("*acquisto di crediti a titolo oneroso*").

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The requirements, the authorisation regime and the conditions for non-Italian entities to carry out the activities described above are specified in the MD 53 and the Italian Consolidated Banking Law.

In addition, it shall be also considered that, according to Articles 46-*bis et seq.* of the Italian Consolidated Financial Law, Italian and EU alternative investment funds ("**EU AIF**") may carry out investment activities in Italy (both in the form of purchasing credit receivables and providing direct lending) to non-consumer borrowers, in accordance with the provisions specified therein and in the relevant implementing regulation. EU AIF managers intending to engage in direct lending in Italy are required to send a prior communication to the Bank of Italy at least 60 days before starting such activity.

The analysis carried out above does not change if the purchaser does business with more than one seller in Italy.

8.2 Servicing. Does the seller require any licences, etc., in order to continue to enforce and collect receivables following their sale to the purchaser, including to appear before a court? Does a third-party replacement servicer require any licences, etc., in order to enforce and collect sold receivables?

Generally, the receivables recovery activity may be carried out in Italy by:

(i) financial intermediaries enrolled under the 106 Register (which may also carry out any activity connected and/or instrumental to the granting of loans (in any form) activities towards the public); and/or

(ii) receivables collection agencies (*agenize di recupero crediti*) pursuant to Article 115 of the Royal Decree No. 773 of 1931 ("**TULPS**") (which mainly carry out extrajudicial receivables collection activity).

In the context of Italian securitisation transactions, the collection of assigned receivables activities (*riscossione dei crediti ceduti*) and the cash and payments services (*servizi di cassa e di pagamento*) shall be carried out by the servicer. According to Article 2, paragraph 6 of the Italian Securitisation Law, such entity shall be a bank or a financial intermediary enrolled under the 106 Register.

In light of the above, it should be considered that:

(a) should the activities of the seller involve the collection and the management of the assigned receivables, such activities should be carried out by a bank or a financial intermediary enrolled under the 106 Register; and

(b) should the activity of the seller be limited to the recovery of the receivables (*e.g.* the activities generally carried out by the so-called "special servicer"), including extrajudicial activities for the recovery of the receivables and sending communications to the debtors for such purposes, such activities may be carried out by entities authorised pursuant to Article 115 of the TULPS.

The same provisions apply to any third-party replacement servicer.

8.3 Data Protection. Does your jurisdiction have laws restricting the use or dissemination of data about or provided by obligors? If so, do these laws apply only to consumer obligors or also to enterprises?

Any processing of personal data, including the processing of data provided by obligors are subject to data protection laws. In this regard, from 25 May 2018, the Regulation (EU) 2016/679 of the European Parliament and the Council of 27 April 2016, on the protection of natural persons with regard to the processing of personal data and on the free movement of such data (the "**General Data Protection Regulation**" or "**GDPR**") will become fully applicable, introducing a number of changes to European data protection laws.

The GDPR – which will be applicable directly in each EU Member State – imposes its obligations not only on organisations located within the EU, but also on organisations located outside of the EU offering services to or monitoring individuals (including obligors) in the EU.

Organisations will therefore have to, among others, take into account stringent transparency requirements (privacy notice to individuals will be more detailed), additional rights for the individual, new organisational and security measures, new safeguards for the processing of data (such as procedures in order to comply with the principle of privacy by design and by default) and documentary requirements in order to comply with accountability principles falling on any processors.

Lack of compliance with the provisions of the GDPR will determine the application of fines up to EUR 20 million or 4% of the total worldwide annual turnover of the proceeding financial year.

8.4 Consumer Protection. If the obligors are consumers, will the purchaser (including a bank acting as purchaser) be required to comply with any consumer protection law of your jurisdiction? Briefly, what is required?

In the context of a sale of receivables where obligors are qualified as "consumers" pursuant to the Italian Consumers' Code, Article 125-*septies* of the Italian Consolidated Banking Law shall apply. In this respect, please refer to question 1.2 above.

However, in the context of securitisation transactions, the provisions of Article 4 of the Italian Securitisation Law shall apply (and, therefore (i) the obligor will be informed of the sales of receivables through the publication of a notice in the Italian Official Gazette, and (ii) certain limitations of the rights of the obligors, including the right to set off their debts (in derogation from any other provision of law), will apply).

In addition, please consider that the purchaser shall comply with the general applicable principles set out in the Italian Consumers' Code relating to consumers' protection.

8.5 Currency Restrictions. Does your jurisdiction have laws restricting the exchange of your jurisdiction's currency for other currencies or the making of payments in your jurisdiction's currency to persons outside the country?

Assuming that the exchange of currency or the payment to persons in non-EMU countries is effected through the banking system, no restrictions should apply.

8.6 Risk Retention. Does your jurisdiction have laws or regulations relating to "risk retention"? How are securitisation transactions in your jurisdiction usually structured to satisfy those risk retention requirements?

In relation to risk retention, the provisions of the relevant EU regulations (Regulation (EU) No. 575/2013 ("**CRR**") in respect of credit institutions and investment firm investors, Commission Delegated Regulation (EU) No. 231/2013 in respect of AIF managers investors and Commission Delegated Regulation (EU) No. 35/2015 in respect of insurance companies investors) shall apply to Italian securitisation transactions.

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For this reason, should the risk retention requirements apply, Italian securitisation transactions are usually structured with the originator or the arranger holding a net economic interest not less than 5% in the transaction in accordance with Article 405 of the CRR (*e.g.* generally, holding 5% of each tranche of the notes or holding the junior notes).

Please note that the new provisions on risk retention set out in Regulation (EU) No. 2402/2017 will also be applied to Italian securitisations, the securities of which are issued on or after 1 January 2019.

In addition, in the context of Italian securitisation transactions carried out by financings granted by the SPV (and not through the purchase of receivables), Article 1, paragraph 1-*ter*, lett. c) of the Italian Securitisation Law sets out certain conditions which need to be met, including that a bank or financial intermediary (which shall identify and assess the relevant borrowers) shall retain a "significant economic interest" in the transaction, in accordance with the implementing measures adopted by the Bank of Italy with Circular No. 288 of 2015. Such measures include the provisions on (i) economic interest of at least 5% in the transaction, (ii) interest must be retained in the manner set out in the CRR, and (iii) interest must be continuously maintained for the entire duration of the transaction.

8.7 Regulatory Developments. Have there been any regulatory developments in your jurisdiction which are likely to have a material impact on securitisation transactions in your jurisdiction?

The Italian Parliament has recently enacted certain provisions which have amended the Italian Securitisation Law in order to facilitate and promote the securitisations of NPLs receivables.

In particular, the new provisions introduced by Article 7.1 of the Italian Securitisation Law can be summarised as follows:

(i) *NPLs securitisation – loans granted by the SPVs*: in the context of NPLs securitisations, the SPVs (which have purchased the relevant receivables from banks or financial intermediaries enrolled under the 106 Register) may grant loans to the relevant debtors with the purpose of improving their prospects of receivables collection and help them returning *in bonis*.

(ii) *Securitisation in the context of recovery or restructuring plans*: in the context of restructuring agreements or composition or recovery procedures or similar procedures and with the purpose of improving prospects of receivables collection and helping the assigned debtors returning *in bonis*, the SPVs may (i) convert the receivables into equity or quasi-equity instruments (issued by the debtor), and (ii) grant loans to the relevant debtors.

(iii) *Establishment of ReoCo for the purchase of assets and leasing agreements*: in the context of securitisation transactions it may be possible to set up special purpose vehicles, in the form of corporations (a so-called "ReoCo"), with the exclusive scope of purchasing, managing and increasing the value of real estate, registered movable assets and any other asset securing the securitised receivables – including the relevant assets of leasing agreements.

(iv) *Publicity regime*: the NPLs receivables purchased by the SPV which are not identified by block criteria are published through the registration in the relevant Companies Register and the transfer notice publication in the Italian Official Gazette.

9 Taxation

9.1 Withholding Taxes. Will any part of payments on receivables by the obligors to the seller or the purchaser be subject to withholding taxes in your jurisdiction? Does the answer depend on the nature of the receivables, whether they bear interest, their term to maturity, or where the seller or the purchaser is located? In the case of a sale of trade receivables at a discount, is there a risk that the discount will be recharacterised in whole or in part as interest? In the case of a sale of trade receivables where a portion of the purchase price is payable upon collection of the receivable, is there a risk that the deferred purchase price will be recharacterised in whole or in part as interest? If withholding taxes might apply, what are the typical methods for eliminating or reducing withholding taxes?

In general terms, no withholding tax is levied in Italy on the payments made by the obligors to a SPV purchaser, regardless of the nature of the receivables and their characteristics.

In case of sale of trade receivables at a discount or when the payment of a portion of the purchase price is deferred, the amount of the discount or of the deferred payment could be characterised as interest (income from capital) or as capital gain depending on certain factual circumstances that should be verified on a case-by-case basis. In principle, in case the amount is recharacterised as interest, this would be subject to taxation in Italy while in case of capital gain certain exemptions may apply.

With reference to interest paid on the notes issued by the SPV, in general terms, Italian withholding tax may be applied on this interest at the ordinary rate of 26%, unless reduced by the Double Tax Treaty in force between Italy and the country of residence of the subscriber. Certain exemptions are applied when interest is paid to (a) entities resident for tax purpose in a White Listed Country, (b) international entities or bodies set up on the basis of international agreements made executive in Italy, (c) institutional investors set up in a White Listed Country, even if not subject to taxation in their country of establishment or (d) central banks or other bodies managing the official reserve of the state.

9.2 Seller Tax Accounting. Does your jurisdiction require that a specific accounting policy is adopted for tax purposes by the seller or purchaser in the context of a securitisation?

No specific accounting policy is provided for tax purposes. The seller and the purchaser will have to draft the financial statement under the ordinary accounting principle (Italian GAAP or IAS/IFRS as the case may be).

With reference to the seller, the potential loss deriving from the disposal of the receivable should be registered in the financial statement and could be in principle deductible.

With reference to the purchaser, please note that under Italian Securitisation Law and official interpretation of the Tax Authorities, the SPV will not be taxed on the income received from the receivables while the securitisation is in place. In case an amount remains undistributed to the notes subscriber at the end of the transaction, such amount would be subject to ordinary taxation in Italy.

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9.3 Stamp Duty, etc. Does your jurisdiction impose stamp duty or other transfer or documentary taxes on sales of receivables?

Under Italian law, if the sale of receivables is considered a financing transaction, then it would be considered an exempt provision of service and as such it would be subject to registration tax at the fixed amount of EUR 200.

Otherwise, the sale of receivables would fall outside the scope of VAT and consequently registration tax would be applied at the proportional rate of 0.5% on the price paid. In certain circumstances, it could be possible to perform the sale through an exchange of correspondence, so that registration tax would be levied only in "case of use", i.e. in case the deed of sale is filed with an Italian court during an administrative procedure, with Italian administrations or public bodies (unless the filing is mandatory under the law), or otherwise in case such deed is expressly named and referred to in another deed or agreement between the same parties that is subject to registration.

A negligible amount of stamp duty would be due.

9.4 Value Added Taxes. Does your jurisdiction impose value added tax, sales tax or other similar taxes on sales of goods or services, on sales of receivables or on fees for collection agent services?

Under Italian law, VAT is generally applied to the sales of goods and services, unless such sales fall within exempt or excluded transactions.

With specific reference to the sale of receivables, in case it could be considered as a financing transaction, it would be exempt from VAT. Otherwise, the sale of receivables would be beyond the scope of Italian VAT.

Please note that with specific reference the fees for collection and credit management would instead be considered service provisions subject to VAT.

In the context of a securitisation, Italian tax authorities recently clarified that servicing activities can be included among the VAT-exempt transactions in the case where the servicer is the originator of the credit. Instead, in case the servicer is not only the originator but also carried out other transactions, the VAT treatment should be determined on a case-by-case analysis.

9.5 Purchaser Liability. If the seller is required to pay value-added tax, stamp duty or other taxes upon the sale of receivables (or on the sale of goods or services that give rise to the receivables) and the seller does not pay, then will the taxing authority be able to make claims for the unpaid tax against the purchaser or against the sold receivables or collections?

The seller and the purchaser, being the parties of the sale, are jointly liable towards the tax authorities for registration tax and stamp duty potentially due on the transaction. Any different agreement between the parties would not be effective against tax authorities.

As far as VAT is concerned, in principle the sale of receivables is not subject to VAT. With reference to VAT related to the sale of goods or services that give rise to the receivables, the liability lies only with the seller and no joint liability arises at the level of the purchaser.

9.6 Doing Business. Assuming that the purchaser conducts no other business in your jurisdiction, would the purchaser's purchase of the receivables, its appointment of the seller as its servicer and collection agent, or its enforcement of the receivables against the obligors, make it liable to tax in your jurisdiction?

Under Italian law, foreign entities are subject to taxation in Italy only in cases when (i) specific withholding taxes are provided by the law on certain services provisions, or (ii) the business activities carried out by the foreign entities give rise to a permanent establishment in Italy. With reference to the securitisation transactions, withholding tax applicable would be that outlined under question 9.1 above. In general terms, the existence of a permanent establishment in Italy could be verified when the purchaser either has a physical presence in Italy or it can be considered a "dependent agent" of a foreign entity in Italy. A case-by-case analysis based on the actual activities carried out in Italy should be performed in order to assess the presence of an Italian permanent establishment.

9.7 Taxable Income. If a purchaser located in your jurisdiction receives debt relief as the result of a limited recourse clause (see question 7.3 above), is that debt relief liable to tax in your jurisdiction?

Debt relief would be considered as a proceed of the SPV, and consequently taxed only at the end of the transaction, if such amount has not been used to pay the subscriber of the relevant notes. In this respect, please refer to question 9.2 above for details.

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Since September 2015, Luciano Morello has been a Partner of the Finance and Projects department. Luciano has extensive experience in finance and structured finance transactions, advising major Italian and European financial institutions. Luciano assists banks and funds in connection to asset securitisation transactions, covered bonds issuances and real estate/energy/structured finance transactions involving Italian and EU institutional counterparties. He also assists his clients in the setting up of pan-European issuance platforms for the offering (to both retail and institutional investors) and listing of a wide range of securities in the EU and in connection with the related legal and regulatory aspects. Luciano advises both investment banks and European companies in relation to the issuance of corporate bonds and their admission to trading on regulated and non-regulated markets. He advises European asset managers in establishing UCITS funds and Alternative Investment Funds in Luxembourg and other EU jurisdictions.

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Since May 2016, Ugo De Vivo has been a Legal Director in the Finance and Projects department. Ugo qualified as a solicitor in England and Wales and is admitted as "*avvocato*" in Italy. He joined DLA Piper as Senior Counsel in May 2013 (until April 2016). Ugo has gained consolidated experience in assisting both banks and corporate clients in connection with corporate finance, restructuring and refinancing transactions. Furthermore, he has extensive experience in structured finance and derivative transactions, having assisted banks and corporations in connection with securitisations of different kind of receivables, including receivables owned by public entities, and in derivative transactions. He has also assisted major banks in the restructuring of derivative transactions with Italian local entities. Ugo also regularly advises clients on bond issuances, placed through public offerings or private placements, and regulatory matters.

DLA Piper in Italy consists of over 200 professionals based in Milan and Rome. The team is formed by Italian and foreign lawyers who have been practising in Italy for many years. Our professionals offer all the advantages of a global team, combining strong knowledge and experience of the international business environment, with a multi-jurisdictional and full service approach. Our cross-disciplinary team approach delivers solutions quickly, efficiently, and with an integrated perspective of business needs and the legal environment in which clients operate. Thanks to the deep understanding our professionals have of our clients' businesses, the service that our firm offers is also characterised according to the sectors in which they operate. Our industry focus and experience enable us to provide a first-class service to our clients in their local and international investments and operations.

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Japan

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1 Receivables Contracts

1.1 Formalities. In order to create an enforceable debt obligation of the obligor to the seller: (a) is it necessary that the sales of goods or services are evidenced by a formal receivables contract; (b) are invoices alone sufficient; and (c) can a binding contract arise as a result of the behaviour of the parties?

It is not necessary for the sale of goods or services to be evidenced by a formal contract, so long as there is a legally binding, effective and valid contract, whether oral or implied. Whether invoices alone would be sufficient as evidence of the existence of an enforceable debt obligation would depend on the facts of each case and would be determined by the courts. The same can be said with respect to a result of the behaviour of the parties; i.e., a binding contract can be proven to exist (if there is sufficient evidence to establish) with a result of the behaviour of the parties, past relationships, or commercial customs.

1.2 Consumer Protections. Do your jurisdiction's laws: (a) limit rates of interest on consumer credit, loans or other kinds of receivables; (b) provide a statutory right to interest on late payments; (c) permit consumers to cancel receivables for a specified period of time; or (d) provide other noteworthy rights to consumers with respect to receivables owing by them?

(a) There are usury laws that restrict the rate of interest on loans (which can include various forms of credit extension), namely the Interest Rate Restriction Law (the "IRR Law") and the Law for Control of Acceptance of Contributions, Money Deposits and Interest, Etc. (the "Contributions Law"). The IRR Law provides that a contractual clause providing for interest on a loan at a rate exceeding a certain prescribed rate (described below) is null and void with respect to the portion exceeding such rate. Significantly, fees, default interest and other amounts received by a lender in connection with the loan will be treated as interest payments for the purpose of calculating the rate of interest.

Principal	Maximum Rate of Interest (*per annum*)
Less than 100,000 Yen	20%
From 100,000 Yen to 1,000,000 Yen	18%
1,000,000 Yen or more	15%

Under the current Contributions Law, no person in the money-lending business may charge interest at a rate exceeding 20% *per annum*. Charging or receiving interest at a rate in excess of such rate is subject to criminal penalties. Similarly with the IRR Law, in calculating the interest rate, any payment that the lender receives in connection with the lending will be deemed to be part of the interest payment. The Moneylenders' Law is a regulatory statute governing non-bank finance companies. The Moneylenders' Law requires registration of those who engage in the business of lending money, and regulates various lending practices, including marketing and collection practices, as well as the rate of interest charged on loans extended by moneylenders. Lastly, a prohibitively high rate of interest on (or interest on late repayments of) credit or other kinds of receivables may possibly be determined as void due to public policy reasons pursuant to the general Civil Code.

(b) There is a statutory right to interest on late payments; specifically, the general Civil Code provides that, unless otherwise agreed by the parties, interest will accrue following a late payment of a monetary obligation at a rate of 5% *per annum* (6% *per annum*, in cases of monetary obligations arising out of commercial conduct, as provided under the Commercial Code).

(c) For certain consumer contracts such as instalment sales agreements (i.e., sale and purchase agreements for which payments of purchase amounts are in instalments) in respect of certain types of products (including, without limitation, life insurance policies purchased outside of the insurance company's premises), the Instalment Sales Law (the "ISL") provides consumers with rights to cancel contracts during the cooling-off period mandated by the law.

(d) The ISL also provides consumers with protection against provisions providing for the business operator's right to terminate the contract or to declare that the consumer's obligation to pay all unpaid instalments has become immediately due and payable even if the consumer does not pay an instalment, unless: the business operator makes a demand against the consumer in writing to pay the instalment within a period prescribed in such written demand (which must be a reasonable period and may not be less than 20 days from such written demand); and the consumer fails to so pay the instalment within such period. In addition, the Consumer Contracts Law (the "CCL") provides, among other things, consumers with rights to rescind consumer contracts, for example, if the consumer had mistakenly manifested his/her intention to enter into the contract as a result of any misrepresentation by the business operator (who is the counterparty to the consumer contract) with respect to material matters such as quality, purpose and other characteristics of goods, rights, services, etc., of such consumer contract.

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1.3 Government Receivables. Where the receivables contract has been entered into with the government or a government agency, are there different requirements and laws that apply to the sale or collection of those receivables?

As a matter of practice, when the government or a governmental agency enters into a receivables contract, the contract would likely include a provision that prohibits transfers/assignments of rights thereunder by the counterparty without the prior consent of the government or the governmental agency, as the case may be. Also, such receivables contract may include a provision requiring that no third party be appointed as a collection servicer without the prior consent of the government. Therefore, although there is no specific statutory requirement, consent of the government or the governmental agency would likely be contractually required for the sale and/or collection of receivables.

2 Choice of Law – Receivables Contracts

2.1 No Law Specified. If the seller and the obligor do not specify a choice of law in their receivables contract, what are the main principles in your jurisdiction that will determine the governing law of the contract?

The Application of Laws (General) Act (the "ALGA") which came into effect on 1 January 2007, provides that if the parties to a contract do not specifically agree on a choice of law, the law of the jurisdiction having the closest relevance with the contract will govern the contract. However, it is generally assumed that a Japanese court will still follow a Supreme Court ruling, made prior to the introduction of the ALGA, to the effect that courts should first determine if the parties had implicitly agreed on the choice of law before applying the principle above. The ALGA also stipulates that if the contracting parties had not specifically agreed on a choice of law, and if the contract obligates a party to undertake a characteristic performance, then the law of such party's residence (or primary office) will be presumed to be the law of the jurisdiction having the closest relevance.

2.2 Base Case. If the seller and the obligor are both resident in your jurisdiction, and the transactions giving rise to the receivables and the payment of the receivables take place in your jurisdiction, and the seller and the obligor choose the law of your jurisdiction to govern the receivables contract, is there any reason why a court in your jurisdiction would not give effect to their choice of law?

In such a case, it would be very unlikely for a court not to uphold the parties' choice of law, at least judging from the published court decisions; provided, however, that if the subject of the receivables contract is a movable, the ownership of which is to be registered, and which is located outside Japan, then under the ALGA, the law of the jurisdiction in which the movable is located could govern the matters relating to the transfer of ownership.

2.3 Freedom to Choose Foreign Law of Non-Resident Seller or Obligor. If the seller is resident in your jurisdiction but the obligor is not, or if the obligor is resident in your jurisdiction but the seller is not, and the seller and the obligor choose the foreign law of the obligor/seller to govern their receivables contract, will a court in your jurisdiction give effect to the choice of foreign law? Are there any limitations to the recognition of foreign law (such as public policy or mandatory principles of law) that would typically apply in commercial relationships such as that between the seller and the obligor under the receivables contract?

Under the ALGA, parties to a contract are allowed to choose the governing law to be applied to their contractual obligations. Accordingly, the seller and the obligor may choose a foreign law to govern the receivables contract. However, if the application of the chosen law would result in a situation that would be against the public welfare or interests of Japan, then a court would not apply the chosen law as the governing law. In addition, different sets of rules under the ALGA are applied to consumer contracts to protect the interests of consumers. For example, if the obligor is a consumer (as defined in the ALGA) and the seller is a business operator (also as defined in the ALGA), then the consumer (i.e., the obligor) may demand that the law of the jurisdiction in which he/she resides be the governing law.

3 Choice of Law – Receivables Purchase Agreement

3.1 Base Case. Does your jurisdiction's law generally require the sale of receivables to be governed by the same law as the law governing the receivables themselves? If so, does that general rule apply irrespective of which law governs the receivables (i.e., your jurisdiction's laws or foreign laws)?

The ALGA does not specifically require that the sale agreement/contract under which receivables are sold be governed by the same law as the law governing the receivables themselves. However, under the ALGA, the "effects of a transfer" in terms of a transfer of a receivable (as opposed to contractual agreements stated in the sale agreement or surrounding the sale) against the obligor and other third parties are to be governed by the law governing the receivable itself, as noted in question 3.2 below.

3.2 Example 1: If (a) the seller and the obligor are located in your jurisdiction, (b) the receivable is governed by the law of your jurisdiction, (c) the seller sells the receivable to a purchaser located in a third country, (d) the seller and the purchaser choose the law of your jurisdiction to govern the receivables purchase agreement, and (e) the sale complies with the requirements of your jurisdiction, will a court in your jurisdiction recognise that sale as being effective against the seller, the obligor and other third parties (such as creditors or insolvency administrators of the seller and the obligor)?

Under the ALGA, the effects of a transfer of a receivable against the obligor and other third parties are governed by the law governing the receivable itself. Therefore, a Japanese court would determine the effects of the transfer resulting from the sale of the receivables (e.g., whether the receivables are effectively transferred) on the basis that

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Japanese law is the governing law. Thus, in this "Example 1" case, courts in Japan will recognise the sale as being effective against the seller, the obligor and other third parties.

3.3 Example 2: Assuming that the facts are the same as Example 1, but either the obligor or the purchaser or both are located outside your jurisdiction, will a court in your jurisdiction recognise that sale as being effective against the seller and other third parties (such as creditors or insolvency administrators of the seller), or must the foreign law requirements of the obligor's country or the purchaser's country (or both) be taken into account?

The ALGA does not take into account the requirements of the law of the obligor's country or the purchaser's country; and, as noted in question 3.2 above, the effects of a transfer of a receivable against the obligor and other third parties are governed by the law governing the receivable itself.

3.4 Example 3: If (a) the seller is located in your jurisdiction but the obligor is located in another country, (b) the receivable is governed by the law of the obligor's country, (c) the seller sells the receivable to a purchaser located in a third country, (d) the seller and the purchaser choose the law of the obligor's country to govern the receivables purchase agreement, and (e) the sale complies with the requirements of the obligor's country, will a court in your jurisdiction recognise that sale as being effective against the seller and other third parties (such as creditors or insolvency administrators of the seller) without the need to comply with your jurisdiction's own sale requirements?

As noted in question 3.2 above, the effects of a transfer of a receivable against the obligor and other third parties are governed by the law governing the receivable itself; therefore, under the ALGA, the sale of the receivable is governed by the law of the obligor's country. Thus, while there is no need to comply with Japan's own sale requirements, a court in Japan will not recognise the sale as being effective against the seller and other third parties, unless the requirements under the law of the obligor's country are complied with. However, this does not necessarily mean that the choice of law under the sale agreement will immediately be deemed void, since the effects of rights and obligations arising directly out of the sale agreement (e.g., whether an act of the seller would constitute a breach of contract giving rise to an indemnification obligation of the seller) would be determined in accordance with the law chosen as the governing law under the agreement, subject to the public welfare or interest doctrine described in question 2.3 above.

3.5 Example 4: If (a) the obligor is located in your jurisdiction but the seller is located in another country, (b) the receivable is governed by the law of the seller's country, (c) the seller and the purchaser choose the law of the seller's country to govern the receivables purchase agreement, and (d) the sale complies with the requirements of the seller's country, will a court in your jurisdiction recognise that sale as being effective against the obligor and other third parties (such as creditors or insolvency administrators of the obligor) without the need to comply with your jurisdiction's own sale requirements?

As noted in question 3.2 above, the effects of a transfer of a receivable against the obligor and other third parties are governed by the law governing the receivable itself. Thus, in this "Example 4" case, courts in Japan will recognise the sale as being effective against the seller, the obligor and other third parties without the need to comply with sale requirements under Japanese law.

3.6 Example 5: If (a) the seller is located in your jurisdiction (irrespective of the obligor's location), (b) the receivable is governed by the law of your jurisdiction, (c) the seller sells the receivable to a purchaser located in a third country, (d) the seller and the purchaser choose the law of the purchaser's country to govern the receivables purchase agreement, and (e) the sale complies with the requirements of the purchaser's country, will a court in your jurisdiction recognise that sale as being effective against the seller and other third parties (such as creditors or insolvency administrators of the seller, any obligor located in your jurisdiction and any third party creditor or insolvency administrator of any such obligor)?

As noted in question 3.2 above, the effects of a transfer of a receivable against the obligor and other third parties are governed by the law governing the receivable itself; therefore, the sale of the receivable needs to be, under the ALGA, governed by the law of Japan. Thus, unless the sale is governed by the law of Japan, a court in Japan will not recognise the sale as being effective against the seller and other third parties. However, this does not necessarily mean that the choice of law under the sale agreement will immediately be deemed void, since the effects of rights and obligations arising directly out of the sale agreement (e.g., whether an act of the seller would constitute a breach of contract giving rise to an indemnification obligation of the seller) would be determined in accordance with the law chosen as the governing law under the agreement, subject to the public welfare or interest doctrine described in question 2.3 above.

4 Asset Sales

4.1 Sale Methods Generally. In your jurisdiction what are the customary methods for a seller to sell receivables to a purchaser? What is the customary terminology – is it called a sale, transfer, assignment or something else?

Under the current system, the customary method for a seller to sell receivables is to enter into a sales agreement with the purchaser in which the subject receivables need to be specified, and the sale be perfected through one of the methods described in question 4.2 below. In some cases, the continuous sales method is adopted. The terminology in the Japanese language is "*baibai*" (a simple translation would be "sale") or "*joto*" (a simple translation would be "assignment").

4.2 Perfection Generally. What formalities are required generally for perfecting a sale of receivables? Are there any additional or other formalities required for the sale of receivables to be perfected against any subsequent good faith purchasers for value of the same receivables from the seller?

The perfection of a sale of receivables is generally made by one of the following methods:

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(a) the seller delivering notice to the obligors, or the seller or purchaser obtaining consent from the obligors, where notice or consent must bear an officially certified date (*kakutei-hizuke*) by means prescribed under law in order to perfect against third parties; or

(b) where the seller is a corporation, the seller registering the sale of receivables in a claim assignment registration file in accordance with the Law Prescribing Exceptions, Etc., to the Civil Code Requirements for Perfection of Transfers of Movables and Receivables (the "Perfection Exception Law").

Provided one of the methods noted above is duly taken, there are no additional formalities required for perfection against subsequent purchasers.

4.3 Perfection for Promissory Notes, etc. What additional or different requirements for sale and perfection apply to sales of promissory notes, mortgage loans, consumer loans or marketable debt securities?

(i) Promissory notes

Under the Promissory Notes Law, the general method of sale and perfection against the obligor and third parties is by the seller endorsing the promissory notes and delivering the same to the purchaser.

(ii) Consumer loans

While there are no additional or different requirements for perfection of sales of consumer loans, please see question 8.3 for regulations regarding sales of loans extended by moneylenders regulated under the Moneylenders' Law (nevertheless, the regulations apply not only to consumer loans but to all loans (including mortgage loans) extended by a moneylender).

(iii) Mortgage loans

For the perfection of a sale of a loan secured by a hypothec (*teito-ken*) or umbrella hypothec (*ne-teito-ken*), the following will be necessary as additional requirements to those described in questions 4.1 and 4.2:

(a) In case of a loan secured by a hypothec

In order for the hypothec to be concurrently transferred to the purchaser with the sale of a loan (secured by the hypothec), no additional action is necessary other than the requirement for the valid and effective sale of the loan itself (*zuihansei*). For perfection of the transfer of the hypothec as a result of the sale of the loan, the transfer of the hypothec needs to be registered through a supplemental registration (*fuki-toki*) in the real estate registry (however, such registration is generally believed to be unnecessary to perfect against a third party who is a transferee of the hypothec together with the loan secured thereby).

(b) In case of a loan secured by an umbrella hypothec

In order for a loan to be transferred together with an umbrella hypothec (or the hypothec resulting from crystallisation of the umbrella hypothec), and for such transfer to be perfected, either of the following methods needs to be used:

(x) For an effective transfer of an umbrella hypothec without crystallisation, the obligor or any other party who created the umbrella hypothec must consent to the transfer (and consent to amend the scope of obligations secured by the umbrella hypothec might also be necessary depending on the terms thereof). For perfection of the transfer of an umbrella hypothec without crystallisation, the transfer needs to be registered through a supplemental registration (*fuki-toki*) in the real estate registry.

(y) For an effective transfer of a loan with a hypothec resulting from the crystallisation of an umbrella hypothec that originally secured the loan, the obligations secured by such umbrella hypothec need to be crystallised (*kakutei*) in accordance with the general Civil Code prior to the sale becoming effective (if not crystallised, and if the consent described in (x) above is not obtained, the relevant loan will be transferred as an unsecured loan). For perfection of the transfer of the hypothec (occurring together with the transfer of the loan secured thereby) resulting from the crystallisation, the requirement described in (a), above, applies.

(iv) Marketable debt securities

While there is no legal concept equivalent to "marketable debt securities" or any legal distinction between marketable securities and non-marketable securities under Japanese law, we will focus on the sale and perfection of Japanese government bonds ("JGBs") and bonds issued by Japanese corporations. The requirements for sale and perfection of these securities depend on their form.

(a) In case of JGBs

(A) If in bearer form with physical certificates (*mukimeikokusai shouken*):

For effective sale and perfection, the seller and purchaser must agree to sell and purchase the JGBs and the seller should deliver the physical certificates to the purchaser. In general, there is no prohibition on the transfer of bearer JGBs.

(B) If registered JGBs (*touroku kokusai*):

For perfection against third parties as well as the government, the transfer needs to be registered in the JGB registry at the Bank of Japan in accordance with the Law Regarding Japanese Government Bonds and rules promulgated thereunder.

(C) If in book-entry form under the Transfer Law (*furikae kokusai*):

For sale and perfection against the government and third parties, the amount of the JGBs assigned to the purchaser as a result of the sale needs to be entered into the purchaser's account book in accordance with the Law Concerning Book-Entry Transfer of Corporate Bonds, Etc. (the "Transfer Law").

(b) Corporate Bonds

(A-1) If in bearer form with physical certificates (*mukimei shasaiken*):

Under the Corporations Act, no transfer will be effected without the physical delivery to the purchaser of the certificate in case of certificated bonds.

(A-2) If in non-bearer form with physical certificates (*kimei shasaiken*):

The same as (A-1) above; under the Corporations Act, no transfer will be effected without the physical delivery to the purchaser of the certificate in case of certificated bonds. In addition, in cases of non-bearer bonds issued pursuant to the Corporations Act, in order to perfect the transfer against third parties and against the issuer company, the purchaser's name and address need to be recorded in the bond registry (*shasai genbo*) in accordance with the Corporations Act.

(B) Book-entry bonds under the Transfer Law (*furikae shasai*):

For sale and perfection against the issuer company and third parties, the amount of the book-entry bonds assigned to the purchaser as a result of the sale needs to be entered into the purchaser's account book in accordance with the Transfer Law.

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4.4 Obligor Notification or Consent. Must the seller or the purchaser notify obligors of the sale of receivables in order for the sale to be effective against the obligors and/or creditors of the seller? Must the seller or the purchaser obtain the obligors' consent to the sale of receivables in order for the sale to be an effective sale against the obligors? Whether or not notice is required to perfect a sale, are there any benefits to giving notice – such as cutting off obligor set-off rights and other obligor defences?

Where the receivables contract prohibits a sale of the receivables thereunder without the consent of the obligor, the consent of the obligor will be required. Therefore, in such a case, naturally, a notification to the obligors would be required as a matter of fact. Otherwise, whether or not the sale is effective against the obligors is a question of perfection against the obligors. That is, if the sale is perfected against the obligors, then the sale is an effective sale against the obligors. Once the sale of receivables is perfected against the obligors, for example, the purchaser will be allowed to enforce the debts directly against the obligors and the obligors will be required to pay the purchaser rather than the seller. In order to perfect the sale of a receivable against the obligor thereof, one of the following methods needs to be used:

(a) the seller must deliver a notice to the obligor or obtain consent from the obligor (in contrast to the perfection against third parties, there is no need for the notice/consent to bear an officially certified date (*kakutei-hizuke*)); or

(b) where the assignment of the receivables is perfected against third parties by registration under the Perfection Exception Law, the seller or purchaser must either use the method noted above in (a) or notify the obligor of the sale of the receivables by delivering a registered certificate (*touki jikou shoumeisho*), or obtain consent from the obligor thereby.

Where the receivables contract prohibits a sale of the receivables thereunder without the consent of the obligor, the consent of the obligor will be required (the question is whether or not the contract prohibits assignments rather than whether the contract permits assignments). Otherwise, whether or not the sale is effective against the obligors is a question of perfection against the obligors.

There is no legal limitation regarding the purchaser notifying the obligor of the sale of receivables after the insolvency of the seller or the obligor; in fact, the customary contractual arrangement in securitisation transactions is that the purchaser will be allowed to notify the obligor of the sale once the seller or the obligor becomes insolvent.

Unless a sale of a receivable is perfected, the obligor will retain set-off rights and other obligor defences, therefore, perfection would be required to prevent those defences. For the avoidance of doubt, set-off rights and other defences that preceded the perfection would remain effective (with the exception of a waiver by the obligor).

4.5 Notice Mechanics. If notice is to be delivered to obligors, whether at the time of sale or later, are there any requirements regarding the form the notice must take or how it must be delivered? Is there any time limit beyond which notice is ineffective – for example, can a notice of sale be delivered after the sale, and can notice be delivered after insolvency proceedings have commenced against the obligor or the seller? Does the notice apply only to specific receivables or can it apply to any and all (including future) receivables? Are there any other limitations or considerations?

With respect to the form of the notice, please see questions 4.2 and 4.4.

As for the time limit for delivering a notice, while notice could be delivered after an insolvency proceeding has commenced against the obligor or the seller, such notice could be voided – if the notice had been delivered with the knowledge of either the fact that the obligor ceased payments or the fact that the petition for the commencement of the insolvency proceedings had been filed – by avoidance rights of insolvency trustees, unless the delivery had been made within 15 calendar days from the sale (as opposed to the commencement date of the insolvency proceedings). While a notice can be applied to future receivables, future receivables do need to be specified in a certain manner for the notice to be legal and valid (see question 4.10).

4.6 Restrictions on Assignment – General Interpretation. Will a restriction in a receivables contract to the effect that "None of the [seller's] rights or obligations under this Agreement may be transferred or assigned without the consent of the [obligor]" be interpreted as prohibiting a transfer of receivables by the seller to the purchaser? Is the result the same if the restriction says "This Agreement may not be transferred or assigned by the [seller] without the consent of the [obligor]" (i.e., the restriction does not refer to rights or obligations)? Is the result the same if the restriction says "The obligations of the [seller] under this Agreement may not be transferred or assigned by the [seller] without the consent of the [obligor]" (i.e., the restriction does not refer to rights)?

Each of the first two restrictions will be binding restrictions prohibiting a transfer of receivables by the seller to the purchaser, absent the consent of the obligor, while the third restriction will not be treated as a restriction that prohibits the seller from transferring its receivables to the purchaser.

4.7 Restrictions on Assignment; Liability to Obligor. If any of the restrictions in question 4.6 are binding, or if the receivables contract explicitly prohibits an assignment of receivables or "seller's rights" under the receivables contract, are such restrictions generally enforceable in your jurisdiction? Are there exceptions to this rule (e.g., for contracts between commercial entities)? If your jurisdiction recognises restrictions on sale or assignment of receivables and the seller nevertheless sells receivables to the purchaser, will either the seller or the purchaser be liable to the obligor for breach of contract or tort, or on any other basis?

There is no general restriction on receivables contracts prohibiting the sale or assignment of receivables, even between commercial entities. As prohibitions on the sale or assignment provided under receivables contracts are recognised, the seller will be liable to the obligor if any damage is incurred by the obligor when the seller breaches the prohibition. However, the sale of a receivable (the receivables contract in respect of which expressly prohibits assignment thereof) will not constitute a valid and effective transfer unless the purchaser, in the absence of both the knowledge of such prohibition and gross negligence in having no knowledge of the prohibition, purchased the receivables from the seller. Therefore, in cases where no transfer will be given effect, the obligor will usually incur no damages as a result of the sale.

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4.8 Identification. Must the sale document specifically identify each of the receivables to be sold? If so, what specific information is required (e.g., obligor name, invoice number, invoice date, payment date, etc.)? Do the receivables being sold have to share objective characteristics? Alternatively, if the seller sells *all* of its receivables to the purchaser, is this sufficient identification of receivables? Finally, if the seller sells *all* of its receivables *other than* receivables owing by one or more specifically identified obligors, is this sufficient identification of receivables?

The sale agreement must specifically identify the receivables in order for the receivables to be validly sold. There is no minimum or specific legal requirement in identifying the receivables and it will vary depending upon the types of receivables and receivables contracts; receivables can be identified by information such as obligor names, amounts of the receivables, invoice numbers, the contract dates and/or the terms of the receivables. For so long as the receivables sold under a sales agreement are sufficiently identified, the receivables sold under the agreement do not need to share objective characteristics. Depending on the nature of the seller, it could be possible to construe that identification of receivables is sufficient if the seller sells all of its receivables; however, this will not be the case if the seller's receivables include receivables that are restricted from sale or assignment; also, if the sale includes the sale of future receivables, the sale may be deemed void. The same will apply with respect to cases where the seller sells all of its receivables other than receivables owing by one or more specifically identified obligors. Please see question 4.9 for the assignability of future receivables.

4.9 Recharacterisation Risk. If the parties describe their transaction in the relevant documents as an outright sale and explicitly state their intention that it be treated as an outright sale, will this description and statement of intent automatically be respected or is there a risk that the transaction could be characterised by a court as a loan with (or without) security? If recharacterisation risk exists, what characteristics of the transaction might prevent the transfer from being treated as an outright sale? Among other things, to what extent may the seller retain any of the following without jeopardising treatment as an outright sale: (a) credit risk; (b) interest rate risk; (c) control of collections of receivables; (d) a right of repurchase/redemption; (e) a right to the residual profits within the purchaser; or (f) any other term?

Any transaction could be recharacterised as, for example, a loan with or without security by a court based on its economic characteristics regardless of the parties' designation of a transaction as a sale or any statement of such intent; on the other hand, economic characteristics of a sale will not prevent the sale from being perfected, unless the characteristics hinder the nature of the transaction and result in recharacterisation thereof. In other words, under Japanese law, provided a transaction is not recharacterised as a loan or any other transaction, economic characteristics will not prevent a sale from being perfected. On the other hand, any characteristics (which may include the seller retaining too much credit risk, interest rate risk, control over the receivables, a right of repurchase/redemption or a right to the residual profits within the purchaser) that are inconsistent with the characteristics of sales transactions, may result in recharacterisation; in this connection, retaining a right of repurchase/redemption could be viewed as generally making the transaction susceptible to recharacterisation.

4.10 Continuous Sales of Receivables. Can the seller agree in an enforceable manner to continuous sales of receivables (i.e., sales of receivables as and when they arise)? Would such an agreement survive and continue to transfer receivables to the purchaser following the seller's insolvency?

It is possible for the seller to agree to continuous sales of receivables in an enforceable manner, however, such continuous sales would be subject to the insolvency officials' right to rescind.

4.11 Future Receivables. Can the seller commit in an enforceable manner to sell receivables to the purchaser that come into existence after the date of the receivables purchase agreement (e.g., "future flow" securitisation)? If so, how must the sale of future receivables be structured to be valid and enforceable? Is there a distinction between future receivables that arise prior to *versus* after the seller's insolvency?

Following a Supreme Court case ruling in 1999, the general belief is that it is possible for the seller to commit to sell future receivables, so long as the receivables are sufficiently specified and identified (by, for example, the obligors thereof, the transactions from which the receivables are generated, the amounts of the receivables and/or the dates on which receivables are, respectively, generated); provided that the sale of the receivables, in whole or in part, may be deemed or determined to be void due to a contradiction with the public welfare/interest or for any other reasons and there also is a possibility of the sale of future receivables being subject to rights of insolvency officials to rescind, especially with regard to receivables arising after the seller's insolvency.

4.12 Related Security. Must any additional formalities be fulfilled in order for the related security to be transferred concurrently with the sale of receivables? If not all related security can be enforceably transferred, what methods are customarily adopted to provide the purchaser the benefits of such related security?

Provided the transfer of the receivables is enforceable and perfected against third parties, it is generally believed that a related security (other than an umbrella security interest such as an umbrella hypothec) securing the transferred receivables will also automatically be recognised as being concurrently transferred in a perfected manner (see question 4.3 above). Provided, however, with respect to certain security interests that can be registered such as a hypothec, the concurrent transfer of the hypothec will not be perfected against a third party that acquires the related security (without acquiring the obligation secured thereby) unless the concurrent transfer is separately perfected; for example, in the case of a hypothec, perfected by registration in the relevant real estate registry through a supplemental registration.

As for umbrella securities, crystallisation thereof will be required in order to provide the purchaser with the benefits of the security (although following a crystallisation, an umbrella security will no longer be an umbrella security but a regular security) or obtain the consent of the obligor or any other party who granted the security in order to transfer the umbrella security as an umbrella security to the purchaser.

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4.13 Set-Off; Liability to Obligor. Assuming that a receivables contract does not contain a provision whereby the obligor waives its right to set-off against amounts it owes to the seller, do the obligor's set-off rights terminate upon its receipt of notice of a sale? At any other time? If a receivables contract does not waive set-off but the obligor's set-off rights are terminated due to notice or some other action, will either the seller or the purchaser be liable to the obligor for damages caused by such termination?

The obligor's set-off rights will terminate once it receives notice of a sale, but only if the notice is made by the seller (not the purchaser or any other party), and the obligor is generally believed to continue to have the ability to set off any prior claims (i.e., claims that the seller owed to the obligor prior to the notice). The obligor's set-off rights will also terminate if, and when, the obligor consents to the sale, and unless the consent is with a reservation to retain its right to set-off, the obligor will no longer have any ability to set off (including its prior claims).

4.14 Profit Extraction. What methods are typically used in your jurisdiction to extract residual profits from the purchaser?

Generally speaking, for the purpose of mitigating the recharacterisation risk, it would be best for the seller to avoid retaining a right to residual profits from the purchaser to the extent possible (see question 4.9 above). However, one of the options for the seller to enjoy residual profits from the purchaser is to create a trust. In usual cases, a trust is created and the trustee thereof acquires the receivables, and most parts of the trust beneficial interests thereof are sold by the seller to third parties. In such instances, if the seller retains a certain portion of the trust beneficial interests (typically, the subordinate trust beneficial interest), the seller may enjoy residual profits from the purchaser (i.e., the trustee) to a certain extent. In any case, it should be noted that the ratio of the subordinate trust beneficial interest retained by the seller must be appropriate in comparison to the actual value of the receivables to be assigned to the trustee.

Also, a "*tokumei kumiai*" (a simple translation would be "anonymous partnership" or "silent partnership") would be an alternative. A *tokumei kumiai* is a contractual relationship between the operator and the investor, where the operator conducts certain business specified in the contract in its own name and the investor makes a contribution to the operator for the purpose of the said business, and the profit and loss generated from the said business will be allocated to the investor. In this regard, if the seller invests in the purchaser in the form of a *tokumei kumiai*, then the seller may extract residual profits from the purchaser. In such instances, it would be also important to determine the amount of *tokumei kumiain* contribution in a manner that would not increase the recharacterisation risk above.

Further, use of a *tokutei mokuteki gaisha* (TMK) could be an option. For more details regarding TMKs, please see question 7.1 below.

5 Security Issues

5.1 Back-up Security. Is it customary in your jurisdiction to take a "back-up" security interest over the seller's ownership interest in the receivables and the related security, in the event that an outright sale is deemed by a court (for whatever reason) not to have occurred and have been perfected (see question 4.9 above)?

Under Japanese law, the methods to execute and perfect a sale of receivables and methods to create, and perfect the creation of, a security interest over receivables are basically the same. Therefore, it is not customary in Japan to take a "back-up" security interest. While there have been arguments about taking a "back-up" security interest in order to protect the interest of the purchaser in the event that the sale is recharacterised as a financing rather than a sale (note that the purpose is different from the term "back-up" for a failure to execute or perfect a sale), since the creation of a "back-up" security interest would seem to contradict the parties' intention to effect a true sale and also because, even if recharacterised, transactions would likely be recharacterised as secured lending with a perfected security, it is generally assumed that the taking of a "back-up" security interest would not add much protection but, at the same time, run the risk of working against the true sale nature of the transactions and, therefore, parties customarily do not create any "back-up" security interest.

5.2 Seller Security. If it is customary to take back-up security, what are the formalities for the seller granting a security interest in receivables and related security under the laws of your jurisdiction, and for such security interest to be perfected?

Seller security is not applicable in Japan.

5.3 Purchaser Security. If the purchaser grants security over all of its assets (including purchased receivables) in favour of the providers of its funding, what formalities must the purchaser comply with in your jurisdiction to grant and perfect a security interest in purchased receivables governed by the laws of your jurisdiction and the related security?

Under Japanese law, there is no simple way to grant a security over "all assets" of the purchaser. The purchaser must grant specific security over each specific asset class/type separately. Therefore, if receivables constitute a part of the purchaser's "all assets", then to effect and/or perfect a security interest over such receivables, the following formalities must be complied with:

For granting a security interest in receivables, a "pledge" (*shichiken*) or a "security assignment" (*jyoto-tampo*) is normally used in Japan.

(i) Pledge

In order to effectively pledge receivables to the creditor, the following need to be satisfied:

- while there is no formality requirement for a pledge agreement, in the agreement, the same as sales of receivables, receivables to be pledged must be specified, and assignments thereof must not be prohibited under the relevant receivables contracts; and

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- the pledgor must deliver to the pledgee the instruments evidencing such receivables, if such instruments need to be delivered in order to effect an assignment of such receivables.

In order to perfect the creation of the pledge against third parties and obligors, one of the following methods needs to be undertaken:

(a) the pledgor must deliver notice to the obligors, or the pledgor or pledgee must obtain consent from the obligors, where notice or consent must bear an officially certified date (*kakutei-hizuke*) by means prescribed under law in order to perfect against third parties (if no officially certified date is affixed, then the creation of the pledge will still be perfected against the obligors but not against third parties); or

(b) if the pledgee is a corporation, the pledgee must register the creation of the pledge in a claim assignment registration file in accordance with the Perfection Exception Law.

(ii) Security assignment

In order to effectively assign receivables for security purposes, the following need to be satisfied:

- while there is no formality requirement for a security assignment agreement, in the agreement, the same as with sales of receivables, receivables to be assigned for security purposes must be specified, and assignments thereof must not be prohibited under the relevant receivables contracts; and
- the same as with pledges of receivables, the assignor must deliver to the assignee the instruments evidencing such receivables, if such instruments need to be delivered in order to effect an assignment of such receivables.

In order to perfect the creation of the security assignment against third parties and obligors, one of the following measures needs to be undertaken:

(a) the assignor must deliver notice to the obligors, or the assignor or assignee must obtain consent from the obligors, which notice or consent must bear an officially certified date (*kakutei-hizuke*) by means prescribed under law in order to perfect against third parties; or

(b) if the assignor is a corporation, the assignor must register the assignment of receivables in a claim assignment registration file in accordance with the Perfection Exception Law.

5.4 Recognition. If the purchaser grants a security interest in receivables governed by the laws of your jurisdiction, and that security interest is valid and perfected under the laws of the purchaser's jurisdiction, will the security be treated as valid and perfected in your jurisdiction or must additional steps be taken in your jurisdiction?

The ALGA, which is the law a Japanese court would apply in determining the applicable governing law, does not explicitly provide for rules relating to the choice of governing law in respect of security interests over receivables. However, according to the general interpretation of the statute that provided for the rules relating to the choice of governing law and which was replaced by the ALGA (which also does not explicitly provide for rules relating to the law governing security interests over receivables), the law governing a creation/granting of a pledge or a security assignment in a receivable is the law governing such receivable. The general notion is that this interpretation will remain the controlling interpretation even after the introduction of the ALGA. Therefore, if the purchaser grants a security interest in the receivables under the laws of the purchaser's country or a third country, even if the security interest is valid under the laws of that country, Japanese courts will not treat the security interest as valid unless the subject receivables are governed by the same country's law.

As for the governing law regarding perfection of a security interest in a receivable, neither the ALGA nor the statute replaced thereby provides or provided any express rule. While the general interpretation under the replaced statute was that the perfection would be governed by the law of the obligor's domicile, it is not expected that the same interpretation will be controlling after the introduction of the ALGA. This is because, while the interpretation was reasoned upon the fact that the replaced statute expressly provided that the law of the obligor's domicile governed the perfection of an assignment of a receivable, the ALGA amended the rule and provides that the governing law of the receivable itself governs the perfection of an assignment of the receivable. Thus, it is believed that the governing law of the receivable will also govern the perfection of a security interest in the receivable. Therefore, if the purchaser perfects a security interest in the receivables (which are governed by the laws of Japan) under the laws of the purchaser's country or a third country, even if the security interest is determined to be perfected under the laws of that country, Japanese courts will not treat the security interest as perfected unless the subject receivables are perfected under the laws of Japan as well.

5.5 Additional Formalities. What additional or different requirements apply to security interests in or connected to insurance policies, promissory notes, mortgage loans, consumer loans or marketable debt securities?

(i) Insurance policies

There is no additional or different requirement specifically applicable only to insurance policies under Japanese law, provided, however, that for those insurance policies that are payable to order (i.e., those that fall under the definition of *sashizu-saiken*), endorsement will be required in order to effect and perfect the transfer.

(ii) Promissory notes

Under the Promissory Notes Law, the general method of granting security interests on promissory notes and perfection against the obligor and third parties is by the grantor endorsing the promissory notes and delivering the same to the grantee.

(iii) Consumer loans

Unlike the sale of (consumer) loans, regulations regarding sales of loans extended by moneylenders regulated under the Moneylenders' Law (see question 8.3) do not apply to the grantee of the security interests on (consumer) loans, even if the loans are extended by a moneylender, unless, and until, the security interests are foreclosed.

(iv) Mortgaged loans

When a security interest is validly and effectively granted over, or in, a loan that itself is secured by a hypothec (*teito-ken*) (but not in the case of an umbrella hypothec (*ne-teito-ken*)), the grantee will automatically benefit from the hypothec as the security interest will grasp the loan as a secured loan without any additional or different requirement (*zuihansei*). However, this does not mean that the grantee would be entitled to directly enforce/foreclose on the hypothec or umbrella hypothec. The security interest granted over, or in, the loan secured by the hypothec or umbrella hypothec must first be enforced/foreclosed. Thereafter, if the grantee acquires the loan secured by the hypothec or umbrella hypothec himself/herself as a result of such enforcement/foreclosure, then the grantee will be able to enforce/foreclose on the hypothec or umbrella hypothec (but only if the loan is due and payable). In order to perfect the interest that the grantee acquires as a result of the granting of the security

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interest over/in the loan secured by the hypothec against third parties who gain interest in the hypothec after the granting of the security interest, a registration (if the security interest is a pledge, in the form of an amendment registration and if the security interest is a security assignment, in the form of a supplemental registration) needs to be made in the relevant real estate registry (however, it is generally believed that the grantee of the security interest in a mortgaged loan will prevail over a third party who acquires the mortgage loan for so long as the granting of the security interest to the grantee is first perfected (even if the registration is not made or was made after the third party's acquisition of the mortgage loan)).

In cases where the loan over which the security interest is created is secured by an umbrella hypothec, in contrast to the above, the grantee will not benefit from the umbrella hypothec as an umbrella hypothec will not be transferred unless, and until, it is crystallised into a regular hypothec.

(v) Marketable debt securities

Similarly to question 4.3 above, we will focus on the granting of a pledge or a security assignment over or in JGBs or corporate bonds and perfection thereof. The requirements for the granting/creation of security interests in respect of these securities and perfection thereof depend on the form of the JGBs and the bonds.

(a) In case of JGBs

In order to pledge JGBs and to perfect such pledge, the following is required:

(A) If in bearer form with physical certificates (*mukimei kokusai shouken*):

- the pledgor and the pledgee must agree on the creation of the pledge of JGBs and the pledgor must deliver the physical certificates to the pledgee; and
- for continued perfection against third parties, the pledgee must continuously keep custody of the physical certificates.

(B) If registered JGBs (*toroku kokusai*):

An effective pledge of registered JGBs will arise if the seller and the purchaser agree to the creation of the pledge, provided that the JGBs do not prohibit the transfer thereof. For perfection against third parties, as well as the government, the transfer needs to be registered in the JGB registry at the Bank of Japan in accordance with the Law Regarding Japanese Government Bonds and rules promulgated thereunder.

(C) If in book-entry form under the Transfer Law (*furikae kokusai*):

For the creation of a pledge over such JGBs and perfection against the government and third parties, the amount of the JGBs pledged to the pledgee needs to be entered into the pledgee's account book in accordance with the Transfer Law.

The requirements for the effective granting of a security assignment of JGBs and perfection thereof are basically the same as the requirements for the effective sale and perfection thereof as outlined in question 4.3 above.

(b) Corporate bonds

In order to pledge corporate bonds and to perfect such pledge, the following is required:

(A-1) If in bearer form with physical certificates (*mukimei shasaiken*):

Under the Corporations Act and the general Civil Code, no creation of a pledge will be effected without the physical delivery to the pledgee of the certificate in case of certificated bonds issued pursuant to the Corporations Act. For continued perfection against third parties, the pledgee must continuously keep custody of the physical certificates.

(A-2) If in non-bearer form with physical certificates (*kimei shasaiken*):

The same as (A-1) above, under the Corporations Act and the general Civil Code, no pledge will be effected without the physical delivery to the pledgee of the certificates in case of certificated bonds issued pursuant to the Corporations Act. In addition, in cases of non-bearer bonds issued pursuant to the Corporations Act, in order to perfect the transfer against third parties and against the issuer company, the pledgee's name and address must be recorded in the bond registry (*shasai genbo*) in accordance with the Corporations Act.

(B) If book-entry bonds under the Transfer Law (*furikae shasai*):

In order to pledge book-entry bonds and to perfect against the issuer company and third parties, the amount of the book-entry bonds pledged to the pledgee must be entered into the pledgee's account book in accordance with the Transfer Law.

The requirements for the effective granting of a security assignment of corporate bonds and perfection thereof are basically the same as the requirements for the effective sale and perfection thereof as outlined in question 4.3 above.

5.6 Trusts. Does your jurisdiction recognise trusts? If not, is there a mechanism whereby collections received by the seller in respect of sold receivables can be held or be deemed to be held separate and apart from the seller's own assets (so that they are not part of the seller's insolvency estate) until turned over to the purchaser?

Yes, trusts are recognised under Japanese law. In fact, a statute entitled the Trust Law governs and sets the statutory rules (some of which are mandatory rules rather than default rules).

5.7 Bank Accounts. Does your jurisdiction recognise escrow accounts? Can security be taken over a bank account located in your jurisdiction? If so, what is the typical method? Would courts in your jurisdiction recognise a foreign law grant of security (for example, an English law debenture) taken over a bank account located in your jurisdiction?

Escrow arrangements may take several forms under Japanese law as there is no legal concept of "escrow" *per se*. A trust would be one of the major legal forms that could be utilised for an escrow arrangement.

While a security interest can be created over rights of the holder of a bank account owing money to a bank in Japan, it is not a security over the bank account *per se*; rather, it is a security over a monetary claim – a claim to receive refund of the deposit – against the bank. Also, there is an argument that a security interest created over the rights of the holder of a bank account would become invalid or unperfected each time the balance of the account changes.

5.8 Enforcement over Bank Accounts. If security over a bank account is possible and the secured party enforces that security, does the secured party control all cash flowing into the bank account from enforcement forward until the secured party is repaid in full, or are there limitations? If there are limitations, what are they?

No. Since, as described in question 5.7 above, a security interest over a bank account is a security over a monetary claim against

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the bank rather than a security over the account *per se*, the secured party will not control all cash flowing into the bank account from the enforcement forward. Technically, it may be possible – although there is, as also described in question 5.7 above, an argument that a security interest created over the rights of the holder of a bank account would become invalid or unperfected each time the balance of the account changes – to create a security interest purporting to cover any and all cash flowing into a bank account, formal foreclosure of such security would need to be made with a specific amount of deposit.

5.9 Use of Cash Bank Accounts. If security over a bank account is possible, can the owner of the account have access to the funds in the account prior to enforcement without affecting the security?

That may be possible, but there is an argument to the contrary (see questions 5.7 and 5.8 above for more details).

6 Insolvency Laws

6.1 Stay of Action. If, after a sale of receivables that is otherwise perfected, the seller becomes subject to an insolvency proceeding, will your jurisdiction's insolvency laws automatically prohibit the purchaser from collecting, transferring or otherwise exercising ownership rights over the purchased receivables (a "stay of action")? If so, what generally is the length of that stay of action? Does the insolvency official have the ability to stay collection and enforcement actions until he determines that the sale is perfected? Would the answer be different if the purchaser is deemed to only be a secured party rather than the owner of the receivables?

Under Japanese law, there is no system or mechanism equivalent to an automatic stay. Neither the filing of the petition for insolvency proceedings, nor the commencement of such proceedings, automatically prohibit creditors from exercising or enforcing their rights; however, once the commencement of insolvency proceedings is petitioned, Japanese insolvency courts will customarily issue stay orders as to payments on, or performance of, obligations of the insolvent up to the commencement of insolvency proceedings. Also, upon and after the commencement of the insolvency proceedings, the creditors to the insolvent will be subjected to such proceedings and will be prohibited from exercising or enforcing their rights outside such proceedings; however, secured creditors will basically be allowed to enforce/foreclose on their security interest if the insolvency proceeding is either (1) a bankruptcy proceeding under the Bankruptcy Code, or (2) a rehabilitation proceeding under the Civil Rehabilitation Law. In each case this will be subject to certain rights of the insolvency official to extinguish the security interest and/or to stay the foreclosure process of the security interest.

More importantly, if the sale of the receivables prior to the commencement of the insolvency proceeding is perfected, and for so long as the sale is not recharacterised as a lending transaction rather than a true sale, the purchaser will not be a creditor to the insolvent in connection with the purchased receivables and, therefore, will have the rights and ability to collect, transfer or otherwise exercise ownership rights over the purchased receivables (note, however, that whether or not the purchaser will have the ability to terminate a servicing agreement (entered into with the seller, if any, in order to let the originator/seller service the receivables) upon the seller becoming subject to the insolvency proceeding is a separate question; if the servicing agreement cannot be terminated, the insolvent seller may remain entitled to collect the receivables, although the purchaser otherwise has the right and ability to collect the receivables).

Conversely, insolvency officials tend to challenge the true sale nature of securitisation transactions in an effort to preclude the purchaser from exercising ownership rights over the receivables and/or challenge that the purchaser may not terminate the servicing agreement, if any, so that the insolvency officials will remain in control of the collection procedures.

6.2 Insolvency Official's Powers. If there is no stay of action, under what circumstances, if any, does the insolvency official have the power to prohibit the purchaser's exercise of its ownership rights over the receivables (by means of injunction, stay order or other action)?

If the sale of receivables is perfected and is a true sale, then the purchaser will not be prohibited from exercising its ownership rights over, or other rights in respect of, the purchased receivables (save for the uncertainty as to the termination of the servicing agreement).

To the contrary, if the sale is not perfected prior to the insolvency or if the sale is not a true sale, then the purchaser's exercise of rights may be prohibited or restricted. Firstly, if the sale was a true sale but not perfected, then the insolvency official would effectively rescind the sale as a result of which the receivables would clawback to the insolvent's estate. Furthermore, if the sale was not a true sale, then, irrespective of whether or not the transaction was perfected, the purchaser would be a creditor, as a result of which the purchaser's ability to exercise its rights may be restricted by the insolvency proceedings (provided, that, as described in question 6.1, if the purchaser is deemed a secured creditor with a perfected security interest, and if the insolvency proceeding was either a bankruptcy proceeding or a rehabilitation proceeding, then the purchaser as a secured creditor would be entitled to enforce/foreclose on its security interest save for limited exceptions).

6.3 Suspect Period (Clawback). Under what facts or circumstances could the insolvency official rescind or reverse transactions that took place during a "suspect" or "preference" period before the commencement of the seller's insolvency proceedings? What are the lengths of the "suspect" or "preference" periods in your jurisdiction for (a) transactions between unrelated parties, and (b) transactions between related parties? If the purchaser is majority-owned or controlled by the seller or an affiliate of the seller, does that render sales by the seller to the purchaser "related party transactions" for purposes of determining the length of the suspect period? If a parent company of the seller guarantee's the performance by the seller of its obligations under contracts with the purchaser, does that render sales by the seller to the purchaser "related party transactions" for purposes of determining the length of the suspect period?

Separately from insolvency officials' right to avoid intentional acts of the insolvent that are harmful to, or that hinder, the insolvent's creditors, the Bankruptcy Code, the Civil Rehabilitation Law and the Corporate Reorganisation Law provide for avoidance rights of insolvency officials with respect to acts of the insolvent that took place after the earlier of the (i) suspension of payments in general and (ii) filing of a petition for the commencement of the insolvency proceedings, subject to certain conditions such as a requirement that relates to the relevant creditor's state of mind being satisfied;

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provided, however, that with respect to actions of the insolvent that relate to the granting of a security interest or discharging of an obligation of the insolvent, the insolvency official is entitled to avoid actions that took place after the earlier of the (a) insolvent's inability to pay its obligations, and (b) filing of a petition for the commencement of the insolvency proceedings, subject to certain conditions such as a requirement that relates to the relevant creditor's state of mind being satisfied (if the insolvent had no legal obligation to grant the security interest or to discharge its obligation at the time, then, the insolvency official may also avoid the relevant action provided it took place within 30 days before the insolvent's inability to pay its obligations). Furthermore, any gratuitous act (including acts that are deemed to be gratuitous) that took place after the suspension of payments or the filing of a petition for the commencement of the insolvency proceedings or within six months before the earlier of the two, can be avoided by the insolvency official. Since, as to the above-described rules, there is no special provision applicable only to transactions between unrelated parties or transactions between related parties under Japanese law, the same rules will apply to both types of transactions.

(Please note that there are certain exceptions to the above-described rules.)

In addition to the above, creditors of the insolvent may rescind actions of the insolvent that would prejudice creditors if certain conditions required under the general Civil Code are satisfied.

6.4 Substantive Consolidation. Under what facts or circumstances, if any, could the insolvency official consolidate the assets and liabilities of the purchaser with those of the seller or its affiliates in the insolvency proceeding? If the purchaser is owned by the seller or by an affiliate of the seller, does that affect the consolidation analysis?

No legal concept or theory that is equivalent or similar to the theory of substantial consolidation under US law exists under Japanese law. However, the insolvency official may be able to achieve a similar result through the application of the Japanese version of piercing the corporate veil doctrine. That is, if the corporate veil of the purchaser is pierced, since all the assets of the purchaser would be deemed part of the seller's (or its affiliate's) assets, a similar result would be achieved. According to case law, a corporate veil will be pierced only when: (a) the legal entity is a sham; or (b) the legal entity is abused so as to avoid certain legal provisions. Note that, while there are certain factors that are to be taken into account in determining whether or not the doctrine should be applied, a recent court judgment suggested that the corporate veil of an SPC would not be pierced merely because it was a paper company. If the purchaser is owned by the seller or by the seller's affiliate, the Japanese version of the piercing the corporate veil doctrine could be more likely to be applied.

6.5 Effect of Insolvency on Receivables Sales. If insolvency proceedings are commenced against the seller in your jurisdiction, what effect do those proceedings have on (a) sales of receivables that would otherwise occur after the commencement of such proceedings, or (b) on sales of receivables that only come into existence after the commencement of such proceedings?

In a bankruptcy proceeding, a rehabilitation proceeding or a reorganisation proceeding, the relevant insolvency official has the ability to rescind the insolvent's obligations under a bilateral contract in respect of which both parties' obligations are yet to be fulfilled.

If an insolvency proceeding is initiated prior to the transfer of receivables resulting from the sales thereof and if the sales price has not been paid, then the insolvency official will have the ability to rescind the sales agreement. To the contrary, a sales agreement of future receivables will not be rescinded simply because the receivables are future receivables. Sales of future receivables may be rescinded if the sale was through a continuous sale in connection with which the sales price for the future receivables has not been paid.

6.6 Effect of Limited Recourse Provisions. If a debtor's contract contains a limited recourse provision (see question 7.3 below), can the debtor nevertheless be declared insolvent on the grounds that it cannot pay its debts as they become due?

Yes, that is possible if the debtor owes any obligation that will not be extinguished via limited recourse provisions.

7 Special Rules

7.1 Securitisation Law. Is there a special securitisation law (and/or special provisions in other laws) in your jurisdiction establishing a legal framework for securitisation transactions? If so, what are the basics? Is there a regulatory authority responsible for regulating securitisation transactions in your jurisdiction?

(1) Special securitisation law

Yes: the Law Concerning Liquidation of Assets (the "Securitisation Law"). The Securitisation Law permits the setting up of a special purpose company (*tokutei mokuteki gaisha*; "TMK") and a special purpose trust (*tokutei mokuteki shintaku*; "TMS").

While there were a number of benefits in comparison to corporations incorporated under the general corporations law used for SPCs when the Securitisation Law was first introduced, following a series of amendments to the general corporations law, many of the benefits were lost, as they no longer belong only to TMKs. The primary benefits that still remain are: the pass-through tax status; beneficial tax treatment in connection especially with real estate taxes; and withholding tax on securities. Characteristically, a TMK is allowed to acquire only certain types of assets listed under the statute and the rules promulgated thereunder. In addition, TMKs are required to obtain evaluation(s) of the assets that each will acquire prior to the actual acquisitions thereof and the evaluations are required to be made by certain individuals/entities satisfying the qualifications stipulated in the statute. TMKs are allowed to issue bonds (*tokutei shasai*), physical CPs (*tokutei yakusoku tegata*) and book-entry CPs (*tokutei tanki shasai*) and preferred equity securities (*yusen shusshi*) to finance their acquisition of assets to be securitised. While a TMK may borrow money to finance such acquisition, some tax benefits would be lost if not from lenders that are qualified institutional investors ("QIIs") defined under the Financial Instruments and Exchange Act of Japan (the "FIEA") (which is the main body of securities regulations of Japan). Since TMKs are designed to be SPCs in nature, the statute prohibits TMKs from certain matters such as hiring employees, having a branch office, not appointing an underwriter/dealer in respect of its securities, doing business other than its "securitisation business" and not delegating the management (including sale and other dispositions) of its assets to qualified third parties.

A TMS has almost never been used due to its inflexibility in connection with structuring and the absence of tax benefits in respect of withholding tax, etc.

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(2) Regulatory authority

In a manner of speaking, yes there is a regulatory authority, but only covering certain types of securitisations and certain aspects of securitisation transactions: the Financial Services Agency (the "FSA") oversees the securities regulations aspect of securitisation transactions. In addition, although the Securitisation Law or other statutes do not specifically state that the FSA is responsible for securitisation transactions, the FSA plays a relatively big role in the regulation of securitisation transactions by administering policymaking concerning the financial system in Japan, supervising financial institutions and other entities, including TMKs, and surveying compliance with a number of statutes related to securitisation transactions such as the FIEA and the Securitisation Law. Furthermore, in cases of securitisation transactions utilising TMKs, certain regulatory oversight is provided for under the Securitisation Law; for example, certain periodical reports are required to be filed with the competent Local Finance Bureau regarding their business and financials.

7.2 Securitisation Entities. Does your jurisdiction have laws specifically providing for establishment of special purpose entities for securitisation? If so, what does the law provide as to: (a) requirements for establishment and management of such an entity; (b) legal attributes and benefits of the entity; and (c) any specific requirements as to the status of directors or shareholders?

Yes, please see question 7.1 above.

(a) While there are not many special requirements in establishing a TMK other than to name it a TMK in accordance with the statute, in order for a TMK to engage in the "securitisation business", among other requirements, the TMK must file a "business commencement statement" (*gyoumu-kaishi-todokede*) with a governmental agency prior to initiation of the TMK's "securitisation business"; an "asset liquidation plan" (*shisan-ryuudouka-keikaku*), which identifies the assets to be securitised and the terms and conditions of asset-backed securities to be issued and/or asset-backed loans to be borrowed to finance the acquisition of such assets by the TMK, must be attached to the statement as part of the exhibits thereto.

As for the management of TMKs, the statute provides certain rules in terms of the corporate governance regime, such as the requirement that no director (*torishimariyaku*) or statutory auditor (*kansayaku*) of a TMK may be a director of the entity that sells assets to the TMK as well as the requirement that an accountant or an accountancy firm be appointed as the TMK's statutory accounting auditor (*kaikei kansanin*) when certain conditions are met.

(b) Please see question 7.1 above.

(c) While there is no positive requirement/qualification for the status of a director or of a shareholder specifically stipulated under the statute, corporations in general and certain persons are barred from becoming a director (the list includes the seller or directors of the seller, bankrupt individuals receiving no rehabilitation order, individuals convicted of certain financial crimes, etc.).

7.3 Location and form of Securitisation Entities. Is it typical to establish the special purpose entity in your jurisdiction or offshore? If in your jurisdiction, what are the advantages to locating the special purpose entity in your jurisdiction? If offshore, where are special purpose entities typically located for securitisations in your jurisdiction? What are the forms that the special purpose entity would normally take in your jurisdiction and how would such entity usually be owned?

In the past, offshore entities were more often used as SPCs, but in recent years, it has become common practice to establish SPCs in Japan. Based on the current legislation, it is relatively easy and more cost-efficient to establish an SPC with bankruptcy remoteness in Japan. In addition, in the case where an SPC is an offshore entity and a non-resident of Japan, depending on the nature of the receivables, the proceeds of the receivables may be subject to withholding tax that would not apply if the SPC were a domestic entity (see question 9.1 below). Therefore, domestic entities are preferable and more suitable for SPCs in most cases.

The two most common forms that SPCs take are *godo kaisha* ("GK") and trusts. A GK is one of the types of corporate entities under the Companies Act. In some respects, it is similar to an LLC in the United States; however, it is not itself a pass-through entity for tax purposes. A GK is usually owned by an *ippan shadan hojin* ("ISH"), another type of corporate entity under special legislation, whose officers are, in cases where the entity is used for this purpose, accountants or other persons who have no interest in certain transactions in order to ensure the GK's bankruptcy remoteness. In such cases, the ISH is not supposed to receive dividends or residual assets from the GK; instead, a *tokumei kumiai* contract is normally entered into between the GK, as the operator, and an investor, and the GK distributes profits from the GK's business (if any) or refunds the *tokumei kumiai* principal to the investor. For more details regarding *tokumei kumiai*, please see question 4.14.

Another typical entity is a trust created in accordance with the Trust Law. In many cases, the trustor and the original holder of the trust beneficial interest is the seller (but in some cases, the arranger of the transaction or a bankruptcy remote SPC), and the trustee, which legally holds receivables or other assets as a result of entrustment or transfer, is either a commercial bank or a trust company that has a licence to conduct "trust business". In usual cases, trust beneficial interests are divided and sold to the investors, and as a result, the trust is owned by the investors, but in some cases, the initial trustor retains ownership of a part of the trust beneficial interests up until the end of the securitisation transaction, in which case, the investors invest in the trust by advancing a loan to the trust.

7.4 Limited-Recourse Clause. Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) limiting the recourse of parties to that agreement to the available assets of the relevant debtor, and providing that to the extent of any shortfall the debt of the relevant debtor is extinguished?

The general belief is that non-recourse provisions will be upheld as valid at least prior to the insolvency of the obligor. The same applies with most types of contracts even if a given contract is governed by non-Japanese law, so long as the provision is valid under that

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governing law. To the contrary, validity and legal effects of non-recourse provisions upon the insolvency of the obligor are not clear under Japanese law.

7.5 Non-Petition Clause. Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) prohibiting the parties from: (a) taking legal action against the purchaser or another person; or (b) commencing an insolvency proceeding against the purchaser or another person?

The general belief is that non-petition provisions will be upheld as valid for so long as the scope of a provision is reasonable (such as the effective term of the provision being limited to one year and one day after the payment in full to the investors); however, a Japanese court may treat a petition made in violation of a non-petition as a valid petition and determine that the remedy for the violation is to be provided through monetary compensation rather than dismissing the petition.

Since the matter concerns proceedings under the Japanese legal system, the governing law of non-petition provisions should be Japanese law. Whether Japanese courts will uphold non-petition provisions governed by non-Japanese law is unclear.

7.6 Priority of Payments "Waterfall". Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) distributing payments to parties in a certain order specified in the contract?

Yes, but excluding insolvency courts. If an insolvency proceeding is commenced in connection with the debtor, then the relevant insolvency statutes will come into effect, in which case, certain waterfall provision that contradicts the priority rules provided under the insolvency statutes will not be honoured by the competent court.

7.7 Independent Director. Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) or a provision in a party's organisational documents prohibiting the directors from taking specified actions (including commencing an insolvency proceeding) without the affirmative vote of an independent director?

The general belief is that such arrangements cannot be made under the Japanese legal environment, and therefore, in most cases, a Japanese SPC will have a sole independent director rather than having multiple directors that may include non-independent directors.

7.8 Location of Purchaser. Is it typical to establish the purchaser in your jurisdiction or offshore? If in your jurisdiction, what are the advantages to locating the purchaser in your jurisdiction? If offshore, where are purchasers typically located for securitisations in your jurisdiction?

It is typical to establish purchasing vehicles in Japan. Please see question 7.3 for more details.

8 Regulatory Issues

8.1 Required Authorisations, etc. Assuming that the purchaser does no other business in your jurisdiction, will its purchase and ownership or its collection and enforcement of receivables result in its being required to qualify to do business or to obtain any licence or its being subject to regulation as a financial institution in your jurisdiction? Does the answer to the preceding question change if the purchaser does business with more than one seller in your jurisdiction?

First, under Japanese law, there is no concept of a qualification to do business in Japan applicable to foreign corporations; however, foreign corporations are required to (1) appoint at least one representative officer/director who resides in Japan, and (2) register with a governmental agency, if they are to continuously do business in Japan; provided, further, that a foreign corporation whose primary purpose is to do business in Japan may not continuously do business in Japan, and a foreign corporation whose head office is located in Japan also may not continuously do business in Japan. Whether a one-time purchase and ownership or its collection and enforcement of receivables by a foreign SPC will be deemed a "continuous business" remains a subtle question; the answer to which is unclear (but if the foreign SPC does business with other sellers, then there is a chance that it will be deemed as doing continuous business in Japan; however, the governmental authority has suggested that the regulation is not intended to be applied to foreign corporations used as vehicles in securitisation transactions).

Separately, regardless of whether the purchaser is a foreign entity or a domestic entity, the purchaser may be prohibited from purchasing receivables depending on the asset class. That is, since the Lawyers' Code provides that no person may engage in the business of purchasing or otherwise acquiring receivables to enforce the receivables by means of litigation, mediation, conciliation or other means, the purchase of receivables may be deemed a violation of the Lawyer's Code, for example, if all of the purchased receivables are destined to be enforced through litigation. However, the Supreme Court has opined that a purchase of receivables does not violate the Lawyer's Code if the purchase does not harm the obligors' or public citizens' rights and legal interests and if the purchase falls within socially and economically justified business.

In addition, if the receivables to be purchased are, or include, a loan or loans extended by a moneylender regulated under the Moneylenders' Law, then certain provisions of the statute will become applicable to the purchaser (even if the purchaser is a foreign entity); please see question 8.3 below.

8.2 Servicing. Does the seller require any licences, etc., in order to continue to enforce and collect receivables following their sale to the purchaser, including to appear before a court? Does a third-party replacement servicer require any licences, etc., in order to enforce and collect sold receivables?

There is no general restriction on a seller of receivables continuing to collect receivables following their sale to the purchaser, however, collection activities of the seller are legally permissible only to the extent that they do not constitute or involve "legal affairs", which include appearance before a court.

Save for limited exceptions available to judicial scriveners and the exception made available to licensed special servicers, only an

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attorney or a legal corporation (which is an incorporated law firm) can represent a third party and appear before a court. Therefore, unless the seller is a special servicer licensed under the Servicer Law (the Act on Special Measures concerning Business of Management and Collection of Claims), the seller will not be able to appear before a court in enforcing the receivables sold to the purchaser.

8.3 Data Protection. Does your jurisdiction have laws restricting the use or dissemination of data about or provided by obligors? If so, do these laws apply only to consumer obligors or also to enterprises?

Yes. The Law Concerning the Protection of Personal Information regulates the: (i) acquisition; (ii) management and use; and (iii) disclosure of personal information about individuals (*kojin-jyoho*), by certain enterprises/individuals handling such personal information (*kojin-jyoho-toriatukai-gyousha*). The statute protects information in respect of individuals but not of corporations.

In addition, certain businesses such as financial institutions and banks are required to maintain and otherwise handle information and data about, or provided by, its clients (especially individuals, but not excluding corporations or other enterprises) with the due care of professionals and maintain adequate confidentiality.

8.4 Consumer Protection. If the obligors are consumers, will the purchaser (including a bank acting as purchaser) be required to comply with any consumer protection law of your jurisdiction? Briefly, what is required?

If the receivables are loans extended by moneylenders regulated under the Moneylenders' Law, the purchaser thereof will be subject to certain provisions of the statute, including, without limitation, the provisions providing for the following requirements:

- the purchaser will be required to deliver to each obligor, without delay, a notice that clearly indicates certain details of the relevant loan as required under the statute and rules promulgated thereunder upon the purchase of such receivables; and
- the purchaser will be required to furnish a receipt to each obligor every time the purchaser receives a payment from the obligor in accordance with the Moneylenders' Law.

8.5 Currency Restrictions. Does your jurisdiction have laws restricting the exchange of your jurisdiction's currency for other currencies or the making of payments in your jurisdiction's currency to persons outside the country?

(i) The Foreign Exchange and Foreign Trade Law, which is the statute primarily governing exchanges of currency does not restrict the exchange of Japanese currency for other currencies; however, there are certain after-the-fact reporting requirements.

(ii) Under the same statute, the making of payments or other transfer of money to persons of certain countries such as countries subject to economic sanctions is subject to approval by the government. Also, if a payment or other transfer of money to persons outside of the country is made by a resident of Japan, then such resident will be required to make an after-the-fact report to the relevant authority, except for cases prescribed in the relevant rules (such as a payment of less than 100 million Yen).

8.6 Risk Retention. Does your jurisdiction have laws or regulations relating to "risk retention"? How are securitisation transactions in your jurisdiction usually structured to satisfy those risk retention requirements?

There are no laws or regulations that force a seller to hold a portion of the securitisation products after selling the securitised assets. There is also a concern under Japanese law in connection with true sale analysis if a seller retains too much risk (and profits or interests) after selling the securitised assets (see also question 4.14). However, under certain guidelines for supervision of financial institutions by the FSA, when financial institutions (including insurance companies) hold securitisation products the risk of which is not held by the seller at all, the financial institutions are practically mandated to analyse such risk more carefully. Furthermore, practically speaking, regardless of whether or not the securitisation products are held by financial institutions, it is often the case that the seller will keep holding the subordinate portions of the securitisation products after selling the securitised assets to an SPC for the seller's economic benefit or at the request of a rating agency or other players in the securitisation transaction.

8.7 Regulatory Developments. Have there been any regulatory developments in your jurisdiction which are likely to have a material impact on securitisation transactions in your jurisdiction?

(i) Amendment of requirements for QII exemption

One of the most common types of securitisation transactions regarding trust beneficial interests in real estate uses a *tokumei kumiai* contract entered into by a GK (as SPC) with an investor or investors (the "TK investor"). In this case, the GK will be subject to the strict registration requirement under the FIEA unless an exemption applies. One of the widely-used exemptions available under the FIEA is the so-called "QII exemption". The requirements for the exemption and the regulations for the GK under the exemption became stricter following the amendment of the FIEA and the relevant cabinet order and cabinet office ordinance under the FIEA, which became effective in 2016.

(ii) Amendment to the Real Estate Specified Joint Enterprise Act (the "REJEA")

If a GK directly holds real estate acquired by raising funds from a TK investor or investors, it is generally subject to the licensing requirement under the REJEA unless an exemption applies. The REJEA was most recently amended in 2017 and new types of exemption were introduced in order to (a) ease restrictions under the REJEA and encourage investment in small-sized real estate, and (b) revise the rules to enhance investment in and the accumulation of improved quality real estate. Under the amendment, an appropriate legal framework for fundraising through crowdfunding has also been formulated.

(iii) Amendments to the general Civil Code

The legislation concerning contracts and obligations in the general Civil Code were amended in a material way in 2017 for the first time since it was enacted in 1896 (note that the amendment will become effective in 2020). The amendment includes material changes to general rules relating to transfers of claims, guarantees and standard terms and conditions applied to similar transactions, etc.; although the wording of the amendment itself is not believed to provide any significant setbacks or obstacles to securitisation practices in Japan, how the new rules are interpreted should be carefully monitored.

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9 Taxation

9.1 Withholding Taxes. Will any part of payments on receivables by the obligors to the seller or the purchaser be subject to withholding taxes in your jurisdiction? Does the answer depend on the nature of the receivables, whether they bear interest, their term to maturity, or where the seller or the purchaser is located? In the case of a sale of trade receivables at a discount, is there a risk that the discount will be recharacterised in whole or in part as interest? In the case of a sale of trade receivables where a portion of the purchase price is payable upon collection of the receivable, is there a risk that the deferred purchase price will be recharacterised in whole or in part as interest? If withholding taxes might apply, what are the typical methods for eliminating or reducing withholding taxes?

Whether withholding tax will be imposed depends on a number of factors, such as the nature of the receivables, whether they bear interest, whether the seller (or the purchaser) is a resident of Japan, whether there is a tax treaty between Japan and the country or jurisdiction of the seller (or the purchaser), and whether the payment by the obligor is made within Japan.

In the case of a sale of trade receivables at a discount, there is a high possibility that the discount will be recharacterised as interest. And, in the case of a sale of trade receivables where the payment of the purchase price is conditioned upon collection of the receivables, there is a risk/possibility that the deferred purchase price will be recharacterised as interest.

Insofar as the nature of the receivables calls for a withholding tax, generally speaking, there is no legal way to eliminate or reduce withholding tax. However, even in cases where withholding tax applies, any amount in excess of applicable income tax at the year-end that has been withheld can be refunded later with a proper filing. In other words, whether or not withholding tax applies, the total amount of tax imposed on the purchaser will not change, and withholding tax will influence only on the timing of the cash flow. Therefore, the influence on the cash flow resulting from withholding tax can be structurally dealt with if the economics of the deal allow, for example, by reserving a necessary amount of funds in advance.

9.2 Seller Tax Accounting. Does your jurisdiction require that a specific accounting policy is adopted for tax purposes by the seller or purchaser in the context of a securitisation?

The Corporations Tax Law generally requires corporations to adopt the Japanese GAAP unless otherwise required by law. Since there is no statute that specifically provides for an accounting policy for the seller or the purchaser in the context of a securitisation transaction, the Japanese GAAP will generally control; although there are certain matters for which tax law requires modifications to the accounting principles. For securitisation of receivables, the Accounting Policy regarding Financial Products introduced by the Accounting Standards Board of Japan, as well as the Practical Policy regarding Financial Products Accounting and Q&A for the Financial Products Accounting published by a committee of the Japanese Institute of Certified Public Accountants, provide the accounting rules.

9.3 Stamp Duty, etc. Does your jurisdiction impose stamp duty or other transfer or documentary taxes on sales of receivables?

Stamp duty (*inshi-zei*) of 200 Yen is imposed on each original copy of a sales contract whereby a receivable is assigned (e.g., a receivables sale agreement) with a sale value equal to or greater than 10,000 Yen.

9.4 Value Added Taxes. Does your jurisdiction impose value added tax, sales tax or other similar taxes on sales of goods or services, on sales of receivables or on fees for collection agent services?

Consumption tax (*shohi-zei*) and local consumption tax (*chiho-shohi-zei*) are imposed on the sale of goods or services otherwise exempted by relevant laws or regulations. With respect to sales of receivables, no consumption tax is imposed, whereas consumption tax and local consumption tax will be imposed on fees for collection agent services.

9.5 Purchaser Liability. If the seller is required to pay value-added tax, stamp duty or other taxes upon the sale of receivables (or on the sale of goods or services that give rise to the receivables) and the seller does not pay, then will the taxing authority be able to make claims for the unpaid tax against the purchaser or against the sold receivables or collections?

(i) Stamp duty

The purchaser is liable jointly and severally with the seller, if both the purchaser and the seller have prepared the documents together.

(ii) Consumption tax and local consumption tax

The taxing authority cannot make claims against the purchaser or on the receivables (so long as the sale is a true and perfected sale) for the unpaid tax.

9.6 Doing Business. Assuming that the purchaser conducts no other business in your jurisdiction, would the purchaser's purchase of the receivables, its appointment of the seller as its servicer and collection agent, or its enforcement of the receivables against the obligors, make it liable to tax in your jurisdiction?

As for stamp duty, please see question 9.5 above (stamp duty will be imposed irrespective of the status of the purchaser). With respect to income tax, if the purchaser is a foreign corporation or a non-resident of Japan, the income from the collection of the receivables will be taxable in Japan (and, if the purchaser has no "permanent establishment" in Japan, then withholding tax would generally be imposed with respect to certain income from receivables such as interest on loans). As for corporate tax, the purchaser's purchase of the receivables, its appointment of the seller as its servicer and collection agent, or its enforcement of the receivables against the obligors will not generally make it liable to corporate tax in Japan as long as the purchaser conducts no other business in Japan and is treated as having no permanent establishment nor its agent/representative in Japan with certain authority to act on behalf of the purchaser.

Note that if there is a tax treaty between Japan and the jurisdiction of the foreign corporation, the rules described above might be amended thereby.

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9.7 Taxable Income. If a purchaser located in your jurisdiction receives debt relief as the result of a limited recourse clause (see question 7.3 above), is that debt relief liable to tax in your jurisdiction?

Yes. Under Japanese tax law, for example, loan proceeds are not treated as taxable income at the time when the loan is advanced, and in turn, if the purchaser received debt relief with respect to repayment of the said loan, then such debt relief will be treated as taxable income whether or not the relief is as a result of a limited recourse clause.

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Luxembourg

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1 Receivables Contracts

1.1 Formalities. In order to create an enforceable debt obligation of the obligor to the seller: (a) is it necessary that the sales of goods or services are evidenced by a formal receivables contract; (b) are invoices alone sufficient; and (c) can a binding contract arise as a result of the behaviour of the parties?

Under Luxembourg law (provided the parties have reached an agreement), it is not necessary that the parties enter into a written agreement to evidence the sales of goods or services. According to article 109 of the Luxembourg Commercial Code, any means of evidence (including invoices) are acceptable in respect of agreements between merchants (*commerçants*) and, depending on the specific circumstances, an agreement between parties may be evidenced by their behaviour. However, according to article 1341 of the Luxembourg Civil Code and the Grand-Ducal Regulation dated 22 December 1986 made pursuant to article 1341 of the Luxembourg Civil Code, a contract, unless entered into between merchants (*commerçants*), shall be evidenced in writing if the value of the contract exceeds the amount of EUR 2,500.

Further, article 1326 of the Luxembourg Civil Code provides that if the agreement creates an obligation to pay a sum of money or deliver a fungible asset to only one party, the agreement must bear the signature of the obligor (handwritten or electronic) and mention the relevant amount/quantity in full words.

1.2 Consumer Protections. Do your jurisdiction's laws: (a) limit rates of interest on consumer credit, loans or other kinds of receivables; (b) provide a statutory right to interest on late payments; (c) permit consumers to cancel receivables for a specified period of time; or (d) provide other noteworthy rights to consumers with respect to receivables owing by them?

Consumer credit. The interest rate may, in principle, be freely determined between the parties to a loan agreement and may exceed the legal interest rate. However, if the interest rate is manifestly usury, a Luxembourg court may reduce it to the applicable legal interest rate. If the borrower is a consumer, information must be provided regarding the effective annual global interest rate (*taux annuel effectif global*) and on the interest amount charged for each instalment.

Interest on late payment. In commercial transactions between professionals, article 5 of the Luxembourg Law dated 18 April 2004 relating to late payment and overdue amounts, as amended, sets a maximum limit calculated on the basis of the ECB's key interest rate (*taux directeur*) plus 8%, unless otherwise provided in the relevant agreement. In transactions between a professional and a consumer, the interest rate on late payments is determined by a grand-ducal regulation for each calendar year; for 2018 it is fixed at 2.25%.

Compounding of interest. Pursuant to article 1154 of the Luxembourg Civil Code, contractual compounding of interest is, in principle, only permitted with respect to interest due and payable for a period of at least one year and where parties have agreed in writing to such compounding.

Early repayment. Under article L. 224-17 of the Luxembourg Consumer Code (the **Consumer Code**), a consumer has the right to proceed to an early repayment of its debt, in full or in part, under a consumer loan agreement without penalties. The lender may not charge any additional amount for the remaining term of the loan (i.e., interests or costs). However, the lender is entitled to recover fair and objectively justified costs which are directly linked to the early repayment, provided that the early repayment has been made during a fixed-rate period.

Consumer's right of withdrawal. Under article L. 224-15 of the Luxembourg Consumer Code, a consumer has a right of withdrawal in connection with its entry into a consumer loan agreement with a professional without any justification and for a period of 14 calendar days calculated on the later of: (i) the day of entry into the loan agreement; or (ii) the receipt by the consumer of the terms and conditions and information (to be included in the loan agreement) of the loan agreement. Under article L. 221-3 of the Luxembourg Consumer Code, a similar right is granted to consumers in relation to a number of other agreements (i.e., distance financial services contracts).

Moratorium on consumers' debts. In relation to their personal debts, individuals may request assistance from *the Commission de Médiation en matière de surendettement* in Luxembourg, in accordance with the provisions of the law of 8 January 2013 concerning over-indebtedness, as amended. The admission of such request by the commission triggers an automatic stay of proceedings which may have been commenced against the applicant. The stay period can last up to six months and may result, among others, in a restructuring of the debts or a reduction of agreed interest rates.

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1.3 Government Receivables. Where the receivables contract has been entered into with the government or a government agency, are there different requirements and laws that apply to the sale or collection of those receivables?

In general, there are no different requirements, which apply under Luxembourg law, if a receivables contract has been entered into with a public entity in Luxembourg provided that the public entity is carrying out a commercial transaction and is acting *jure gestionis*, i.e., the transaction is governed by private law as opposed to sovereign acts *jure imperii*, which are governed by public law.

2 Choice of Law – Receivables Contracts

2.1 No Law Specified. If the seller and the obligor do not specify a choice of law in their receivables contract, what are the main principles in your jurisdiction that will determine the governing law of the contract?

The provisions of Regulation (EC) No. 593/2008 of the European Parliament and Council dated 17 June 2008 on applicable law to contractual obligations (the **Rome I Regulation**), are directly applicable in Luxembourg. According to article 4 of the Rome I Regulation, where the seller and the obligor do not specify an express choice of law governing the receivables contract, the applicable law will be the law of the country which is (i) most closely connected to the situation, and (ii) typically the law of the country where the party to effect the characteristic performance of the contract has its residence, except when it results from the circumstances of the case that the contract is manifestly more closely connected with another country, in which case the law of that country shall apply.

2.2 Base Case. If the seller and the obligor are both resident in your jurisdiction, and the transactions giving rise to the receivables and the payment of the receivables take place in your jurisdiction, and the seller and the obligor choose the law of your jurisdiction to govern the receivables contract, is there any reason why a court in your jurisdiction would not give effect to their choice of law?

If (i) both the seller and the obligor have their seat in Luxembourg, (ii) the transfer of the receivables and their payment will occur in Luxembourg, and (iii) the seller and the obligor have chosen the law of Luxembourg to govern the receivables contract, the choice of the parties to have the receivables contract governed by Luxembourg law will be recognised and upheld by a Luxembourg court in accordance with the provisions of the Rome I Regulation.

2.3 Freedom to Choose Foreign Law of Non-Resident Seller or Obligor. If the seller is resident in your jurisdiction but the obligor is not, or if the obligor is resident in your jurisdiction but the seller is not, and the seller and the obligor choose the foreign law of the obligor/seller to govern their receivables contract, will a court in your jurisdiction give effect to the choice of foreign law? Are there any limitations to the recognition of foreign law (such as public policy or mandatory principles of law) that would typically apply in commercial relationships such as that between the seller and the obligor under the receivables contract?

If either: (i) the seller has its seat in Luxembourg but not the obligor; or (ii) the obligor has its seat in Luxembourg but not the seller, and the parties choose the foreign law of the country in which either the obligor or the seller have their respective seat to govern the receivables contract, the choice of the parties to have the receivables contract governed by foreign law will be recognised and upheld by a Luxembourg court in accordance with the provisions of the Rome I Regulation, unless the application of the provisions of foreign law would be manifestly incompatible with Luxembourg public policy (*ordre public*) provisions as provided by article 3(3) of the Rome I Regulation.

3 Choice of Law – Receivables Purchase Agreement

3.1 Base Case. Does your jurisdiction's law generally require the sale of receivables to be governed by the same law as the law governing the receivables themselves? If so, does that general rule apply irrespective of which law governs the receivables (i.e., your jurisdiction's laws or foreign laws)?

In principle, Luxembourg law does not require the sale of receivables to be governed by the same law as the law governing the receivables given that, in accordance with the provisions of the Rome I Regulation, the parties are free to choose the governing law of the transfer agreement which will determine the relation between the assignor and the assignee. However, the law governing the receivables will, pursuant to article 14 of the Rome I Regulation, among others, determine: (i) the assignability of the receivables; (ii) the relationship between the assignee and the obligor; (iii) the conditions under which the assignment can be invoked against the obligor; and (iv) whether payment by the obligor shall have the effect of discharging the obligor's obligations.

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3.2 Example 1: If (a) the seller and the obligor are located in your jurisdiction, (b) the receivable is governed by the law of your jurisdiction, (c) the seller sells the receivable to a purchaser located in a third country, (d) the seller and the purchaser choose the law of your jurisdiction to govern the receivables purchase agreement, and (e) the sale complies with the requirements of your jurisdiction, will a court in your jurisdiction recognise that sale as being effective against the seller, the obligor and other third parties (such as creditors or insolvency administrators of the seller and the obligor)?

A court in Luxembourg will recognise the sale of receivables as being effective against the seller, the obligor and other third parties (such as the creditors of the seller) provided that the sale of receivables is compliant with Luxembourg law. As per the effectiveness of such sale against insolvency administrators appointed with respect to the seller, it has to be highlighted that, under Luxembourg law, an insolvency administrator is not considered a third party and may, under certain circumstances, challenge the effectiveness of the sale of the receivables.

In the event that the receivables are sold by or to a Luxembourg securitisation vehicle governed by the Securitisation Law dated 22 March 2004, as amended (the **Securitisation Law**), pursuant to article 55 of the Securitisation Law, such sale will become effective between the parties and against third parties as from the moment the assignment is agreed on.

3.3 Example 2: Assuming that the facts are the same as Example 1, but either the obligor or the purchaser or both are located outside your jurisdiction, will a court in your jurisdiction recognise that sale as being effective against the seller and other third parties (such as creditors or insolvency administrators of the seller), or must the foreign law requirements of the obligor's country or the purchaser's country (or both) be taken into account?

Assuming the provisions of the Rome I Regulation are applicable, the sale of receivables is effective against the seller, the purchaser and the obligor. However, it is not clear, under the Rome I Regulation, which legal provisions determine the effectiveness of a transfer of receivables against third parties other than the obligor. Luxembourg conflict-of-law rules would generally point to the law of the country where the obligor is located and hence the formalities provided by the relevant foreign law for effectiveness against third parties would need to be analysed on a case-by-case basis.

If the receivables were assigned to a Luxembourg securitisation vehicle governed by the Securitisation Law, article 58 of that law provides that "*the law governing the assigned claim determines the assignability of such claim, the relationship between the assignee and the debtor, the conditions under which the assignment is effective against the debtor*".

As per the effectiveness of such sale against insolvency administrators appointed with respect to the seller, please refer to the answer to question 3.2 above.

3.4 Example 3: If (a) the seller is located in your jurisdiction but the obligor is located in another country, (b) the receivable is governed by the law of the obligor's country, (c) the seller sells the receivable to a purchaser located in a third country, (d) the seller and the purchaser choose the law of the obligor's country to govern the receivables purchase agreement, and (e) the sale complies with the requirements of the obligor's country, will a court in your jurisdiction recognise that sale as being effective against the seller and other third parties (such as creditors or insolvency administrators of the seller) without the need to comply with your jurisdiction's own sale requirements?

A court in Luxembourg will recognise the receivables purchase agreement as being effective against the seller – without the need to comply with Luxembourg's own sale requirements – assuming that the chosen applicable law to the receivables purchase agreement is compliant with the relevant provisions of the Rome I Regulation, unless the application of the provisions of foreign law would be manifestly incompatible with Luxembourg public policy (*ordre public*) provisions as provided by article 3(3) of the Rome I Regulation.

As per the effectiveness of the receivables purchase agreement against third parties and/or insolvency administrators, please refer to the answers to questions 3.2 and 3.3 above.

3.5 Example 4: If (a) the obligor is located in your jurisdiction but the seller is located in another country, (b) the receivable is governed by the law of the seller's country, (c) the seller and the purchaser choose the law of the seller's country to govern the receivables purchase agreement, and (d) the sale complies with the requirements of the seller's country, will a court in your jurisdiction recognise that sale as being effective against the obligor and other third parties (such as creditors or insolvency administrators of the obligor) without the need to comply with your jurisdiction's own sale requirements?

With respect to the effectiveness of the receivables purchase agreement against the obligor, a Luxembourg court will recognise the receivables purchase agreement as being effective against the obligor pursuant to article 14(2) of the Rome I Regulation which provides that the "*law governing the assigned or subrogated claim determines the conditions under which the assignment can be invoked against the obligor*".

With respect to the effectiveness of the receivables purchase agreement against third parties, a Luxembourg court will tend to designate the law of the country where the obligor has its seat (by application of Luxembourg conflict-of-law rules, which would generally point to the law of the country where the obligor is located). Hence, if the seat of the obligor is located in Luxembourg, the receivables purchase agreement will be effective and binding against third parties, if the obligor has been notified of the transfer of receivables in accordance with article 1690 of the Luxembourg Civil Code.

As per the effectiveness of the receivables purchase agreement against insolvency administrators, please refer to the answer to question 3.2 above.

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3.6 Example 5: If (a) the seller is located in your jurisdiction (irrespective of the obligor's location), (b) the receivable is governed by the law of your jurisdiction, (c) the seller sells the receivable to a purchaser located in a third country, (d) the seller and the purchaser choose the law of the purchaser's country to govern the receivables purchase agreement, and (e) the sale complies with the requirements of the purchaser's country, will a court in your jurisdiction recognise that sale as being effective against the seller and other third parties (such as creditors or insolvency administrators of the seller, any obligor located in your jurisdiction and any third party creditor or insolvency administrator of any such obligor)?

If the obligor has its seat in a foreign country, please refer to the answer to question 3.4. If the obligor has its seat in Luxembourg, please refer to the answer to question 3.5.

4 Asset Sales

4.1 Sale Methods Generally. In your jurisdiction what are the customary methods for a seller to sell receivables to a purchaser? What is the customary terminology – is it called a sale, transfer, assignment or something else?

Under Luxembourg law, a receivable can be transferred by way of assignment, subrogation or novation.

All rights and obligations on the receivables may be assigned by a seller to a purchaser pursuant to articles 1689 *et seq.* of the Luxembourg Civil Code. The purchaser will therefore become the legal owner of the receivables so transferred. Such transfer of the receivable should be then notified to the obligor in accordance with article 1690 of the Luxembourg Civil Code.

Pursuant to articles 1249 *et seq.* of the Luxembourg Civil Code, receivables may also be transferred by way of contractual subrogation, i.e., a third party will pay to the original creditor the amount owed by the obligor and will then be subrogated to all rights and actions the original creditor could have exercised against the obligor prior to the payment by the third party.

Also, pursuant to articles 1271 *et seq.* of the Luxembourg Civil Code, receivables may be transferred by way of novation, i.e., all parties must consent that a new creditor will substitute the original creditor and assume its obligations under a new agreement made between the new creditor and the obligor.

It has to be noted that pursuant to article 1278 of the Luxembourg Civil Code, any security interests (such as privileges or mortgages), attached to a former (extinct) claim lapse by virtue of the novation unless the creditor has explicitly reserved them to subsist.

4.2 Perfection Generally. What formalities are required generally for perfecting a sale of receivables? Are there any additional or other formalities required for the sale of receivables to be perfected against any subsequent good faith purchasers for value of the same receivables from the seller?

The perfection of the sale of receivables by way of assignment requires the notification of the obligor pursuant to article 1690 of the Luxembourg Civil Code. Prior to the notification, and provided the obligor is not aware of the assignment, the obligor will be discharged while making payments to the seller and the sale will not be enforceable against any subsequent purchasers provided that they are acting in good faith.

The formalities to be observed for perfection of a transfer of receivables by way of subrogation may vary depending on the context and should be analysed on the basis of the relevant facts. A notification to the debtor is, however, strongly recommended.

If the sale of receivables by way of assignment occurs as a transfer of title by way of security (*transfert de propriété à titre de garantie*) governed by the Law of 5 August 2005 on financial collateral arrangements, as amended (the **Law on Financial Collateral**), the assignment is perfected when the seller and purchaser have executed the transfer agreement. Hence, for perfection purposes, a notification of the transfer to the obligor is not required. However, provided the obligor is not aware of the assignment, the obligor will be discharged while making payments to the seller.

In the event that the purchaser is a securitisation vehicle, governed by the Securitisation Law, and provided both the seller and the obligor have their seat in Luxembourg, article 55 of the Securitisation Law provides that the assignment of the receivables is perfected, becoming effective between the parties and against third parties when the seller and purchaser have executed the transfer agreement, unless otherwise provided for in the relevant transfer agreement. Hence, for perfection purposes, a notification of the transfer to the obligor is not required. However, provided the obligor is not aware of the assignment, the obligor will be discharged while making payments to the seller.

4.3 Perfection for Promissory Notes, etc. What additional or different requirements for sale and perfection apply to sales of promissory notes, mortgage loans, consumer loans or marketable debt securities?

Promissory notes and bills of exchange. Promissory notes (*billets à ordre*) and bills of exchange (*lettre de change*) are commercial papers (*effets de commerce*), the transfers of which are regulated by the law of 8 January 1962 relating to promissory notes and bills of exchange, as amended. Pursuant to articles 11 *et seq.* of that law, promissory notes are transferred through endorsement (*endossement*) by means of physical delivery.

Consumer loans. Pursuant to article L. 224-18 of the Consumer Code, the assignment of a consumer loan to a third party must be notified to the contracting consumer, except where the original lender, by agreement with the assignee, continues to service the credit *vis-à-vis* the consumer. Consequently, in the first scenario, if the assignment has not been notified to the consumer, all payments made by the consumer towards the original lender are valid, as the original lender remains the sole financial counterparty of the consumer and not the purchaser.

Mortgage loans. Mortgages over real estate and other assets must be (i) formalised in a notarial deed passed in the presence of two notaries or one notary and two witnesses following article 2127 of the Luxembourg Civil Code and (ii) registered with the appropriate mortgage register. There are no specific provisions under Luxembourg law dealing with the perfection requirements applying to the transfer of mortgage as accessory. However, following the general rule provided by article 1692 of the Luxembourg Civil Code which applies to accessory security in Luxembourg, the transfer of receivables includes the transfer of its accessory rights such as a mortgage. Therefore, by transferring the mortgage loan to the transferee, the mortgage will, by operation of law, automatically be transferred to the transferee and hence, no specific provisions under Luxembourg law require the assignment of the mortgage to

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be registered in the mortgage register, to be enforceable against third parties. Registration of the mortgage may thus be done at any time before the mortgage lapses or is enforced. Pursuant to article 2154 of the Luxembourg Civil Code, the registration of the mortgage is valid and enforceable against third parties for 10 years and renewable for unlimited 10-year periods, provided that the underlying loan for which the mortgage was created is not extinguished and the 10-year term has not expired. In the absence of such renewal in due time, the security will no longer be enforceable and the secured creditor will lose its preferential rank over such immovable property.

Marketable debt securities. According to the provisions of the law of 10 August 1915 on commercial companies, as amended, the transfer of debt securities in bearer form is effected by the means of physical delivery from the transferor to the transferee without any further formalities, whereas the transfer of the debt securities in registered form must be recorded in the relevant register and be notified to the obligor in accordance with article 1690 of the Luxembourg Civil Code. The transfer of registered debt securities held on an account within the system of a securities depositary will be carried out by matching instructions from the transferor and the transferee to the securities depositary pursuant to which the securities depositary will transfer the purchase price to the account of the transferor and the debt securities to the account of the transferee.

Debt securities may also be issued in dematerialised form and are transferred by book-entry transfer between the relevant securities accounts.

4.4 Obligor Notification or Consent. Must the seller or the purchaser notify obligors of the sale of receivables in order for the sale to be effective against the obligors and/or creditors of the seller? Must the seller or the purchaser obtain the obligors' consent to the sale of receivables in order for the sale to be an effective sale against the obligors? Whether or not notice is required to perfect a sale, are there any benefits to giving notice – such as cutting off obligor set-off rights and other obligor defences?

As set out above, the sale of receivables must, in principle, be notified by the seller or the purchaser to the obligor in order to be perfected. In any case, if the obligor is not aware of the assignment, the obligor will be discharged while making payments to the seller. The obligor's consent to the assignment is not required provided that the agreement does not contain a clause preventing the seller from transferring the receivables. If the seller, despite such a clause in the agreement, assigns the receivables to the purchaser, the purchaser is, from a Luxembourg law perspective, likely not to be bound by this clause except if the purchaser has accepted the terms of the agreement.

If the purchaser of the receivables is a securitisation vehicle governed by the Securitisation Law and the agreement between the seller and the obligor prevents an assignment of the receivables, following article 57 of the Securitisation Law, the assignment will not be enforceable against the assigned obligor, unless (i) the obligor has agreed thereto, (ii) the assignee legitimately ignored such non-compliance, or (iii) the assignment relates to a monetary claim (*créance de somme d'argent*).

Provided that the conditions for a set-off under articles 1289 *et seq*. of the Luxembourg Civil Code are satisfied at the time of the perfection of the assignment, the obligor may set off its debt against obligations owed by the seller to the obligor even after a notification of the assignment.

4.5 Notice Mechanics. If notice is to be delivered to obligors, whether at the time of sale or later, are there any requirements regarding the form the notice must take or how it must be delivered? Is there any time limit beyond which notice is ineffective – for example, can a notice of sale be delivered after the sale, and can notice be delivered after insolvency proceedings have commenced against the obligor or the seller? Does the notice apply only to specific receivables or can it apply to any and all (including future) receivables? Are there any other limitations or considerations?

There are no particular rules applying to the form of notice and the manner in which the notice is delivered to the obligor. Pursuant to article 1129 of the Luxembourg Civil Code, only receivables that are determined or determinable at the time of the sale can be the subject of an assignment, hence the notice can extend to future receivables provided the future receivables are determined or determinable.

In principle, the notice can be delivered to the obligor after the sale of the receivables and after insolvency proceedings have been commenced against the seller. However, the notification of the sale to the obligor after insolvency proceedings have been commenced against the seller would not be binding against third parties, including the insolvency administrator appointed in respect of the seller.

If the purchaser of the receivables is a securitisation vehicle, then article 55 (2) of the Securitisation Law, which provides that "a future receivable can be assigned to a securitisation undertaking provided that it can be identified as being part of the assignment at the time it comes into existence or at any other time agreed between the parties", will be applicable to such a case.

4.6 Restrictions on Assignment – General Interpretation. Will a restriction in a receivables contract to the effect that "None of the [seller's] rights or obligations under this Agreement may be transferred or assigned without the consent of the [obligor]" be interpreted as prohibiting a transfer of receivables by the seller to the purchaser? Is the result the same if the restriction says "This Agreement may not be transferred or assigned by the [seller] without the consent of the [obligor]" (i.e., the restriction does not refer to rights or obligations)? Is the result the same if the restriction says "The obligations of the [seller] under this Agreement may not be transferred or assigned by the [seller] without the consent of the [obligor]" (i.e., the restriction does not refer to rights)?

The assessment of the above depends on the governing law, the specific content and the purpose of the agreement made between the seller and the obligor and must therefore be analysed on a case-by-case basis. Among others, it needs to be analysed whether the purchaser of the receivables will replace the seller in the contractual relationship with the obligor as a consequence of the assignment.

Depending on the type of contract and the main contractual obligations agreed between the parties, a restriction on assignment as regards the agreement as a whole could, from a purely Luxembourg law perspective, not necessarily be construed as requiring the consent of the obligor with respect to the transfer of receivables by the seller to the purchaser provided the receivables could qualify as specific rights and obligations, which are separate from the agreement as a whole.

Conversely, a restriction on assignment as regards the rights and obligations under the agreement would, from a purely Luxembourg law perspective, generally be construed as prohibiting a transfer

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of receivables from the seller to the purchaser given that the rights and obligations deriving from the receivables qualify as rights and obligations under the agreement.

If a restriction on assignment refers to the sole obligations of a seller, it is not likely to request for the obligor's consent in the event of an assignment of rights.

4.7 Restrictions on Assignment; Liability to Obligor. If any of the restrictions in question 4.6 are binding, or if the receivables contract explicitly prohibits an assignment of receivables or "seller's rights" under the receivables contract, are such restrictions generally enforceable in your jurisdiction? Are there exceptions to this rule (e.g., for contracts between commercial entities)? If your jurisdiction recognises restrictions on sale or assignment of receivables and the seller nevertheless sells receivables to the purchaser, will either the seller or the purchaser be liable to the obligor for breach of contract or tort, or on any other basis?

As regards the enforceability of clauses in an agreement restricting the assignment of receivables, please see the answer to question 4.4 above. Provided the obligor has suffered damages, the seller and the purchaser (if the purchaser is not acting in good faith) could, in principle, be held liable for breach of contract or tort.

4.8 Identification. Must the sale document specifically identify each of the receivables to be sold? If so, what specific information is required (e.g., obligor name, invoice number, invoice date, payment date, etc.)? Do the receivables being sold have to share objective characteristics? Alternatively, if the seller sells *all* of its receivables to the purchaser, is this sufficient identification of receivables? Finally, if the seller sells *all* of its receivables *other than* receivables owing by one or more specifically identified obligors, is this sufficient identification of receivables?

The transfer agreement does not need to specifically identify each of the receivables. However, the assigned receivables must be determined or determinable at the time of the sale.

4.9 Recharacterisation Risk. If the parties describe their transaction in the relevant documents as an outright sale and explicitly state their intention that it be treated as an outright sale, will this description and statement of intent automatically be respected or is there a risk that the transaction could be characterised by a court as a loan with (or without) security? If recharacterisation risk exists, what characteristics of the transaction might prevent the transfer from being treated as an outright sale? Among other things, to what extent may the seller retain any of the following without jeopardising treatment as an outright sale: (a) credit risk; (b) interest rate risk; (c) control of collections of receivables; (d) a right of repurchase/redemption; (e) a right to the residual profits within the purchaser; or (f) any other term?

In principle, a Luxembourg court will consider the economic characteristics of an agreement, the common interest of the parties and not rely *per se* on the denomination of the transaction given by the parties.

Unless a Luxembourg court, based on the factual elements of a transaction, takes the view that it was the intention of the parties to transfer the receivables for security purposes rather than to achieve a true sale and despite the seller retaining (i) the credit risk, (ii) the interest risk, (iii) the control of collections of receivables, or (iv) a repurchase/redemption right in relation to the receivables, it is unlikely that a Luxembourg court would, provided the sale of receivables has been duly perfected, recharacterise the transaction as a secured loan, even though this has not yet been tested in court.

Pursuant to article 56 (1) of the Securitisation Law, a claim assigned to a securitisation vehicle becomes part of its property as from the date on which the assignment becomes effective, notwithstanding (i) any undertaking by the securitisation vehicle to reassign the claim at a later date, and (ii) that the assignment can be recharacterised on grounds relating to the existence of such undertaking. Furthermore, the securitisation vehicle may entrust the assignor or a third party with the collection of receivables or with any other task relating to their management pursuant to article 59 of the Securitisation Law.

4.10 Continuous Sales of Receivables. Can the seller agree in an enforceable manner to continuous sales of receivables (i.e., sales of receivables as and when they arise)? Would such an agreement survive and continue to transfer receivables to the purchaser following the seller's insolvency?

The seller may agree to a continuous sale of receivables provided the receivables are determined or determinable. It is, however, recommended to notify such sale to the obligors for enforceability purposes.

As per the effectiveness of the sale of receivables following the seller's insolvency, please refer to the answers to questions 6.1 and 6.3 below.

4.11 Future Receivables. Can the seller commit in an enforceable manner to sell receivables to the purchaser that come into existence after the date of the receivables purchase agreement (e.g., "future flow" securitisation)? If so, how must the sale of future receivables be structured to be valid and enforceable? Is there a distinction between future receivables that arise prior to *versus* after the seller's insolvency?

In principle, a sale of future receivables is possible under Luxembourg law provided the future receivables are determined or determinable and that the sale has been notified to the obligor(s).

The Securitisation Law (under article 55 paragraphs (2) and (3)) expressly allows the assignment of future receivables and a securitisation vehicle can assert the assignment against third parties from the time of the agreement with the seller on the effective assignment of future receivables, which applies notwithstanding the opening of insolvency proceedings against the seller prior to the date on which the receivables come into existence.

4.12 Related Security. Must any additional formalities be fulfilled in order for the related security to be transferred concurrently with the sale of receivables? If not all related security can be enforceably transferred, what methods are customarily adopted to provide the purchaser the benefits of such related security?

The assignment of the receivables triggers, from a Luxembourg law perspective, the transfer of all rights and obligations incidental to the assigned receivables in favour of the purchaser. Thus, all accessory security interests (provided they are governed by

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Luxembourg law) securing the obligations under the assigned receivables are transferred, by operation of the law, to the purchaser and are enforceable by the purchaser against third parties.

The Securitisation Law (under article 56 paragraph (2)) explicitly provides that (i) the assignment of receivables entails the transfer of the guarantees and security interests securing such receivables, and (ii) no further formalities are requested under Luxembourg law in this respect.

4.13 Set-Off; Liability to Obligor. Assuming that a receivables contract does not contain a provision whereby the obligor waives its right to set-off against amounts it owes to the seller, do the obligor's set-off rights terminate upon its receipt of notice of a sale? At any other time? If a receivables contract does not waive set-off but the obligor's set-off rights are terminated due to notice or some other action, will either the seller or the purchaser be liable to the obligor for damages caused by such termination?

Legal set-off arises automatically and by operation of law where there are reciprocal claims between the parties, which are certain, due and payable. Provided the receivables contract does not contain a waiver as regards the set-off rights of the obligor against the seller, the notification of the transfer of receivables by the seller to the obligor does not trigger the termination of the obligor's set-off rights. As a result, provided the conditions for a legal set-off are satisfied at the time of the perfection of the assignment, the obligor may set off its debt against obligations owed by the seller to the obligor even after a notification of the assignment.

Provided that: (i) the conditions for a set-off were not satisfied at the time of the perfection of the assignment (i.e., the scenario set out in the previous paragraph does not occur and the notification of the transfer of receivables by the seller terminates the obligor's set-off rights); (ii) the receivables contract does not contain a waiver as regards the set-off rights of the obligor against the seller; and (iii) the obligor has suffered damages, the seller and the purchaser (if the purchaser is not acting in good faith) could, in principle, be held liable for breach of contract or tort.

4.14 Profit Extraction. What methods are typically used in your jurisdiction to extract residual profits from the purchaser?

In principle, Luxembourg law-governed securitisation vehicles do not generate profits due to their passive nature given that all income deriving from the underlying assets will be paid to the investors holding the securities or, as the case may be, to the shareholder(s) of the securitisation vehicle or the originator of the underlying assets.

5 Security Issues

5.1 Back-up Security. Is it customary in your jurisdiction to take a "back-up" security interest over the seller's ownership interest in the receivables and the related security, in the event that an outright sale is deemed by a court (for whatever reason) not to have occurred and have been perfected (see question 4.9 above)?

Given that, in general, it can be ascertained that the sale of receivables has been perfected, it is not customary from a Luxembourg law perspective to take a back-up security over the seller's ownership interest in the receivables. However, the taking of additional security is, of course, possible.

5.2 Seller Security. If it is customary to take back-up security, what are the formalities for the seller granting a security interest in receivables and related security under the laws of your jurisdiction, and for such security interest to be perfected?

Please see the answers to questions 5.1 and 5.3.

5.3 Purchaser Security. If the purchaser grants security over all of its assets (including purchased receivables) in favour of the providers of its funding, what formalities must the purchaser comply with in your jurisdiction to grant and perfect a security interest in purchased receivables governed by the laws of your jurisdiction and the related security?

The Law on Financial Collateral typically governs agreements creating security interests over receivables.

In practice, security interests over receivables are either created by a pledge agreement or by a transfer of title by way of security agreement, each governed by the provisions of the Law on Financial Collateral.

To perfect a pledge over receivables the purchaser acting as pledgor must be dispossessed with respect of the pledged assets, which can typically and automatically be achieved by the conclusion of the pledge over receivables agreement between the purchaser acting as pledgor and the pledgee. When executed by the purchaser and the secured parties, the pledge over receivables has been perfected against the debtor and third parties. However, the obligor of the receivables will be discharged while making payments to the purchaser unless the obligor has been notified of the pledge over receivables to the secured parties.

With respect to a transfer of title by way of security, the purchaser transfers the ownership in relation to the receivables to the secured parties until the secured obligations have been discharged, triggering the obligation of the secured parties to retransfer the receivables to the purchaser. When executed by the purchaser and the secured parties, the transfer agreement has been perfected. However, the obligor of the receivables will be discharged while making payments to the purchaser unless the obligor has been notified of the transfer of the title of the receivables to the secured parties.

A securitisation vehicle may only create security interests over its assets for the purpose of securing the obligations it has assumed for their securitisation or in favour of its investors or the trustee or fiduciary-representative acting for the investors.

5.4 Recognition. If the purchaser grants a security interest in receivables governed by the laws of your jurisdiction, and that security interest is valid and perfected under the laws of the purchaser's jurisdiction, will the security be treated as valid and perfected in your jurisdiction or must additional steps be taken in your jurisdiction?

The creation, perfection and enforcement of a security interest over receivables, which are, or are deemed to be, located in Luxembourg, are, pursuant to applicable Luxembourg conflict-of-law rules, governed by Luxembourg law.

Hence, even if the security interest over Luxembourg receivables were to be validly created and perfected pursuant to the applicable law of the country, where the purchaser has its seat, said security interest will, from a Luxembourg conflict-of-law perspective, only be validly created, perfected and enforceable, if the applicable Luxembourg rules are complied with.

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5.5 Additional Formalities. What additional or different requirements apply to security interests in or connected to insurance policies, promissory notes, mortgage loans, consumer loans or marketable debt securities?

Security interests over claims arising under insurance policies, mortgage loans or consumer loans are granted either in the form of a pledge or a transfer of title by way of security and insofar, as regards their perfection, the answer to question 5.3 is applicable.

A security interest over a promissory note is perfected by way of endorsement indicating that the security has been transferred for security purposes.

A security interest over debt securities in bearer form is perfected by the physical delivery of the debt securities to the pledgee or, as the case may be, depositary acting for the pledgee. A security interest over debt securities in registered form is perfected by inscription of the pledge in the register held with the issuer of the debt securities. A security interest over debt securities held in an account within the system of a securities depositary is perfected by, among others: (i) the entry into the pledge agreement made between the pledgor, the pledgee and the securities depositary or between the pledgor and the pledgee with notification to the securities depositary provided the latter will follow the pledgee's instructions relating to the debt securities; (ii) the registration of the debt securities in an account opened in the name of the pledgee; or (iii) the indication in the books of the securities depositary that the debt securities are pledged provided the debt securities are held in an account opened in the name of the pledgor.

A transfer of title by way of security in relation to registered debt securities is perfected by (i) the transfer of the debt securities to an account opened in the name of the transferee, or (if the debt securities are held in an account opened in the name of the transferor (book-entry securities)) (ii) the indication in the books of the account bank that legal title to the debt securities has been transferred to the transferee.

5.6 Trusts. Does your jurisdiction recognise trusts? If not, is there a mechanism whereby collections received by the seller in respect of sold receivables can be held or be deemed to be held separate and apart from the seller's own assets (so that they are not part of the seller's insolvency estate) until turned over to the purchaser?

Pursuant to the law of 27 July 2003 on trusts and fiduciary agreements, as amended (the **Fiduciary Law**) foreign trusts are recognised in Luxembourg to the extent that they are authorised by the law of the jurisdiction in which they are created.

Furthermore, according to the Fiduciary Law, a Luxembourg fiduciary may enter into a fiduciary agreement with a fiduciant, pursuant to which the fiduciary becomes the owner of a certain pool of assets forming the fiduciary estate, which are, even in an insolvency scenario, segregated from the assets of the fiduciary and held off-balance.

5.7 Bank Accounts. Does your jurisdiction recognise escrow accounts? Can security be taken over a bank account located in your jurisdiction? If so, what is the typical method? Would courts in your jurisdiction recognise a foreign law grant of security (for example, an English law debenture) taken over a bank account located in your jurisdiction?

Luxembourg law recognises the mechanism of escrow accounts, although this mechanism does not constitute a security *stricto sensu* and is not covered by the Law on Financial Collateral.

Security interests may be created over the balance standing to the credit of a specific bank account, which typically take the form of a pledge governed by the Law on Financial Collateral.

If, pursuant to Luxembourg conflict-of-law rules, an account is located, or would be deemed to be located, in Luxembourg, the relevant Luxembourg provisions will apply regarding the creation, perfection and enforceability of a security interest over such account. Hence, if the foreign law would not provide for the same rules, a Luxembourg court will not recognise the foreign law security interest over a Luxembourg account and would apply the relevant Luxembourg rules as regards the creation, perfection and enforceability of a security interest over an account located in Luxembourg.

Fiduciary mechanisms can also be used for the purpose of an escrow arrangement.

5.8 Enforcement over Bank Accounts. If security over a bank account is possible and the secured party enforces that security, does the secured party control all cash flowing into the bank account from enforcement forward until the secured party is repaid in full, or are there limitations? If there are limitations, what are they?

If a pledge has been granted on a bank account, upon the occurrence of the agreed event of default, the secured party would enforce the account pledge. As a result, the account's bank would block the pledged account and the pledgor would have no further access to the account. Hence, the pledgee controls, upon the occurrence of an event of default, the pledged account (unless the parties have agreed on a different mechanism in the pledge agreement regarding access to the account after an event of default has occurred) until the secured obligations have been fully discharged. Following the discharge of the secured obligations, the pledgee has the obligation to unblock the account and to release the pledge.

5.9 Use of Cash Bank Accounts. If security over a bank account is possible, can the owner of the account have access to the funds in the account prior to enforcement without affecting the security?

Pursuant to the provisions of the Law on Financial Collateral, the owner of the account (typically the pledger) may have access to the funds in the pledged account until enforcement of the pledge, without affecting the security.

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6 Insolvency Laws

6.1 Stay of Action. If, after a sale of receivables that is otherwise perfected, the seller becomes subject to an insolvency proceeding, will your jurisdiction's insolvency laws automatically prohibit the purchaser from collecting, transferring or otherwise exercising ownership rights over the purchased receivables (a "stay of action")? If so, what generally is the length of that stay of action? Does the insolvency official have the ability to stay collection and enforcement actions until he determines that the sale is perfected? Would the answer be different if the purchaser is deemed to only be a secured party rather than the owner of the receivables?

Provided the sale of the receivables cannot be challenged by the insolvency administrator appointed with respect to the seller, i.e., (i) the sale of receivables has been perfected in connection with applicable law, (ii) the sale has not been executed during the pre-bankruptcy suspect period, which is a period of six months and 10 days preceding the opening of insolvency proceedings against the seller, or (iii) the receivables were not transferred under value, there will be no stay of action preventing the purchaser from collecting, transferring or otherwise exercising ownership rights with respect to the receivables.

In addition, the transfer of receivables, provided that provisions of the Law on Financial Collateral are applicable to such transfer, may only be set aside in case of manifest fraud.

6.2 Insolvency Official's Powers. If there is no stay of action, under what circumstances, if any, does the insolvency official have the power to prohibit the purchaser's exercise of its ownership rights over the receivables (by means of injunction, stay order or other action)?

The insolvency administrator could prohibit the purchaser's exercise of rights by way of summary proceedings while challenging the validity of the transfer or the perfection of the transfer of the receivables.

6.3 Suspect Period (Clawback). Under what facts or circumstances could the insolvency official rescind or reverse transactions that took place during a "suspect" or "preference" period before the commencement of the seller's insolvency proceedings? What are the lengths of the "suspect" or "preference" periods in your jurisdiction for (a) transactions between unrelated parties, and (b) transactions between related parties? If the purchaser is majority-owned or controlled by the seller or an affiliate of the seller, does that render sales by the seller to the purchaser "related party transactions" for purposes of determining the length of the suspect period? If a parent company of the seller guarantee's the performance by the seller of its obligations under contracts with the purchaser, does that render sales by the seller to the purchaser "related party transactions" for purposes of determining the length of the suspect period?

As stated in the answer to question 6.1 above, the insolvency administrator could challenge the validity of the transfer of receivables, if the transfer was executed during the pre-bankruptcy suspect period, which is a period of six months and 10 days preceding the opening of insolvency proceedings against the seller.

As regards the length of the pre-bankruptcy suspect period, there is no difference with respect to transactions carried out between related or unrelated parties. However, if the activities and assets of the seller and the purchaser are commingled and hence could be seen as one common estate, the insolvency administrator may, depending on the factual circumstances, extend to the purchaser insolvency proceedings which were initially commenced against the seller.

6.4 Substantive Consolidation. Under what facts or circumstances, if any, could the insolvency official consolidate the assets and liabilities of the purchaser with those of the seller or its affiliates in the insolvency proceeding? If the purchaser is owned by the seller or by an affiliate of the seller, does that affect the consolidation analysis?

In principle, and subject to what is stated in the answer to question 6.3 above, the insolvency administrator could not, in the context of an insolvency scenario, consolidate the assets and liabilities of the purchaser with those of the seller or its affiliates.

6.5 Effect of Insolvency on Receivables Sales. If insolvency proceedings are commenced against the seller in your jurisdiction, what effect do those proceedings have on (a) sales of receivables that would otherwise occur after the commencement of such proceedings, or (b) on sales of receivables that only come into existence after the commencement of such proceedings?

Provided the provisions of the Securitisation Law are applicable, a securitisation vehicle can assert the assignment of future receivables against third parties from the time of the agreement with the seller on the effective assignment of future receivables, which applies notwithstanding the opening of insolvency proceedings against the seller prior to the date on which the receivables come into existence.

6.6 Effect of Limited Recourse Provisions. If a debtor's contract contains a limited recourse provision (see question 7.3 below), can the debtor nevertheless be declared insolvent on the grounds that it cannot pay its debts as they become due?

There is only little published case law and legal literature as regards limited recourse provisions under Luxembourg law. As a consequence, Luxembourg law would tend to turn to Belgian legal doctrine and case law, which we understand admit, in principle, the validity and enforceability of limited recourse provisions provided the *pari passu* treatment of creditors is not violated and the limited recourse provisions are not designed to unfairly impair the rights of certain creditors to the detriment of one or more creditors.

Provided that the contractual limited recourse provisions in the documentation, to which the debtor and the creditor are a party, are effective and lawful under Luxembourg law (when the debtor is a securitisation undertaking under the Securitisation Law or a fiduciary within the meaning of the Fiduciary Law), the creditor should, from a Luxembourg law perspective, not have an interest to act (*intérêt à agir*) against the securitisation undertaking or the fiduciary beyond the available pool of assets to which its recourse is limited and, depending on the contractual mechanism embedded

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in the documentation, its claim should be extinguished once the relevant assets have been realised. As a result, the creditor should not be in a position to file a valid petition for bankruptcy against the securitisation undertaking or the fiduciary with the competent Luxembourg court on the basis of the balance of the outstanding debt, where the assets of the securitisation undertaking or the fiduciary prove to be insufficient to fully satisfy the claim of the creditor.

7 Special Rules

7.1 Securitisation Law. Is there a special securitisation law (and/or special provisions in other laws) in your jurisdiction establishing a legal framework for securitisation transactions? If so, what are the basics? Is there a regulatory authority responsible for regulating securitisation transactions in your jurisdiction?

The Securitisation Law established a particular legal framework for securitisation transactions in Luxembourg.

In accordance with the Securitisation Law, a securitisation is a transaction by which a securitisation vehicle (i) acquires or assumes, directly or through another vehicle, risks relating to claims, other assets, or obligations assumed by third parties, and (ii) issues securities, whose value or yield depends on such risks.

Under the Securitisation Law, almost all classes of assets are capable of being securitised.

The securitisation may be completed either (i) on a true sale basis, whereas the securitisation vehicle will acquire full legal title in relation to the underlying assets, or (ii) by the synthetic transfer of the risk pertaining to the underlying assets through the use of derivative instruments. To finance the transfer of risk, the securitisation vehicle must issue negotiable securities, i.e., equity or debt instruments, which can be freely transferred by assignment or physical delivery and which are subscribed by the investors. With the issue proceeds derived from the securities' issue, the securitisation vehicle will acquire the risks pertaining to the underlying assets.

As per the regulatory authority responsible for regulating securitisation transactions in Luxembourg, please see the answer to question 7.2 below.

7.2 Securitisation Entities. Does your jurisdiction have laws specifically providing for establishment of special purpose entities for securitisation? If so, what does the law provide as to: (a) requirements for establishment and management of such an entity; (b) legal attributes and benefits of the entity; and (c) any specific requirements as to the status of directors or shareholders?

The Securitisation Law allows for two types of securitisation entities, which may be set up in the form of a company or a fund.

A securitisation fund does not have legal personality, is managed by a management company and consists of one or more co-ownerships (*copropriétés*) or one or more fiduciary estates. The management regulations expressly specify whether the fund is subject to the provisions of the Luxembourg Civil Code on co-ownership or the rules on trusts and fiduciary contracts set out in the Fiduciary Law, which allow for the legal separation of the fiduciary assets from the trustee's assets.

It should be noted that, in practice, securitisation funds are not often used and, in most cases, the securitisation vehicle is incorporated in accordance with the general provisions of the Luxembourg law dated 10 August 1915 on commercial companies, as amended, whereas the articles of incorporation of the securitisation vehicle are expressly made subject to the provisions of the Securitisation Law.

A securitisation company can be set up as a public limited liability company (*société anonyme*), a corporate partnership limited by shares (*société en commandite par actions*), a private limited liability company (*société à responsabilité limitée*) or a co-operative company organised as a public limited company (*société coopérative organisée comme une société anonyme*).

Luxembourg securitisation vehicles are, in principle, unregulated entities not subject to any authorisation or prudential supervision by the Luxembourg financial sector regulator (the **CSSF**) unless they issue securities to the public on a continuous basis. In such a case their activity must be authorised by the CSSF prior to the first issue of securities. However, the securitisation vehicle may be exempt from the requirement to be licensed by the CSSF provided it does not issue more than three series of securities per year to the public or the denomination of the securities is at least EUR 125,000.

If a securitisation vehicle is a regulated entity, the CSSF must (i) approve the directors of the vehicle and hence the directors will need to evidence a certain track record and experience within the field of securitisation and (ii) examine whether its direct or indirect shareholders are in a position to exercise a significant influence over the conduct of the business of such securitisation vehicle, are of sufficiently good repute and have the experience or means required for the performance of their duties.

As of 18 April 2018, 33 securitisation vehicles are registered on the official list of authorised securitisation vehicles held and published by the CSSF and hence subject to the supervision of the CSSF.

7.3 Location and form of Securitisation Entities. Is it typical to establish the special purpose entity in your jurisdiction or offshore? If in your jurisdiction, what are the advantages to locating the special purpose entity in your jurisdiction? If offshore, where are special purpose entities typically located for securitisations in your jurisdiction? What are the forms that the special purpose entity would normally take in your jurisdiction and how would such entity usually be owned?

Establishment of special purpose vehicles in Luxembourg and advantages to locating the special purpose entity in Luxembourg: Luxembourg is a well-known jurisdiction for the establishment of securitisation vehicles which can benefit from the provisions of the Securitisation Law and the favourable tax regime applicable to securitisation vehicles in Luxembourg. However, the special purpose vehicle's shares are usually held by an offshore company for tax and insolvency remoteness reasons.

Typical forms of the special purpose entities: Luxembourg securitisation vehicles are often set-up as a public limited liability company (*société anonyme*) or a private limited liability company (*société à responsabilité limitée*).

Ownership of the special purpose entities: Luxembourg special purpose vehicles are usually owned by orphan entities for tax and insolvency remoteness purposes, such as a Dutch *Stichting* (being a special type of Dutch trust foundation controlled by a board of directors). Such orphan entities are mainly used in order to isolate the obligations of the special purpose vehicle from those of the originator.

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7.4 Limited-Recourse Clause. Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) limiting the recourse of parties to that agreement to the available assets of the relevant debtor, and providing that to the extent of any shortfall the debt of the relevant debtor is extinguished?

Under the Securitisation Law, contractual limited recourse clauses are recognised (even if the relevant agreement or the terms and conditions of the notes are not governed by Luxembourg law) and will be upheld by Luxembourg courts. In addition, the Securitisation Law provides for a statutory ring-fencing mechanism, which can be established by the creation of compartments within the securitisation vehicle. The securitisation vehicle may allocate assets and liabilities to a specific compartment and the creditors and investors of that specific compartment have no recourse to assets, which are allocated to other compartments of the securitisation vehicle, i.e., each compartment forms a separate estate and the assets of which are segregated from those allocated to other compartments of the securitisation vehicle. The constitutional documents of the securitisation vehicle and the transaction documents entered into in relation to a specific securitisation transaction should always contain the appropriate limited recourse wording.

7.5 Non-Petition Clause. Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) prohibiting the parties from: (a) taking legal action against the purchaser or another person; or (b) commencing an insolvency proceeding against the purchaser or another person?

Under the Securitisation Law non-petition clauses are recognised (even if the relevant agreement or the terms and conditions of the notes are not governed by Luxembourg law) and will be upheld by Luxembourg courts. Hence, investors or creditors of the securitisation vehicle may waive their right to submit a petition for the commencement of insolvency proceedings against the securitisation vehicle.

The constitutional documents of the securitisation vehicle and the transaction documents entered into in relation to a specific securitisation transaction should always contain the appropriate non-petition wording.

7.6 Priority of Payments "Waterfall". Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) distributing payments to parties in a certain order specified in the contract?

Under the Securitisation Law, subordination clauses are recognised (even if the relevant agreement or the terms and conditions of the notes are not governed by Luxembourg law) and will be upheld by Luxembourg courts. The constitutional documents of the securitisation vehicle and the transaction documents entered into in relation to a specific securitisation transaction should always contain the appropriate subordination wording.

7.7 Independent Director. Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) or a provision in a party's organisational documents prohibiting the directors from taking specified actions (including commencing an insolvency proceeding) without the affirmative vote of an independent director?

The enforceability of contractual provisions prohibiting the directors from taking specified actions (including commencing insolvency proceedings) without the affirmative vote of an independent director could be problematic from a Luxembourg perspective given that, in certain circumstances, the directors may have the legal obligation to make a filing for insolvency. However, the relevant articles of incorporation could provide that certain actions can only be validly taken with the affirmative vote of the independent director. The relevance of such a clause may be less important in the Luxembourg context, since a Luxembourg securitisation vehicle should be insolvency-remote.

7.8 Location of Purchaser. Is it typical to establish the purchaser in your jurisdiction or offshore? If in your jurisdiction, what are the advantages to locating the purchaser in your jurisdiction? If offshore, where are purchasers typically located for securitisations in your jurisdiction?

Luxembourg is a well-known jurisdiction for the establishment of securitisation vehicles which can benefit from the provisions of the Securitisation Law. As per the advantages to locating the securitisation vehicle in Luxembourg, please refer to the answer to question 7.3 above.

8 Regulatory Issues

8.1 Required Authorisations, etc. Assuming that the purchaser does no other business in your jurisdiction, will its purchase and ownership or its collection and enforcement of receivables result in its being required to qualify to do business or to obtain any licence or its being subject to regulation as a financial institution in your jurisdiction? Does the answer to the preceding question change if the purchaser does business with more than one seller in your jurisdiction?

The purchaser will not be required to obtain a business licence in Luxembourg or an authorisation from the CSSF approving its activity in connection with the provisions of the Luxembourg law dated 5 April 1993 on the financial sector, as amended (the **Financial Sector Law**), only because the purchaser will purchase or collect receivables from one or more sellers having their seat in Luxembourg or enforce, as the case may be, the receivables in Luxembourg acquired from them.

8.2 Servicing. Does the seller require any licences, etc., in order to continue to enforce and collect receivables following their sale to the purchaser, including to appear before a court? Does a third-party replacement servicer require any licences, etc., in order to enforce and collect sold receivables?

Assuming that provisions of Luxembourg law apply to the seller, a debt collection activity carried out in Luxembourg requires, in

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principle, the prior authorisation of the CSSF pursuant to article 28-3 of the Financial Sector Law. However, a securitisation vehicle may entrust the seller or a third party with the collection of receivables pursuant to article 60 of the Securitisation Law. In such a scenario, the seller or the third party, acting as a servicer, does not need to apply for a CSSF licence under the Financial Sector Law.

In a true sale transaction, the purchaser or, as the case may be, its representative will appear in court with respect to any litigation in connection with the receivables given that the purchaser is the legal owner of the receivables.

8.3 Data Protection. Does your jurisdiction have laws restricting the use or dissemination of data about or provided by obligors? If so, do these laws apply only to consumer obligors or also to enterprises?

The Law of 2 August 2002 on the protection of persons with regard to the processing of personal data, as amended, (the **Data Protection Law**), implementing the Directive 95/46/EC on the protection of individuals (the **Data Protection Directive**), establishes standards for the collection and processing of personal data, which restrict, among others, the use and dissemination of data about, or provided by, obligors to third parties and to entities having their seat in non-EU Member States. The person, whose data will be processed, has a right of information, a right to access the data, and a right to oppose any processing or communication of that data. The Data Protection Law only covers the collection and processing of personal data in relation to individual consumers.

The Data Protection Law and the Data Protection Directive will be replaced by the Regulation (EU) No. 2016/679 on the protection of natural persons with regard to the processing of personal data (the **GDPR**) and by a new Luxembourg law yet to be passed, as from 25 May 2018. On 12 September 2017, a draft bill of the law complementing the GDPR was submitted to the Luxembourg Chamber of Deputies.

8.4 Consumer Protection. If the obligors are consumers, will the purchaser (including a bank acting as purchaser) be required to comply with any consumer protection law of your jurisdiction? Briefly, what is required?

The Luxembourg Consumer Code provides rules that are binding on the purchaser of receivables arising under a consumer credit contract. In general, notification with respect to the transfer of the receivables to the obligor should be made by the seller (article L. 224-18 (2) of the Luxembourg Consumer Code). However, a notification is not required if the seller continues to service the credit *vis-à-vis* the consumer. Further, pursuant to article L. 224-18 (1) of the Luxembourg Consumer Code, the consumer retains the right to raise all defences and exceptions against the purchaser, which it could have raised against the seller prior to the perfection of the transfer of the receivables.

8.5 Currency Restrictions. Does your jurisdiction have laws restricting the exchange of your jurisdiction's currency for other currencies or the making of payments in your jurisdiction's currency to persons outside the country?

Luxembourg does not have currency or exchange controls or central bank approval requirements restricting payments to entities located outside Luxembourg.

8.6 Risk Retention. Does your jurisdiction have laws or regulations relating to "risk retention"? How are securitisation transactions in your jurisdiction usually structured to satisfy those risk retention requirements?

The Regulation (EU) No. 575/2013 on prudential requirements for credit institutions and investment firms (the **CRR Regulation**), which has been directly applicable since 1 January 2014 and the Law of 15 July 2015 transposing, among others, the Directive 2013/36/EU on access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms (the **CRD Law**), apply to Luxembourg securitisation transactions (within the meaning of "securitisation" therein). The CRR Regulation and the CRD Law provide that credit institutions when acting in a particular capacity, such as originator, sponsor or lender, and also when investing in securitisation transactions, shall be exposed to the credit risk of the securitisation position in their trading book or non-trading book and must explicitly disclose that they will retain, on an ongoing basis, a material net economic interest measured at the origination which, in any event, shall not be less than 5 % of the nominal value of the securitisation position.

In addition, the Regulation (EU) 2017/2402 on simple, transparent and standardised securitisation (the **STS Regulation**), which will apply from 1 January 2019, will also require that the originator, sponsor or original lender of a "securitisation" (as defined therein) shall retain, on an ongoing basis, a material net economic interest in the securitisation transaction of no less than 5%. However, there shall be no multiple applications of the retention requirements for any given securitisation.

The risk retention requirements of the CRD Law/CRR Regulation and the STS Regulation are typically satisfied by having the originator, sponsor or original lender hold at least 5% of the outstanding principal balance of each class of securities (vertical slice) or 5% of the fair value of all the issued securities (horizontal slice).

Further, the European Banking Authority guidelines EB/GL/2015/20 (the **EBA Guidelines**), to be read in conjunction with the CSSF Circular No. 16/647, on limits on exposure to shadow banking entities that carry out bank-like activities outside a regulated framework (and developed in accordance with article 395(2) of the CRR Regulation), apply to all institutions subject to part four (Large Exposures) of the CRR Regulation which shall comply with the aggregate exposure limits or tighter individual limits set on exposures to shadow banking entities carrying out banking activities outside a regulated framework (including special-purpose vehicles engaged in securitisation transactions).

8.7 Regulatory Developments. Have there been any regulatory developments in your jurisdiction which are likely to have a material impact on securitisation transactions in your jurisdiction?

PRIIPs Regulation

Regulation (EU) No. 1286/2014 on key information documents for packaged retail and insurance-based investment products (the **PRIIPs Regulation**) entered into force on 29 December 2014 and took effect on 1 January 2018. The PRIIPs Regulation requires that all packaged retail and insurance-based investment products (the **PRIIPs**) manufacturers provide a key information document (the **KID**) to retail investors in order to enable retail investors to understand and compare the key features and risks of the PRIIPs. Structured securities, e.g., mortgage backed securities (**MBS**) or

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asset backed securities (**ABS**), including financial instruments issued by special purpose vehicles, fall under the scope of the definition of PRIIPs. Hence as from 1 January 2018, any securitisation vehicle which issues debt securities falling under the scope of the PRIIPs Regulation must provide its potential retail investors with a KID according to the standard laid down in the PRIIPs Regulation.

The Commission Delegated Regulation (EU) 2017/653 of 8 March 2017 supplementing the PRIIPs Regulation lays down regulatory technical standards with regard to the presentation, content, review and revision of KIDs and the conditions for fulfilling the requirement to provide such documents, and applies as of 1 January 2018.

On 25 October 2017, a draft bill implementing the PRIIPs Regulation and modifying the amended Luxembourg Law of 17 December 2010 on undertaking for collective investment and the amended Luxembourg Law of 7 December 2015 on the insurance sector, was deposited with the Luxembourg Chamber of Deputies. The draft bill designates the CSSF and the *Commissariat aux Assurances* (**CAA**) as the competent supervisory authorities regarding supervision and compliance with the requirements of the PRIIPs Regulation.

The application of the PRIIPs Regulation to Luxembourg securitisation vehicles should be analysed on a case-by-case basis considering that most Luxembourg securitisation vehicles are unregulated entities, not subject to any authorisation or prudential supervision by the CSSF, and issue debt securities to institutional and professional investors rather than to retail investors.

STS Regulation

On 28 December 2017, the STS Regulation was published in the Official Journal of the European Union. The STS Regulation lays down a general framework for securitisation, defines securitisation and establishes due diligence, risk-retention and transparency requirements for parties involved in securitisations, criteria for credit granting, requirements for selling securitisations to retail clients, a ban on re-securitisation, requirements for securitisation vehicles as well as conditions and procedures for securitisation repositories. It also creates a specific framework for simple, transparent and standardised (**STS**) securitisation.

The STS Regulation came into force on 17 January 2018 and will apply, subject to transitional provisions, from 1 January 2019.

The Securitisation Law which outlines the legal framework for securitisation in the broad sense is bound to be amended in the near future in order to comply with the requirements of the STS Regulation as Member States retain discretion as to whether and how to apply certain provisions contained in the STS Regulation. No draft bill has been submitted to the Chamber of Deputies in this respect yet.

9 Taxation

9.1 Withholding Taxes. Will any part of payments on receivables by the obligors to the seller or the purchaser be subject to withholding taxes in your jurisdiction? Does the answer depend on the nature of the receivables, whether they bear interest, their term to maturity, or where the seller or the purchaser is located? In the case of a sale of trade receivables at a discount, is there a risk that the discount will be recharacterised in whole or in part as interest? In the case of a sale of trade receivables where a portion of the purchase price is payable upon collection of the receivable, is there a risk that the deferred purchase price will be recharacterised in whole or in part as interest? If withholding taxes might apply, what are the typical methods for eliminating or reducing withholding taxes?

As a matter of principle, there is no withholding tax in Luxembourg on payments of all items of income from capital other than dividends. In particular, Luxembourg does not apply any withholding tax on interest paid by one of its residents to a Luxembourg non-resident (unless such interest is not at arm's length or paid under a profit participating bond/security). The withholding tax exemption also covers dividend payments made by securitisation companies or funds on shares.

By way of exception, an individual beneficial owner of interest or similar income made or ascribed by a paying agent (in the sense of the law of 23 December 2005, as amended, the **Relibi Law**) established in Luxembourg to an individual beneficial owner who is a resident of Luxembourg, will be subject to a withholding tax of currently 20%. Such a withholding tax will be in full discharge of income tax if the beneficial owner is an individual acting in the course of the management of his/her private wealth (the **20% Withholding Tax**). Responsibility for the withholding of such tax will be assumed by the Luxembourg paying agent.

An individual beneficial owner of interest or similar income, who is a resident of Luxembourg and acts in the course of the management of his/her private wealth, may opt for a final 20% Withholding Tax when he/she receives or is deemed to receive such interest or similar income from a paying agent established in an EU Member State (other than Luxembourg) or in a state of the European Economic Area (which is not an EU Member State).

Unless the terms of a sale of trade receivables could be considered abusive, there is no reason to recharacterise a discount or a deferred purchase price as interest. However, it should be noted that a repayment above the discounted price would be fully taxable unless such sale at a discount would be structured in a tax-efficient way.

9.2 Seller Tax Accounting. Does your jurisdiction require that a specific accounting policy is adopted for tax purposes by the seller or purchaser in the context of a securitisation?

Luxembourg has no specific accounting policy for tax purposes in the context of securitisation insofar as the Luxembourg tax law usually follows the accounting rules applicable in Luxembourg as per the law of 10 August 1915 on commercial companies, as

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amended and the law of 19 December 2002 on the Luxembourg trade and companies register as well as accountancy and companies annual accounts, as amended (the **2002 Law**).

The Luxembourg accounting rules will vary according to the legal form adopted by the seller or purchaser.

With regard to securitisation vehicles, the form may either be that of a securitisation company or that of a securitisation fund. In both cases, the accounts of a securitisation company must be audited by an independent auditor. If the securitisation vehicle issues securities to the public on a continuous basis, both the securitisation vehicle and the independent auditor must be authorised by the CSSF.

A securitisation company is subject to the accounting rules under the 2002 Law, whereas a securitisation fund is subject to accounting and tax regulations applicable to investment funds provided for by the law of 17 December 2010 relating to undertakings for collective investments, as amended. Thus, the securitisation company may choose between Luxembourg generally accepted accounting principles (the **GAAP**) under the historical cost convention, Luxembourg GAAP under the fair value convention, or international financial reporting standards (the **IFRS**), while the securitisation fund may choose IFRS or Luxembourg GAAP under mark-to-market convention unless otherwise stated in the management regulations.

Crucially, the CSSF has confirmed that securitisation companies with multiple compartments should present their financial statements in such a form that the financial data for each compartment is clearly stated.

In addition, waterfall structures and valuation methods used to identify impairments or losses related thereto should be presented in the notes to be appended to the relevant financial statements.

Finally, a securitisation vehicle may book additional liability (at least tax-wise) to compensate "technical profit", i.e., profit linked to cash flows received by the securitisation vehicle which will be distributed to the shareholders of the securitisation company or the unit holders of the securitisation fund in later financial years, in order to provide a true and fair view of the financial situation and to avoid unwarranted taxation.

9.3 Stamp Duty, etc. Does your jurisdiction impose stamp duty or other transfer or documentary taxes on sales of receivables?

According to article 52 § 1 of the Securitisation Law, all agreements entered into in the context of a securitisation transaction, as well as all other deeds relating to such transaction, are exempt from registration formalities if they do not have the effect of transferring rights pertaining to Luxembourg real estate, aircraft or ships. However, they may be presented for registration, in which case they will be subject to a fixed charge of EUR 12.

9.4 Value Added Taxes. Does your jurisdiction impose value added tax, sales tax or other similar taxes on sales of goods or services, on sales of receivables or on fees for collection agent services?

A securitisation vehicle should be considered as a taxable person according to Circular No. 723 issued by the Luxembourg Value Added Tax Administration (*Administration de l'enregistrement et des domaines*). Should the purchaser be considered as a taxable person in Luxembourg, the sale of goods or services would generally be subject to a value added tax (VAT) at rates typically lower than those of Luxembourg's neighbours (14% and 17%). However, transactions (except those related to collection of receivables) and negotiations related to receivables as well as management of securitisation vehicles located in Luxembourg are exempt from VAT.

The concept of "management" of securitisation vehicles is quite vague. In addition to the management of the portfolio (by the securitisation company itself, a management company or fiduciary representative), most administrative services should benefit from the VAT exemption.

9.5 Purchaser Liability. If the seller is required to pay value-added tax, stamp duty or other taxes upon the sale of receivables (or on the sale of goods or services that give rise to the receivables) and the seller does not pay, then will the taxing authority be able to make claims for the unpaid tax against the purchaser or against the sold receivables or collections?

The purchaser is jointly and severally liable for the payment of VAT on goods and services sold to it (including relevant fines) toward the country where the VAT is due except if the purchaser proves that it has, in good faith, paid the VAT to the supplier.

9.6 Doing Business. Assuming that the purchaser conducts no other business in your jurisdiction, would the purchaser's purchase of the receivables, its appointment of the seller as its servicer and collection agent, or its enforcement of the receivables against the obligors, make it liable to tax in your jurisdiction?

With regard to the tax to be withheld by the purchaser, the rules detailed above in answer to question 9.1 are applicable. As the investors are treated like bondholders with no direct profit participation, no withholding tax should be applicable unless the payments of the purchaser fall under the scope of the Relibi Law.

Regarding net wealth tax, since 1 January 2016, securitisation vehicles have been subject to a minimum net wealth tax in Luxembourg (contingent to their balance sheet of either a fixed amount of EUR 4,815 or to a progressive rate between EUR 535 and EUR 32,100).

Regarding corporate income tax and municipal business tax, the tax treatment depends on the corporate form of the purchaser.

A. Securitisation vehicle organised as a corporate entity

A securitisation vehicle organised as a corporate entity with either its statutory seat or central administration in Luxembourg, is fully liable to corporate income and municipal business taxes at an aggregate tax rate of 26.01% (irrespective of the vehicle's activity and possible appointment of a servicer or collection agent). However, in this case, commitments made by the purchaser to remunerate its investors qualify as interest on debt (even if paid as return on equity) and are fully tax deductible. Hence, the purchaser's taxable basis should, as a rule, be very limited if not nil.

The purchaser should, nevertheless, be subject to a minimum net wealth tax. Should the purchaser be identified as a *Soparfi* (i.e., a corporation that has aggregate financial assets, securities and bank deposits exceeding 90% of its balance sheet total and an amount of EUR 350,000) it should be subject to a EUR 4,815 minimum net wealth tax (including solidarity surcharge).

Moreover, no capital duty applies on incorporation of the corporate form (except for a fixed registration duty of EUR 75).

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Ultimately, securitisation companies may obtain tax residency certificates from the Luxembourg tax authorities to fully benefit from the European directives and Luxembourg's important tax treaty network.

B. Securitisation funds

Securitisation funds should arguably be considered tax-wise as investment funds transparent for Luxembourg tax purposes. Hence, they are not liable to corporate income tax and municipal business tax.

Finally, both the fiduciary representative and the management company of a securitisation fund with their statutory seat or central administration (or even permanent establishment) in Luxembourg should be subject to corporate income tax, municipal business tax and net wealth tax in Luxembourg. They may also be subject to VAT (please refer to the answer of question 9.4 above). The fiduciary representative must, in addition, pay a registration tax of EUR 1,000 and an annual registration tax of EUR 1,000 to the CSSF.

9.7 Taxable Income. If a purchaser located in your jurisdiction receives debt relief as the result of a limited recourse clause (see question 7.3 above), is that debt relief liable to tax in your jurisdiction?

In general, a debt relief should be a taxable item in Luxembourg.

However, in case the purchaser is a securitisation company, taxable profits should be very limited or neutralised completely at the level of a securitisation company given the fact that commitments assumed *vis-à-vis* the investors and any other creditor by a securitisation company, are considered fully tax-deductible business expenses.

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Malta

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1 Receivables Contracts

1.1 Formalities. In order to create an enforceable debt obligation of the obligor to the seller: (a) is it necessary that the sales of goods or services are evidenced by a formal receivables contract; (b) are invoices alone sufficient; and (c) can a binding contract arise as a result of the behaviour of the parties?

(a) As a general principle of Maltese law, there are no specific formalities which are required to evidence a sale of goods or services. The Civil Code, Chapter 16 of the Laws of Malta (the "**Civil Code**"), however, establishes instances where the contract needs to be in the form of a public deed or a private writing. Notwithstanding the above, it is always good practice to evidence sales of goods and services through a contract.

For certain consumer credit agreements (entered into between a creditor or a credit intermediary, where applicable, and a consumer) additional rules apply in terms of Consumer Credit Regulations, Subsidiary Legislation 378.12 of the Laws of Malta (the "**Consumer Credit Regulations**") and the Credit Agreements for Consumers Relating to Residential Immovable Property Regulations, Subsidiary Legislation 378.10 (the "**Consumer Residential Property Regulations**") where the credit agreement shall be drawn up in writing or on a durable medium and must contain certain specified information.

(b) While a written agreement is not strictly required to create an enforceable debt obligation, invoices alone do not constitute an enforceable debt obligation unless countersigned by the buyer. An invoice is merely evidence of an obligation owed to the seller by the obligor to pay but must generally be accompanied by further circumstances that together demonstrate sufficient evidence of the debt obligation such as, for example, the express or tacit acknowledgment of the invoice of the debtor.

(c) Yes. Maltese Law recognises tacit/implied contracts that are not formalised in writing. The party alleging a binding contract, however, must be able to prove it. This does not apply where the law requires the contract to be in the written form.

1.2 Consumer Protections. Do your jurisdiction's laws: (a) limit rates of interest on consumer credit, loans or other kinds of receivables; (b) provide a statutory right to interest on late payments; (c) permit consumers to cancel receivables for a specified period of time; or (d) provide other noteworthy rights to consumers with respect to receivables owing by them?

(a) In terms of the Civil Code, the general limit on interest rates is set at 8% *per annum*. However, in terms of the Interest Rate (Exemptions) Regulations (Subsidiary Legislation 16.06 of the Laws of Malta), credit institutions (including banks) may charge higher interest rates (as they are exempt from the above-mentioned limitation) when providing loans, advances or other credit facilities. This notwithstanding, it should be noted that the Securitisation Act, Chapter 484 of the Laws of Malta (the "**Securitisation Act**") expressly provides that the provisions of the Civil Code or of any other law that limits or restrict the charging of interest and compound interest shall not apply to debts or any other obligations in the context of a securitisation transaction subject to the Securitisation Act, and it shall be lawful for the amount of interest due in respect of any such debt or other obligation to exceed the amount of capital due in respect of any such debt or obligation.

(b) In terms of the Consumer Residential Property Regulations and the Consumer Credit Regulations, the creditor may specify an interest rate applicable for late payments. In terms of the Civil Code of Malta, such interest must be capped at 8% and must be due for a period of not less than a year.

(c) For certain consumer credit arrangements (excluding those instances where the credit agreement must be entered into in front of a notary), in terms of the Consumer Credit Regulations, the consumer has a right to withdraw from a credit agreement without giving any reasons. This right to withdraw must be exercised within 14 running days calculated in terms of Consumer Credit Regulations.

d) In terms of both Consumer Credit Regulations and the Consumer Residential Property Regulations, the consumer is given various statutory rights including those which relate to the disclosures which must be made to the consumer and those which relate to information which must be included in the relevant credit agreement. Notably, this includes a statutory right given to the consumer to the full early repayment of the receivable subject to the payment of compensation to the creditor.

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1.3 Government Receivables. Where the receivables contract has been entered into with the government or a government agency, are there different requirements and laws that apply to the sale or collection of those receivables?

The law does not distinguish between receivables owed by the government, government agencies or otherwise. However, additional aspects including rules on sovereign immunity, state aid, public procurement and the capacity of the relevant entity to enter into such a contract should be considered. In terms of the Code of Organisation and Civil Procedure (Chapter 12 of the Laws of Malta), there are certain issues which would need to be considered in so far as the enforcement of warrants on government property.

2 Choice of Law – Receivables Contracts

2.1 No Law Specified. If the seller and the obligor do not specify a choice of law in their receivables contract, what are the main principles in your jurisdiction that will determine the governing law of the contract?

Regulation (EC) No. 593/2008 of the European Parliament and of the Council on the law applicable to contractual obligations of 17 June 2008 (the "**Rome I Regulation**"), which is directly applicable in Malta, sets out the law applicable to contractual obligations on civil and commercial matters.

The choice of law to govern the transaction documents relating to a securitisation transaction would generally be recognised and given effect to as a valid choice of law in any action before the courts of Malta in accordance with the provisions of the Rome I Regulation, subject to the specific circumstances of each case as set out further below.

The Securitisation Act further expressly provides that the parties to a securitisation transaction shall be free to choose any law to govern contracts relating or ancillary to a securitisation transaction. In accordance with the Rome I Regulation, where the parties do not specify a law in terms of Article 3 of the Rome I Regulation, the applicable law will be determined in light of the nature of the relevant contract in terms of Article 4 of the Rome I Regulation. In the case of receivables contracts, the contract shall be governed by:

(a) the law where the party required to effect the characteristic performance of the contract has their habitual residence;

(b) the law of another jurisdiction, if it emerges from the circumstances of the case that the contract is manifestly more closely connected to that jurisdiction; or

(c) where the applicable law cannot be determined in accordance with (a) and (b), the law of the country with which the contract is most closely connected.

For certain contracts, including contracts of carriage, insurance contracts and individual employment contracts, certain specific rules apply. These rules are subject to certain overriding mandatory provisions including public policy considerations and other instances for the safeguarding of a state's public interests, such as its political, social or economic organisation.

2.2 Base Case. If the seller and the obligor are both resident in your jurisdiction, and the transactions giving rise to the receivables and the payment of the receivables take place in your jurisdiction, and the seller and the obligor choose the law of your jurisdiction to govern the receivables contract, is there any reason why a court in your jurisdiction would not give effect to their choice of law?

Maltese courts would apply Article 3 of Rome I Regulation which allows the contracting parties to freely choose their governing law. It should be noted, however, that:

(a) in terms of the Rome I Regulation, there are certain instances where other laws may prevail irrespective of the choice of governing law, including: (i) in the case of overriding mandatory provisions or the public policy of the forum; (ii) where all other 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 the parties does not prejudice the application of provisions of the law of that other country which cannot be derogated from by agreement; and (iii) where all other elements relevant to the situation at the time of choice are located in one or more Member States of the European Communities, the parties' choice of applicable law other than that of a Member State shall not prejudice the application of provisions of Community law, where appropriate as implemented in the Member State of the forum, which cannot be derogated from by agreement; and

(b) in certain instances, the Rome I Regulation also imposes limits on the autonomy of the will of the parties to select the applicable law in contract, such as the law applicable to contracts of carriage, consumer contracts, insurance contract and individual employment contracts.

2.3 Freedom to Choose Foreign Law of Non-Resident Seller or Obligor. If the seller is resident in your jurisdiction but the obligor is not, or if the obligor is resident in your jurisdiction but the seller is not, and the seller and the obligor choose the foreign law of the obligor/seller to govern their receivables contract, will a court in your jurisdiction give effect to the choice of foreign law? Are there any limitations to the recognition of foreign law (such as public policy or mandatory principles of law) that would typically apply in commercial relationships such as that between the seller and the obligor under the receivables contract?

As stated in question 2.2 above, in terms of the Rome I Regulation, a Maltese court will give effect to the parties' choice of law, provided that where all other elements relevant to the particular situation are connected with Malta, the choice of law does not prejudice the application of public policy rules. Other considerations which should be considered on a case-specific basis include where the contract is one of insurance, individual employment contracts and where a contract is concluded with a consumer.

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3 Choice of Law – Receivables Purchase Agreement

3.1 Base Case. Does your jurisdiction's law generally require the sale of receivables to be governed by the same law as the law governing the receivables themselves? If so, does that general rule apply irrespective of which law governs the receivables (i.e., your jurisdiction's laws or foreign laws)?

No, although in practice assignment of receivables agreements (as well as any security agreements) are almost always governed by the law of the jurisdiction of the receivables.

In terms of the Rome I Regulation, the parties are free to choose any law irrespective of the law governing the sale of receivables, subject to any restrictions indicated in questions 2.2 and 2.3 above. The choice of law governing the sale of receivables will govern the relationship between the assignor and assignee.

Article 14 of the Rome I Regulation provides that the law governing the underlying receivables will determine the following matters:

- whether it can be assigned;
- the relationship between the assignee and the debtor;
- the conditions under which the assignment or subrogation can be invoked against the debtor; and
- any question whether the debtors obligations have been discharged.

This takes into account the obligatory aspects of the assignment and not the proprietary aspects of the transfer.

3.2 Example 1: If (a) the seller and the obligor are located in your jurisdiction, (b) the receivable is governed by the law of your jurisdiction, (c) the seller sells the receivable to a purchaser located in a third country, (d) the seller and the purchaser choose the law of your jurisdiction to govern the receivables purchase agreement, and (e) the sale complies with the requirements of your jurisdiction, will a court in your jurisdiction recognise that sale as being effective against the seller, the obligor and other third parties (such as creditors or insolvency administrators of the seller and the obligor)?

Yes, as long as all the requisite formalities applicable to the assignment have been complied with in terms of Maltese law. See question 4.2 below.

3.3 Example 2: Assuming that the facts are the same as Example 1, but either the obligor or the purchaser or both are located outside your jurisdiction, will a court in your jurisdiction recognise that sale as being effective against the seller and other third parties (such as creditors or insolvency administrators of the seller), or must the foreign law requirements of the obligor's country or the purchaser's country (or both) be taken into account?

Yes, as long as all the requisite formalities applicable to the assignment have been complied with in terms of Maltese law. See question 4.2 below.

3.4 Example 3: If (a) the seller is located in your jurisdiction but the obligor is located in another country, (b) the receivable is governed by the law of the obligor's country, (c) the seller sells the receivable to a purchaser located in a third country, (d) the seller and the purchaser choose the law of the obligor's country to govern the receivables purchase agreement, and (e) the sale complies with the requirements of the obligor's country, will a court in your jurisdiction recognise that sale as being effective against the seller and other third parties (such as creditors or insolvency administrators of the seller) without the need to comply with your jurisdiction's own sale requirements?

Yes. See question 3.1 above.

3.5 Example 4: If (a) the obligor is located in your jurisdiction but the seller is located in another country, (b) the receivable is governed by the law of the seller's country, (c) the seller and the purchaser choose the law of the seller's country to govern the receivables purchase agreement, and (d) the sale complies with the requirements of the seller's country, will a court in your jurisdiction recognise that sale as being effective against the obligor and other third parties (such as creditors or insolvency administrators of the obligor) without the need to comply with your jurisdiction's own sale requirements?

Yes. See question 3.1 above.

3.6 Example 5: If (a) the seller is located in your jurisdiction (irrespective of the obligor's location), (b) the receivable is governed by the law of your jurisdiction, (c) the seller sells the receivable to a purchaser located in a third country, (d) the seller and the purchaser choose the law of the purchaser's country to govern the receivables purchase agreement, and (e) the sale complies with the requirements of the purchaser's country, will a court in your jurisdiction recognise that sale as being effective against the seller and other third parties (such as creditors or insolvency administrators of the seller, any obligor located in your jurisdiction and any third party creditor or insolvency administrator of any such obligor)?

Yes, see question 3.1 above. However, it would also be prudent to comply with all the requisite formalities applicable to the assignment under Maltese law (as the governing law of the receivable). See question 4.2 below.

4 Asset Sales

4.1 Sale Methods Generally. In your jurisdiction what are the customary methods for a seller to sell receivables to a purchaser? What is the customary terminology – is it called a sale, transfer, assignment or something else?

Receivables are usually transferred by assignment, the governing law of which would be the same as the governing law of the receivables, which may, but would typically not, be Maltese law. However, the Securitisation Act provides that the seller and the purchaser have absolute discretion to choose which method is employed in

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transferring the securitisation assets to the purchaser, including, without limitation, by novation, sale, assignment, and declaration of trust. Receivables are usually transferred by assignment, the governing law of which would be the same as the governing law of the receivables, which in most cases would not be Maltese law.

4.2 Perfection Generally. What formalities are required generally for perfecting a sale of receivables? Are there any additional or other formalities required for the sale of receivables to be perfected against any subsequent good faith purchasers for value of the same receivables from the seller?

The formalities required for perfection of a sale of receivables will depend on the governing law of the receivables and the governing law of the sale or assignment. While requirements vary from jurisdiction to jurisdiction, perfection typically takes place by notifying or obtaining acknowledgment of the assignment from the obligor. Even where Maltese law is not the governing law of the receivables and the assignment, it is prudent to ensure that perfection requirements of Maltese law are also satisfied.

The Civil Code regulates assignments of debts and other rights in general. The Civil Code generally provides that the assignment or sale of a debt is complete, and the ownership is automatically acquired by the assignee, as soon as the debt or the right and the price have been agreed upon, provided that an assignment must be in writing in order for it to be valid. Moreover, the obligor must be notified of the assignment by judicial act (which involves a court process) in order for it to be effective against third parties (i.e. for perfection of the assignment). Notification is not required where the obligor as acknowledged the assignment.

Article 1484A of the Civil Code, however, provides that notice of an assignment need not fulfil the aforementioned formalities and could instead be satisfied by simple notification in writing (by any means), where in the case of an assignment of one or more debts:

- the assignor is a trader (i.e. a person that exercises acts of trade in his own name);
- the debts being assigned arise out of or in connection with the trade or business being carried out by the trader; and
- the assignee is a person licensed to carry out the business of banking or the business of factoring under the applicable laws of Malta, or the equivalent laws in a jurisdiction recognised by Malta Financial Service Authority (the "MFSA").

Moreover, certain provisions of the Securitisation Act were specifically introduced to disapply or modify various provisions of the Civil Code relating to assignment of rights in order to relax what are generally considered to be overly onerous procedures (stemming from Malta's civil law tradition) within a securitisation context. An assignment of assets to a Maltese securitisation vehicle is complete and the ownership of the assets is automatically acquired by the securitisation vehicle as soon as the assignment is reduced to writing. Obligors can be notified in writing by any means or by publication of a notice in a daily newspaper circulated wholly or mainly in the jurisdiction where the majority of the Obligors reside (as opposed to notification by judicial act).

The notification of assignment of existing receivables or future receivables must include the relevant features of the class of receivables being assigned. See question 4.8 for the relevant features that must be identified in relation to existing receivables and future receivables, respectively.

4.3 Perfection for Promissory Notes, etc. What additional or different requirements for sale and perfection apply to sales of promissory notes, mortgage loans, consumer loans or marketable debt securities?

Promissory Notes. The transfer requirements for promissory notes (and other negotiable instruments) are governed by the Commercial Code of Malta (Chapter 13 of the Laws of Malta), which provides that they are transferable by the endorsement of the promissory note by the transferee.

Mortgage or Consumer Loans. There are generally no additional or specific requirements to those outlined in question 4.2 above.

Marketable Debt Securities. The transfer of bearer securities is perfected by delivery to the transferee. The transfer of registered securities is perfected by registration of the transferee in the relevant register. Transfers of non-dematerialised marketable securities in a Maltese company must be in writing and delivered to the company for registration. Dematerialised marketable securities (in a Maltese company) held through a central securities depository and represented by book-entries may be transferred by an entry on the register maintained by the central securities depository (and by debiting the central securities depository account of the relevant seller and crediting the central securities depository account of the purchaser) without the need for any instrument in writing.

4.4 Obligor Notification or Consent. Must the seller or the purchaser notify obligors of the sale of receivables in order for the sale to be effective against the obligors and/or creditors of the seller? Must the seller or the purchaser obtain the obligors' consent to the sale of receivables in order for the sale to be an effective sale against the obligors? Whether or not notice is required to perfect a sale, are there any benefits to giving notice – such as cutting off obligor set-off rights and other obligor defences?

The Obligor must be notified of the assignment (by judicial act, by simple notification or as otherwise permitted by the Securitisation Act, as applicable – see question 4.2 above) in order for the assignment to be effective against third parties, provided that notification is not required where the Obligor has acknowledged the assignment.

The Civil Code provides that in default of notice being given to the Obligor:

- the Obligor may not set up the assignment against the seller, and if he pays the debt to him he is thereby discharged;
- if the seller, after having assigned the debt to a purchaser, makes a second assignment thereof to another person who is in good faith, such other person, if he has given notice of the assignment made in his favour, shall be preferred to the former purchaser;
- if the creditors of the seller shall sue out a garnishee order attaching the sum due in the hands of the Obligor, they shall be preferred to the purchaser, even though they have become creditors only after the assignment; and
- the Obligor is entitled to set off any sum which may become due to him by the seller; but the purchaser may not set off the debt assigned to the purchaser against any sum owing by the purchaser to the Obligor.

The Securitisation Act importantly provides that when a securitisation asset is assigned to a Maltese securitisation vehicle in accordance with the Securitisation Act (including the relevant debtor notification formalities, although not as onerous as the general Civil Code

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requirements), the assignment will be treated as final, absolute and binding on the seller, the purchaser and on all third parties, and the assignment shall not be subject to:

- annulment, rescission, revocation or termination, variation or abatement by any person and for any reason whatsoever;
- any rights of the creditors of the seller for any reason whatsoever; or
- any rights of a liquidator, provisional administrator, receiver, curator, controller, special controller of the seller or other similar officer of the seller for any reason whatsoever.

4.5 Notice Mechanics. If notice is to be delivered to obligors, whether at the time of sale or later, are there any requirements regarding the form the notice must take or how it must be delivered? Is there any time limit beyond which notice is ineffective – for example, can a notice of sale be delivered after the sale, and can notice be delivered after insolvency proceedings have commenced against the obligor or the seller? Does the notice apply only to specific receivables or can it apply to any and all (including future) receivables? Are there any other limitations or considerations?

See question 4.2 with regard to form and delivery requirements of the notice. Notice requirements apply to all types of receivables, including future receivables. The Securitisation Act provides that if the seller becomes insolvent following the date of the assignment to a Maltese securitisation vehicle but prior to the date of the notification, such insolvency shall not have any effect on the assignment and any notification of the assignment (made in accordance with the provisions of the Securitisation Act) shall still be valid and effective.

4.6 Restrictions on Assignment – General Interpretation. Will a restriction in a receivables contract to the effect that "None of the [seller's] rights or obligations under this Agreement may be transferred or assigned without the consent of the [obligor]" be interpreted as prohibiting a transfer of receivables by the seller to the purchaser? Is the result the same if the restriction says "This Agreement may not be transferred or assigned by the [seller] without the consent of the [obligor]" (i.e., the restriction does not refer to rights or obligations)? Is the result the same if the restriction says "The obligations of the [seller] under this Agreement may not be transferred or assigned by the [seller] without the consent of the [obligor]" (i.e., the restriction does not refer to rights)?

This would generally depend on the governing law of the receivables and the instrument of assignment. Such restrictions on assignment would generally be binding under Maltese law. The Securitisation Act, however, provides that an assignment of receivables to a Maltese securitisation vehicle will be final, absolute and binding on the seller, the securitisation vehicle and all third parties and this notwithstanding any underlying statutory or contractual prohibition or restriction (which might arise under the governing law of the receivables) on the seller to assign in whole or in part the securitisation asset to any third party.

4.7 Restrictions on Assignment; Liability to Obligor. If any of the restrictions in question 4.6 are binding, or if the receivables contract explicitly prohibits an assignment of receivables or "seller's rights" under the receivables contract, are such restrictions generally enforceable in your jurisdiction? Are there exceptions to this rule (e.g., for contracts between commercial entities)? If your jurisdiction recognises restrictions on sale or assignment of receivables and the seller nevertheless sells receivables to the purchaser, will either the seller or the purchaser be liable to the obligor for breach of contract or tort, or on any other basis?

This would generally depend on the governing law of the receivables and the instrument of assignment. Such restrictions on assignment would generally be enforceable under Maltese law and the seller may be liable to the Obligor for breach of contract. Notwithstanding any such liability, however, the Securitisation Act provides that an assignment of receivables to a Maltese securitisation vehicle will be final, absolute and binding on the seller, the securitisation vehicle and all third parties and this notwithstanding any underlying statutory or contractual prohibition or restriction (which might arise under the governing law of the receivables) on the seller to assign in whole or in part the securitisation asset to any third party.

4.8 Identification. Must the sale document specifically identify each of the receivables to be sold? If so, what specific information is required (e.g., obligor name, invoice number, invoice date, payment date, etc.)? Do the receivables being sold have to share objective characteristics? Alternatively, if the seller sells *all* of its receivables to the purchaser, is this sufficient identification of receivables? Finally, if the seller sells *all* of its receivables *other than* receivables owing by one or more specifically identified obligors, is this sufficient identification of receivables?

In the case of an assignment that falls within the parameters of 1484A of the Civil Code (see question 4.2):

- classes of existing debts may be assigned provided the Obligor is identified in the contract of assignment; and
- future debts (or classes thereof) may also be assigned provided that the Obligor and the latest date by which the future debts shall come into existence are identified in the contract of assignment.

The Securitisation Act provides that all types of assets and receivables can be securitised whether existing or future, movable or immovable, tangible or intangible. In terms of identification of the receivables being assigned, the Securitisation Act distinguishes between the assignment to a Maltese securitisation vehicle of existing assets and future receivables.

Existing Assets. With regard to existing receivables, the Securitisation Act provides that an assignment of receivables from a seller to a Maltese securitisation vehicle shall be valid and effective if the assignment identifies at least two of the following features of the class of receivables being subject to the assignment (so as to enable any interested party to reasonably determine which receivables are included in the assignment):

- the type of debt or asset or contract giving rise to the debt;
- the class or type of Obligors; and/or
- the repayment period when the debts fall due. It shall not be necessary to specify the name of the Obligor or Obligors, the date or the amount of any particular debt.

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Future receivables. With regard to future receivables the Securitisation Act provides that an assignment of future receivables shall be valid and effective provided that it identifies certain key features of the future receivables (as specified by the Securitisation Act) that will enable any interested party to reasonably determine which receivables are included in the assignment and it shall not be necessary to specify the name of the Obligor or debtors, the date or the amount of any particular debt. The features that must be identified are at least one of:

- the type of debt or asset or contract giving rise to the debt;
- the class or type of debtors; and/or
- the assets (including future assets) which give rise to the receivables.

And at least one of:

- the time period during which the debt may arise; and/or
- the repayment period when the debts may fall due.

4.9 Recharacterisation Risk. If the parties describe their transaction in the relevant documents as an outright sale and explicitly state their intention that it be treated as an outright sale, will this description and statement of intent automatically be respected or is there a risk that the transaction could be characterised by a court as a loan with (or without) security? If recharacterisation risk exists, what characteristics of the transaction might prevent the transfer from being treated as an outright sale? Among other things, to what extent may the seller retain any of the following without jeopardising treatment as an outright sale: (a) credit risk; (b) interest rate risk; (c) control of collections of receivables; (d) a right of repurchase/redemption; (e) a right to the residual profits within the purchaser; or (f) any other term?

The Securitisation Act specifically addresses the requirement of 'true sale' in asset securitisation transactions by providing that a transfer or assignment to a securitisation vehicle will be treated as final, absolute and binding on the originator, the securitisation vehicle and all third parties and will not be subject to recharacterisation for any reason whatsoever, nor will it be subject to the claims of the originator's creditors in insolvency or otherwise. Therefore, there should not be any risk (in principle) of the transfer of title being recharacterised. This is subject only to the exceptions of fraud on the part of the securitisation vehicle or knowledge of pending insolvency proceedings of the originator. There are no specific provisions under Maltese law that prohibit the seller from retaining particular risks relating to the assets, particular rights in respect of the assets or control of collections in respect of the assets. Indeed, the Securitisation Act expressly provides that a Maltese securitisation vehicle may enter into an agreement with the seller to the effect that the seller is given rights by the securitisation vehicle over all or part of the securitisation assets of the securitisation vehicle that may be available after payment of the securitisation creditors (i.e. any repurchase rights or right to residual profits). The Securitisation Act also provides that a Maltese securitisation vehicle may delegate the management responsibility for the day-to-day administration of the vehicle of the assets, including the collection of any claims, to any third party including the seller.

4.10 Continuous Sales of Receivables. Can the seller agree in an enforceable manner to continuous sales of receivables (i.e., sales of receivables as and when they arise)? Would such an agreement survive and continue to transfer receivables to the purchaser following the seller's insolvency?

Yes, the seller can agree in an enforceable manner to continuous sales of receivables, although any assignment of receivables concluded following the seller's insolvency would likely be subject to a 'claw-back' by the seller's liquidator in such a scenario.

4.11 Future Receivables. Can the seller commit in an enforceable manner to sell receivables to the purchaser that come into existence after the date of the receivables purchase agreement (e.g., "future flow" securitisation)? If so, how must the sale of future receivables be structured to be valid and enforceable? Is there a distinction between future receivables that arise prior to *versus* after the seller's insolvency?

The Securitisation Act provides that it shall be lawful for future receivables of a seller, including future claims against future Obligors, to be the subject matter of an assignment in favour of a securitisation vehicle. See question 4.8 above with regard to identification of the receivables being transferred.

An assignment of one or more future receivables is deemed to be effective at the time of the conclusion of the original contract of assignment between the assignor and the assignee, without a new act of transfer being required to assign each such receivable on coming into existence. Moreover, the original notice of assignment duly given in terms of the Securitisation Act (see question 4.2 above) shall be valid and effective in relation to all of the future receivables being assigned and need not be repeated once the receivable comes into existence.

The insolvency of the seller should not have any effect on the validity and effectiveness of a prior assignment (undertaken in accordance with the provisions of the Securitisation Act) to a Maltese securitisation vehicle of future receivables that arise after such insolvency.

In the case of an assignment that falls within the parameters of 1484A of the Civil Code (see question 4.2 above), the assignment of future debts which have not yet come into existence on the date a winding up or bankruptcy order of the seller is made by a Court, may be rescinded by the liquidator or the curator of the seller. The right of rescission of the assignment of future debts shall be conditional on the refund of any consideration paid by the purchaser to the seller for such future debts.

4.12 Related Security. Must any additional formalities be fulfilled in order for the related security to be transferred concurrently with the sale of receivables? If not all related security can be enforceably transferred, what methods are customarily adopted to provide the purchaser the benefits of such related security?

The Civil Code provides that the assignment of a debt includes every security, privilege or hypothec attached to the debt and every other thing accessory to it (but shall not include the fruits accrued due or any rescissory action, unless express mention thereof has been made in the assignment).

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The Securitisation Act further provides that:

- unless the assignment agreement expressly provides otherwise, the assignment of a debt shall also include every suretyship, warranty or indemnity for the payment of the debt;
- the assignment of a debt shall include every suretyship, warranty or indemnity accessory to the debt, and this notwithstanding any contractual prohibition or restriction against such assignment of the debt in the contract of suretyship, guarantee or indemnity; and
- notices of assignment made to the Obligor or class of Obligors in accordance with the Securitisation Act, shall have effect in relation to all persons granting any suretyship, guarantee or indemnity without the need of further notice or other formalities in their regard.

4.13 Set-Off; Liability to Obligor. Assuming that a receivables contract does not contain a provision whereby the obligor waives its right to set-off against amounts it owes to the seller, do the obligor's set-off rights terminate upon its receipt of notice of a sale? At any other time? If a receivables contract does not waive set-off but the obligor's set-off rights are terminated due to notice or some other action, will either the seller or the purchaser be liable to the obligor for damages caused by such termination?

The Obligor's set-off rights against the seller terminate upon the Obligor's receipt of notice of the assignment in accordance with the applicable notification requirements of the Civil Code or the Securitisation Act.

In terms of liability to the Obligor, the Securitisation Act provides that unless the terms of any transfer to a Maltese securitisation vehicle provide otherwise, the Obligor shall have no right or claim against the securitisation vehicle in connection with any obligation relating to the securitisation assets. The Obligor shall continue to enjoy all rights under the assigned contract against the seller who shall remain solely responsible for the performance of all obligations thereunder.

4.14 Profit Extraction. What methods are typically used in your jurisdiction to extract residual profits from the purchaser?

As a result of the 'statutory' bankruptcy remoteness of Maltese securitisation vehicles under the Securitisation Act, there is, strictly speaking, no need for the vehicle to be orphaned, which allows a seller to retain an equity interest in the vehicle and extract profits by simple dividend. Other typically used methods of profit extraction include extraction through servicer and other fees charged to the purchaser or through junior variable rate debt securities issued by the purchaser.

The Securitisation Act provides that it shall be lawful (without affecting the bankruptcy remoteness analysis) for a securitisation vehicle to enter into an agreement with the originator to the effect that the seller is given rights over all or part of the securitisation assets that may remain (as profit) after payment of the securitisation creditors.

5 Security Issues

5.1 Back-up Security. Is it customary in your jurisdiction to take a "back-up" security interest over the seller's ownership interest in the receivables and the related security, in the event that an outright sale is deemed by a court (for whatever reason) not to have occurred and have been perfected (see question 4.9 above)?

It is not customary for the purchaser to take a 'back-up' security interest in addition to its acquisition of ownership in the receivables and the related security interests in respect of those receivables. The statutory true sale provisions of the Securitisation Act significantly reduce any recharacterisation risk as explained in question 4.9 above.

5.2 Seller Security. If it is customary to take back-up security, what are the formalities for the seller granting a security interest in receivables and related security under the laws of your jurisdiction, and for such security interest to be perfected?

It is not customary to take 'back-up' security.

5.3 Purchaser Security. If the purchaser grants security over all of its assets (including purchased receivables) in favour of the providers of its funding, what formalities must the purchaser comply with in your jurisdiction to grant and perfect a security interest in purchased receivables governed by the laws of your jurisdiction and the related security?

Perfection of a security interest would depend on the particular security interest involved and would need to take place in accordance with the governing law of that security interest. While requirements vary from jurisdiction to jurisdiction, perfection typically takes place by registering the security interest in a public register or by notifying or obtaining an acknowledgment of the security interest from the debtor.

A pledge is one of the most common forms of security interest used under Maltese law and is governed by the relevant provisions of the Civil Code. It has a high ranking and is available in relation to a number of movable assets whether tangible or intangible including shares, receivables, bank accounts and various other assets. If the asset being pledged is tangible, the pledge is constituted by the delivery to the creditor of the thing pledged or of the document conferring the exclusive right to the disposal of the thing. If the asset being pledged consists of an intangible asset in relation to which there is no such document conferring the exclusive right to its disposal, the privilege granted to the pledgee shall not arise unless the pledge results from a public deed or a private writing, and either notice of the pledge has been given by a judicial act served on the debtor of the debt or other right or such debtor has in writing acknowledged the pledge. It is market practice to document the pledge by means of a private writing and to obtain the debtor's acknowledgment in writing.

The Securitisation Act provides that under Maltese law, any notices of assignment made to the debtor (or class of debtors) in accordance with the provisions of the Securitisation Act will also be effective in relation to all persons granting any suretyship, guarantee or indemnity without the need for further notice or other

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specific formalities, thereby relaxing the more onerous notification procedures generally required outside of the securitisation context (as it has also done in relation to the assignment of receivables).

In addition to any security granted to them, the holders of securities issued by a securitisation vehicle are granted (pursuant to the Securitisation Act) a statutory special privilege over the securitisation assets. This privilege extends to the proceeds derived from the securitisation assets and to any other assets acquired with those proceeds, and ranks ahead of all other claims at law, except for securitisation creditors who enjoy a prior ranking granted to them with the consent or knowledge of the securities holders.

As transaction security documents are almost always governed by the law of the underlying assets (which is invariably not Maltese law), the intention behind this particular provision of the Securitisation Act was to ensure that all validly given security over securitisation assets would be enforced and given full effect as a first-ranking privilege of the investors under Maltese law, irrespective of the governing law of the security interests.

5.4 Recognition. If the purchaser grants a security interest in receivables governed by the laws of your jurisdiction, and that security interest is valid and perfected under the laws of the purchaser's jurisdiction, will the security be treated as valid and perfected in your jurisdiction or must additional steps be taken in your jurisdiction?

If the receivables are governed by Maltese law then it is always recommended that the security interest over those receivables also be governed by Maltese law, and that the security interest is perfected in accordance with the requirements of Maltese law for that particular security interest.

5.5 Additional Formalities. What additional or different requirements apply to security interests in or connected to insurance policies, promissory notes, mortgage loans, consumer loans or marketable debt securities?

Notwithstanding the provisions of the Civil Code relating to pledge of rights, a pledge of a contract of life insurance and any designation or substitution in the beneficiary designated in such contract (or the assignment of such benefit) shall generally not be valid without the consent in writing of the third party whose life is insured. Moreover, where the policyholder has designated a named beneficiary under a life insurance contract and such beneficiary has accepted the designation, a pledge of the policy may be made only with the prior written consent of the beneficiary (provided that a pledge made without such consent shall be valid but shall be subject to the prior ranking rights of the designated beneficiary).

Pledges of debt securities issued by a Maltese company are subject to specific formalities set out in the Companies Act (Chapter 386 of the Laws of Malta) regarding pledging of securities, which generally requires notification of the company whose securities have been pledged as well as the registration of a notice of pledge delivered to the Registry of Companies, with the pledge to be effective in relation to third parties (i.e. perfected) only after such registration. The perfection requirements vary for listed securities, in respect of which the relevant market would need to be notified (together with a certified copy of the pledge agreement) of the pledge in order for it to be effective in relation to third parties.

5.6 Trusts. Does your jurisdiction recognise trusts? If not, is there a mechanism whereby collections received by the seller in respect of sold receivables can be held or be deemed to be held separate and apart from the seller's own assets (so that they are not part of the seller's insolvency estate) until turned over to the purchaser?

Maltese law recognises trusts under the Trusts and Trustees Act (Chapter 331 Laws of Malta). The Securitisation Act expressly provides that where a Maltese securitisation vehicle has delegated the management responsibility of the assets, including the collection of any claims, to any third party (including the seller):

- such third party (including the seller) shall be obliged to segregate such assets from his own assets (and those of other customers), which segregation shall clearly identify the receivables or securitisation assets which belong to the securitisation vehicle while keeping detailed records of all assets received and disposed of; and
- any assets held by such third party (including the seller) shall be considered as being held on trust by such third party for the benefit of the securitisation vehicle.

5.7 Bank Accounts. Does your jurisdiction recognise escrow accounts? Can security be taken over a bank account located in your jurisdiction? If so, what is the typical method? Would courts in your jurisdiction recognise a foreign law grant of security (for example, an English law debenture) taken over a bank account located in your jurisdiction?

Escrow accounts are used in Malta even though they are not expressly regulated under Maltese law. Security can be taken over bank accounts located in Malta, and this would typically be taken in the form of a pledge. Rights over a bank account may be pledged by means of a public deed or a private writing, and the privilege or preference granted to the pledge at law will arise upon notice by a judicial act served on the bank of the right pledged, or upon the bank acknowledging the pledge in writing. Maltese Courts would generally recognise a foreign security interest taken over a bank account in Malta provided that it is considered as a valid security interest under Maltese law and all of the relevant perfection requirements have complied with Maltese law as the *lex rei sitae*.

For this reason, it is always recommended that a security interest granted over a Maltese bank account is governed by Maltese law.

5.8 Enforcement over Bank Accounts. If security over a bank account is possible and the secured party enforces that security, does the secured party control all cash flowing into the bank account from enforcement forward until the secured party is repaid in full, or are there limitations? If there are limitations, what are they?

The terms of the relevant pledge agreement will regulate whether the secured party controls the cash in the bank account whether prior to or following enforcement. Upon enforcement, the secured party will be entitled to obtain full payment from the cash in the account until the secured debt is repaid in full.

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5.9 Use of Cash Bank Accounts. If security over a bank account is possible, can the owner of the account have access to the funds in the account prior to enforcement without affecting the security?

See question 5.8 above. Access to funds in the account by either party to the pledge will be determined by the terms of the relevant pledge agreement.

6 Insolvency Laws

6.1 Stay of Action. If, after a sale of receivables that is otherwise perfected, the seller becomes subject to an insolvency proceeding, will your jurisdiction's insolvency laws automatically prohibit the purchaser from collecting, transferring or otherwise exercising ownership rights over the purchased receivables (a "stay of action")? If so, what generally is the length of that stay of action? Does the insolvency official have the ability to stay collection and enforcement actions until he determines that the sale is perfected? Would the answer be different if the purchaser is deemed to only be a secured party rather than the owner of the receivables?

One of the unique features of Maltese securitisation vehicles established in terms of the Securitisation Act is that they are bankruptcy remote from the seller by operation of law.

The Securitisation Act expressly provides that (a) no insolvency proceedings taken in relation to the seller under any law will have any effect on the securitisation vehicle, the securitisation assets acquired (or risks assumed) by the securitisation vehicle, or other assets of the securitisation vehicle, including payments due by the underlying debtors, cashflows or other proceeds owing to the vehicle in connection with the securitised assets, and (b) a transfer of assets to the securitisation vehicle shall be treated as final, absolute and binding on the seller, the securitisation vehicle and all third parties and shall not be subject to the rights of the creditors of the seller or any rights of a liquidator, provisional administrator or similar officer of the seller for any reason whatsoever.

Moreover, the Securitisation Act also provides that no court or arbitral tribunal may grant or sanction any moratorium or stay whatsoever in connection with a securitisation vehicle.

6.2 Insolvency Official's Powers. If there is no stay of action, under what circumstances, if any, does the insolvency official have the power to prohibit the purchaser's exercise of its ownership rights over the receivables (by means of injunction, stay order or other action)?

See question 6.1 above.

6.3 Suspect Period (Clawback). Under what facts or circumstances could the insolvency official rescind or reverse transactions that took place during a "suspect" or "preference" period before the commencement of the seller's insolvency proceedings? What are the lengths of the "suspect" or "preference" periods in your jurisdiction for (a) transactions between unrelated parties, and (b) transactions between related parties? If the purchaser is majority-owned or controlled by the seller or an affiliate of the seller, does that render sales by the seller to the purchaser "related party transactions" for purposes of determining the length of the suspect period? If a parent company of the seller guarantee's the performance by the seller of its obligations under contracts with the purchaser, does that render sales by the seller to the purchaser "related party transactions" for purposes of determining the length of the suspect period?

The Securitisation Act provides that an assignment to a Maltese securitisation vehicle will be treated as final, absolute and binding on the seller, the purchaser and on all third parties, and the assignment shall not be subject to:

- annulment, rescission, revocation or termination, variation or abatement by any person and for any reason whatsoever;
- any rights of the creditors of the seller for any reason whatsoever; or
- any rights of a liquidator, provisional administrator, receiver, curator, controller, special controller of the seller or other similar officer of the seller for any reason whatsoever.

The Securitisation Act, however, provides, without specifying any particular suspect periods, that the only exception to the above rule is where there is fraud on the part of the securitisation vehicle or in respect of an assignment entered into at a time at which the securitisation vehicle knew, or ought to have known that an application for the dissolution and winding up of the seller by reason of insolvency was pending, or that the seller had taken formal steps under applicable law to bring about its dissolution and winding up by reason of insolvency.

This analysis does not differ in respect of related party transactions or unrelated party transactions.

6.4 Substantive Consolidation. Under what facts or circumstances, if any, could the insolvency official consolidate the assets and liabilities of the purchaser with those of the seller or its affiliates in the insolvency proceeding? If the purchaser is owned by the seller or by an affiliate of the seller, does that affect the consolidation analysis?

See question 6.1 above. A Maltese securitisation vehicle is bankruptcy remote from a seller by operation of law. As a result of the 'statutory' bankruptcy remoteness of Maltese securitisation vehicles under the Securitisation Act, there is, strictly speaking, no need for the vehicle to be orphaned in order to avoid substantive consolidation concerns, and this even allows a seller to retain an equity interest in the vehicle.

Generally, the concept of substantive consolidation is not recognised under Maltese law. Maltese company law, based primarily on English company law (and with the Maltese courts looking to English law

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as a persuasive authority), respects the doctrine of separate legal personality. This will only be disregarded (and the corporate veil pierced) in very limited circumstances, which generally relate to the use of a structure for fraudulent or improper purposes.

Although from a purely Maltese perspective one need look no further than the Securitisation Act to determine the remoteness of the securitisation vehicle from the insolvency of the seller, additional steps are often taken to further alleviate investor concerns, and meet rating agencies' strict legal criteria for special purpose entities.

These include the orphaning of the securitisation vehicle and generally ensuring separateness and independence of the vehicle from the seller in its activities, processes and management.

6.5 Effect of Insolvency on Receivables Sales. If insolvency proceedings are commenced against the seller in your jurisdiction, what effect do those proceedings have on (a) sales of receivables that would otherwise occur after the commencement of such proceedings, or (b) on sales of receivables that only come into existence after the commencement of such proceedings?

The Securitisation Act provides that an assignment of one or more future receivables is deemed to be effective at the time of the conclusion of the original contract of assignment between the assignor and the assignee, without a new act of transfer being required to assign each such receivable on coming into existence. Accordingly (subject to the exceptions outlined in question 6.3 above), the subsequent insolvency of the seller should not have any effect on the validity and effectiveness of a prior assignment (undertaken in accordance with the provisions of the Securitisation Act) to a Maltese securitisation vehicle of future receivables that arises after such insolvency. If a sale of receivables does not relate to an already perfected assignment of future receivables, and such sale occurs after the commencement of insolvency proceedings, it would likely be treated as a separate assignment and possibly subject to a 'claw-back' by the seller's liquidator if the securitisation vehicle is found to have had actual or constructive knowledge of such insolvency proceedings at the time of the assignment (see question 6.3 above).

6.6 Effect of Limited Recourse Provisions. If a debtor's contract contains a limited recourse provision (see question 7.3 below), can the debtor nevertheless be declared insolvent on the grounds that it cannot pay its debts as they become due?

The Securitisation Act expressly provides that any contract entered into in connection with a securitisation transaction shall be valid and enforceable in accordance with its terms, and where the parties agree in writing as to the effects that will arise on the occurrence of a specified event, it shall not be necessary for either party to obtain any court judgment or declaration confirming that the specified event has occurred or otherwise. This provision of the Securitisation Act will be respected by the Maltese courts, thereby confirming that limited recourse clauses typically included in transaction documents entered into between securitisation vehicles and securitisation creditors will be given effect to and enforced. On this basis, provided the limited recourse clause contains appropriate wording limiting a creditor's claims (and thus the debtor's obligations) to the assets of the securitisation vehicle, the vehicle's debts should technically be reduced to the extent of those assets and the vehicle should therefore never be in a position where it cannot pay its debts as they become due.

7 Special Rules

7.1 Securitisation Law. Is there a special securitisation law (and/or special provisions in other laws) in your jurisdiction establishing a legal framework for securitisation transactions? If so, what are the basics? Is there a regulatory authority responsible for regulating securitisation transactions in your jurisdiction?

The legal framework for securitisation in Malta is set out in the:

- Securitisation Act, which provides for the establishment of securitisation vehicles for the purpose of undertaking securitisation transactions. The Securitisation Act is broad in scope and allows for asset (true sale) securitisation, synthetic securitisation (including the securitisation of insurance risk) and whole business securitisation structures (through the granting of a secured loan or other secured facility from the securitisation vehicle to the seller);
- Securitisation Transactions (Deductions) Rules, Subsidiary Legislation 123.128 of the Laws of Malta (the "**Securitisation Tax Rules**"), which set out the special tax regime for Maltese securitisation vehicles;
- Securitisation Cell Companies Regulations, Subsidiary Legislation 386.16 of the Laws of Malta (the "**SCC Regulations**"), which provide for the establishment of securitisation cell companies ("**SCCs**") that can undertake securitisation transactions through segregated cells within an SCC; and
- Reinsurance Special Purpose Vehicle Regulations, Subsidiary Legislation 403.19 of the Laws of Malta (the "**RSPV Regulations**"), which allow securitisation vehicles to be established as reinsurance special purpose vehicles ("**RSPVs**") for the purpose of assuming insurance risk and issuing insurance-linked securities, subject to the prior authorisation of the MFSA. RSPVs can also be established as SCCs and are therefore subject to both the SCC Regulations and the RSPV Regulations.

The regulatory authority responsible for the regulation of securitisation in Malta is the MFSA, although it should be noted that a securitisation vehicle (or an SCC) requires authorisation by the MFSA only if it is established for the purpose of assuming insurance risk (i.e. RSPVs) or if it issues financial instruments to the public on a continuous basis.

7.2 Securitisation Entities. Does your jurisdiction have laws specifically providing for establishment of special purpose entities for securitisation? If so, what does the law provide as to: (a) requirements for establishment and management of such an entity; (b) legal attributes and benefits of the entity; and (c) any specific requirements as to the status of directors or shareholders?

(a) The Securitisation Act specifically provides for the establishment of special purpose entities for securitisation (see question 7.1 above).

Securitisation vehicles established in Malta under the Securitisation Act can be a company, partnership, trust or any other legal structure that the MFSA may expressly permit. Securitisation vehicles are typically established as limited liability companies and can be incorporated in Malta within a day or two of submission of its organisational documents to the Registry of Companies. The objects of a securitisation must be expressly limited to such matters that are necessary to carry out all or any transactions intended or required to implement or participate in a securitisation transaction and all related and ancillary acts.

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The Securitisation Act does not set out any requirements for the management of securitisation vehicles (with the exception of certain requirements applicable to public securitisation vehicles – see question 8.1 below). From a corporate law perspective, a securitisation vehicle established as a private limited liability company must have at least one director, while a securitisation vehicle established as a public limited liability company must have at least two directors. A securitisation vehicle is expressly permitted by the Securitisation Act to delegate the management responsibility for the day-to-day administration of the vehicle of the assets, including the collection of any claims, to any third party including the seller.

(b) The Securitisation Act provides an attractive legal framework for securitisation transactions and the establishment of the special purpose entity (purchaser), offering a unique combination of benefits for investors and originators. As described throughout this questionnaire, the Act provides statutory solutions and greater certainty of outcomes for many of the legal challenges that investors and credit rating agencies are typically concerned with, including true sale, bankruptcy remoteness and the privileges of securitisation creditors over the vehicle's assets. These structural enhancements that are inherent to Maltese securitisation vehicles under the Act allow for competitive borrowing costs relative to any recognised issuer jurisdiction.

Moreover, the SCC option allows for a single legal entity that can create multiple segregated cells for the purpose of undertaking securitisation transactions (i.e. each cell acting as a distinct purchaser in the particular transaction for which it has been established). The SCC structure, which offers lower costs and quicker set-up time for each transaction, is ideal for asset-backed securities offering programmes or asset-based financing (or other) platforms, with many arrangers now offering these options to originators.

(c) There are no specific requirements as to the status of directors or shareholders.

7.3 Location and form of Securitisation Entities. Is it typical to establish the special purpose entity in your jurisdiction or offshore? If in your jurisdiction, what are the advantages to locating the special purpose entity in your jurisdiction? If offshore, where are special purpose entities typically located for securitisations in your jurisdiction? What are the forms that the special purpose entity would normally take in your jurisdiction and how would such entity usually be owned?

Special purpose entities are typically established in Malta as securitisation vehicles subject to the provisions of the Securitisation Act. The Securitisation Act also contemplates the possibility of foreign legal structures being established as securitisation vehicles that are subject to the Securitisation Act, provided that these legal structures are established in a jurisdiction recognised by the MFSA.

To date all securitisation vehicles established under the Securitisation Act have been incorporated in Malta and the MFSA has not yet expressly recognised any particular jurisdictions in this regard. Also, the potential benefits of having a foreign vehicle established pursuant to the Securitisation Act have yet to be identified.

The main reason for selecting Malta as the jurisdiction for the establishment of the issuer SPV in securitisation transactions is the attractive legal framework and unique combination of benefits that Maltese securitisation vehicles provide to investors and originators looking to secure financing from those investors; benefits include statutory bankruptcy remoteness and true sale.

Securitisation vehicles established in Malta pursuant to the Securitisation Act can take the form of a company, partnership, trust or any other legal structure that the MFSA may expressly permit to be used for a securitisation transaction. However, securitisation vehicles are typically established as limited liability companies.

Maltese securitisation vehicles are typically 'orphaned' from the originator (for bankruptcy remoteness purposes) by establishing a Maltese purpose foundation (with no beneficiaries or owners) for the sole purpose of owning either all of the voting share capital of the vehicle or, alternatively, a 'golden' share with veto rights over key corporate actions (such as amendment of the organisational documents of the vehicle or the commencement of winding up or insolvency proceedings). However, Maltese securitisation vehicles do not, strictly speaking, need to be orphaned in this manner because the Securitisation Act provides a statutory confirmation that no insolvency proceedings relating to the originator will have any effect on a Maltese securitisation vehicle or its assets (once these have been transferred to the vehicle by the originator).

7.4 Limited-Recourse Clause. Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) limiting the recourse of parties to that agreement to the available assets of the relevant debtor, and providing that to the extent of any shortfall the debt of the relevant debtor is extinguished?

The Securitisation Act expressly provides that any contract entered into in connection with a securitisation transaction shall be valid and enforceable in accordance with its terms, and where the parties agree in writing as to the effects that will arise in the occurrence of a specified event, it shall not be necessary for either party to obtain any court judgment or declaration confirming that the specified event has occurred or otherwise. This provision of the Securitisation Act will be respected by the Maltese courts, thereby confirming that limited recourse clauses typically included in transaction documents entered into between securitisation vehicles and securitisation creditors will be given effect to and enforced.

7.5 Non-Petition Clause. Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) prohibiting the parties from: (a) taking legal action against the purchaser or another person; or (b) commencing an insolvency proceeding against the purchaser or another person?

The Securitisation Act provides that:

- securitisation vehicles can enter into agreements with provisions whereby securitisation creditors or shareholders accept to restrict or waive their rights to commence any form of any dissolution and winding up proceedings, company recovery procedure, company reconstruction or any proceedings affecting creditors' rights generally in respect of the securitisation vehicle;
- the constitutive documents of the securitisation vehicle can give any securitisation creditor or class of them (including, for example, the trustee on behalf of investors), to the exclusion of all other persons, the right to demand or place the securitisation vehicle under any dissolution and winding up proceedings, company recovery procedure, company reconstruction or any proceedings affecting creditors' rights generally; and
- any contract entered into in connection with a securitisation transaction shall be valid and enforceable in accordance with

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its terms, and where the parties agree in writing as to the effects that will arise on the occurrence of a specified event, it shall not be necessary for either party to obtain any court judgment or declaration confirming that the specified event has occurred or otherwise.

Accordingly, market standard non-petition clauses included in transaction documents should be given effect to and enforced by the Maltese courts in accordance with the Securitisation Act.

7.6 Priority of Payments "Waterfall". Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) distributing payments to parties in a certain order specified in the contract?

The Civil Code importantly provides that it shall be lawful for a creditor to subordinate, postpone, waive or otherwise modify his existing or future rights of payment, enforcement, ranking and other similar existing or future rights in favour of another person. This would generally be the case even if the relevant agreement is governed by foreign law. The Securitisation Act also recognises the right of various securitisation creditors to contractually regulate their ranking between themselves (including in the event of insolvency) in relation to the securitisation assets, ensuring that any subordination of claims between the various securitisation creditors will be respected.

7.7 Independent Director. Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) or a provision in a party's organisational documents prohibiting the directors from taking specified actions (including commencing an insolvency proceeding) without the affirmative vote of an independent director?

Generally speaking, a Maltese court will give effect to a provision included in the transaction documents or in the company's organisational documents requiring the consent of an independent director for the taking of certain specified actions. See also question 7.4 above.

7.8 Location of Purchaser. Is it typical to establish the purchaser in your jurisdiction or offshore? If in your jurisdiction, what are the advantages to locating the purchaser in your jurisdiction? If offshore, where are purchasers typically located for securitisations in your jurisdiction?

Securitisation transactions undertaken in Malta generally relate to the securitisation of foreign assets/receivables with all of the parties being located outside of Malta (and the majority of the transaction documents governed by foreign law) other than the purchaser, which would be invariably a Maltese securitisation vehicle subject to the provisions of the Securitisation Act. The advantages of establishing the purchaser as a Maltese securitisation vehicle are generally set out in question 7.2 above and elsewhere in this chapter.

8 Regulatory Issues

8.1 Required Authorisations, etc. Assuming that the purchaser does no other business in your jurisdiction, will its purchase and ownership or its collection and enforcement of receivables result in its being required to qualify to do business or to obtain any licence or its being subject to regulation as a financial institution in your jurisdiction? Does the answer to the preceding question change if the purchaser does business with more than one seller in your jurisdiction?

The Securitisation Act distinguishes between public securitisation vehicles and those securitisation vehicles that are not public securitisation vehicles (generally referred to as private securitisation vehicles). A public securitisation vehicle is a securitisation vehicle that issues or intends to issue financial instruments to the public on a continuous basis. Public securitisation vehicles are required to be licensed by the MFSA prior to issuing financial instruments to the public. As indicated above, securitisation vehicles established as RSPVs are also subject to the prior authorisation of the MFSA.

A private securitisation vehicle is, by implication, a securitisation vehicle that does not issue or intend to issue financial instruments to the public on a continuous basis. Private securitisation vehicles are not required to be licensed by the MFSA but are required to notify the MFSA of their intention to enter into one or more securitisation transactions prior to commencing business, which notification must include certain basic corporate information of the securitisation vehicle and details of the securitisation transaction.

Other than the licensing requirement for public securitisation vehicles and RSPVs, Maltese securitisation vehicles are specifically exempt from licensing or authorisation requirements (in Malta) of any kind for the sort of activities in which they might engage – activities that would normally require licensing if undertaken by entities that are not established as securitisation vehicles (under the Investment Services Act, Banking Act or Financial Institutions Act, for example). Of particular relevance to transactions with a managed or dynamic portfolio of assets, the Securitisation Act provides that Maltese securitisation vehicles are not to be considered collective investment schemes (including in the form of an 'alternative investment fund' under the AIFMD), thereby exempting them from the local regulatory regime applicable to collective investment schemes (including the regime for alternative investment funds).

It should be noted that securitisation vehicles (whether subject to authorisation or mere notification requirements) qualify as 'financial vehicle corporations' under Regulation (EU) 1075/2013 of the European Central Bank and are accordingly required to inform the Central Bank of Malta of its existence within one week from the date on which it has taken up business. Thereafter, a securitisation vehicle is required to submit quarterly statistical reports on its assets and liabilities to the Central Bank of Malta.

8.2 Servicing. Does the seller require any licences, etc., in order to continue to enforce and collect receivables following their sale to the purchaser, including to appear before a court? Does a third-party replacement servicer require any licences, etc., in order to enforce and collect sold receivables?

Outside of any licensing requirements in its own jurisdiction, a seller of receivables to a Maltese securitisation vehicle is not required to be licensed in Malta to act as servicer and collection agent to the securitisation vehicle, nor is a third-party replacement servicer required to be licensed in Malta to provide such services.

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8.3 Data Protection. Does your jurisdiction have laws restricting the use or dissemination of data about or provided by obligors? If so, do these laws apply only to consumer obligors or also to enterprises?

The Securitisation Act provides that any data or information transferred within the context of a securitisation transaction shall be transferable without any restriction or limitation and that, for the purposes of the Data Protection Act (Chapter 440 of the Laws of Malta), any transfer of personal data shall be deemed to be for a purpose that concerns a legitimate interest of the transferor and transferee of such data and, accordingly, a permissible transfer of personal data.

8.4 Consumer Protection. If the obligors are consumers, will the purchaser (including a bank acting as purchaser) be required to comply with any consumer protection law of your jurisdiction? Briefly, what is required?

The underlying receivables contract (if governed by Maltese law) would be subject to certain consumer protections. See question 1.2 above. However, the Securitisation Act provides that unless the terms of any transfer to a Maltese securitisation vehicle provide otherwise, the Obligor shall have no right or claim against the securitisation vehicle in connection with any obligation relating to the securitisation assets (which would include any consumer protection obligations arising under the receivables contract). The Obligor shall continue to enjoy all rights under the assigned contract against the seller who shall remain solely responsible for the performance of all obligations thereunder.

8.5 Currency Restrictions. Does your jurisdiction have laws restricting the exchange of your jurisdiction's currency for other currencies or the making of payments in your jurisdiction's currency to persons outside the country?

There are no currency restrictions in Malta.

8.6 Risk Retention. Does your jurisdiction have laws or regulations relating to "risk retention"? How are securitisation transactions in your jurisdiction usually structured to satisfy those risk retention requirements?

The Regulation (EU) 575/2013 on prudential requirements for credit institutions and investment firms (in relation to securitisation positions) is applicable in Malta. In article 405 of the same Regulation, it is provided that a credit institution or investment firm can only be exposed to the credit risk of a securitisation position if originator, sponsor or original lender has explicitly disclosed that it will retain, on an ongoing basis, a material net economic interest in the securitisation position of at least 5%. Similar restrictions regarding exposure to securitisation positions also apply to alternative investment fund managers and insurers that are subject to the EU Alternative Investment Fund Managers Directive (Directive 2011/61/EU) or the EU Solvency II Directive (Directive 2009/138/EC), respectively. This has not really had an effect on the securitisation market in Malta.

See also question 8.7 below in relation to recent European regulatory developments, which do not affect the method or quantum of risk retention but which will, once they are applicable, create a direct obligation on originators to retain risk. This is currently (until 1 January 2019) an indirect requirement on EU institutional investors (pursuant to the aforementioned EU Regulation and Directives) to invest in transactions only where such risk is retained by the originator.

8.7 Regulatory Developments. Have there been any regulatory developments in your jurisdiction which are likely to have a material impact on securitisation transactions in your jurisdiction?

A fundamental part of the European Commission's Capital Markets Union initiative, Regulation (EU) 2017/2402 laying down a general framework for securitisation and creating a specific framework for simple, transparent and standardised securitisation (the Securitisation Regulation), and Regulation (EU) 2017/2401 amending Regulation (EU) 575/2013 on prudential requirements for credit institutions and investment firms (in relation to securitisation positions), were published in the Official Journal of the European Union on the 12 December 2017. The Regulations came into force on 1 January 2018, although the date of application of the new Regulations will be 1 January 2019, to allow European Supervisory Authorities EBA and ESMA the necessary time to develop the regulatory technical standards required to implement the Regulations. The new STR/CRR legislative package was agreed upon following lengthy negotiations by the Maltese EU Council presidency team (co-chaired by the author of this article) during the first half of 2017. These regulatory developments are not expected to have a material impact on securitisation transactions undertaken in Malta but can generally be viewed as complementary to Malta's special purpose vehicle regime – the Securitisation Act – and the various statutory enhancements that it provides to Maltese securitisation vehicles.

9 Taxation

9.1 Withholding Taxes. Will any part of payments on receivables by the obligors to the seller or the purchaser be subject to withholding taxes in your jurisdiction? Does the answer depend on the nature of the receivables, whether they bear interest, their term to maturity, or where the seller or the purchaser is located? In the case of a sale of trade receivables at a discount, is there a risk that the discount will be recharacterised in whole or in part as interest? In the case of a sale of trade receivables where a portion of the purchase price is payable upon collection of the receivable, is there a risk that the deferred purchase price will be recharacterised in whole or in part as interest? If withholding taxes might apply, what are the typical methods for eliminating or reducing withholding taxes?

There are many variables that need to be taken into consideration for the purposes of assessing whether any Maltese withholding taxes should be applicable in respect of payments made by the Maltese securitisation vehicle.

In general, Maltese income tax laws impose an obligation to withhold tax in case of payments to non-residents where the said non-resident is liable to tax in Malta in respect of said income. A non-resident person would, in general, be subject to Maltese income tax if the income has a Maltese source and, either there is no specific exemption applicable in terms of Maltese domestic law, or Malta's taxing rights are not excluded in terms of any applicable double tax treaty.

The Securitisation Tax Rules provide specifically for certain incomes to be taxable at the level of the seller (the originator), mainly:

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- sums payable to the seller (originator) for the transfer of securitisation assets to the securitisation vehicle; and
- income of the seller (the originator) arising as a result of a further deduction allowed to the securitisation vehicle to wipe out its profits.

However, the Securitisation Tax Rules provide that such income is not considered to arise in Malta (and hence taxable in Malta) if the control and management of the business of the seller (the originator) is not exercised in Malta.

A specific exemption applies in terms of Maltese income tax laws in respect of interest paid to non-residents provided that a number of straightforward conditions are satisfied mainly that:

- the person is not carrying on any trade or business in Malta through a permanent establishment herein; and
- the person as the beneficial owner of the interest is not owned and controlled by, directly or indirectly, nor acts on behalf of an individual or individuals who are ordinarily resident and domiciled in Malta.

9.2 Seller Tax Accounting. Does your jurisdiction require that a specific accounting policy is adopted for tax purposes by the seller or purchaser in the context of a securitisation?

From a timing perspective, the general principle under Maltese law is that receivability without receipt should not result in taxation. However, in case of persons engaged in trade or business the Inland Revenue allows the tax profits to be based on the accounting profits provided that this is adopted on a consistent basis.

Purchaser (securitisation vehicle)

However, the Securitisation Tax Rules specifically provide that for the purposes of determining the total income of a Maltese securitisation vehicle, income or gains shall be deemed to arise or become realised during the year in which such income or gains fall to be recognised for accounting purposes. Tax allowable deductions should also be taken in the year during which they are recognised for accounting purposes.

Thus, if the securitisation vehicle is accounting for its income on an accruals basis of accounting, the tax will be computed on such income and the same applies for deductions.

Seller (originator of receivables)

The Securitisation Tax Rules allows the securitisation vehicle, *inter alia*, the right to deduct:

- sums payable to the seller (originator) for the transfer of securitisation assets to the securitisation vehicle; and
- a further deduction to wipe out all the chargeable income of the securitisation vehicle. Such further deduction is only allowed provided the seller (originator) gives his irrevocable consent for such deduction.

These deductible expenses are deemed to be income for the seller (the originator).

The Securitisation Tax Rules provide that in case of sums payable to the seller for the transfer of a securitisation asset, such income shall be deemed to arise for the seller (originator) in the year in which the securitisation asset was transferred.

In respect of income of the seller (the originator) arising as a result of the further deduction allowed to the securitisation vehicle to wipe out its profits, the Securitisation Tax Rules provide that such income is deemed to arise for the seller (the originator) in the year in which the deduction is claimed by the securitisation vehicle.

9.3 Stamp Duty, etc. Does your jurisdiction impose stamp duty or other transfer or documentary taxes on sales of receivables?

Stamp duty is levied in Malta on documents evidencing transfers of immovable property, marketable securities (defined as holding of share capital in any company and any document representing the same) or an interest in a partnership as well as on certain specified documents such as policies of insurance. There should be no stamp duty in connection with the sale of the receivables.

9.4 Value Added Taxes. Does your jurisdiction impose value added tax, sales tax or other similar taxes on sales of goods or services, on sales of receivables or on fees for collection agent services?

VAT is payable on every supply of goods or of services where for Malta VAT purposes such supply is deemed to take place in Malta and an exemption from Malta VAT (either in terms of exempt without credit or exempt with credit) does not apply. The standard Malta VAT rate is 18%.

In terms of Value Added Tax Act (Chapter 406 of the Laws of Malta), the following services are exempt without credit services:

- the granting and the negotiation of credit and the management of credit by the person granting it;
- the negotiation of or any dealings in credit guarantees or any other security for money and the management of credit guarantees by the person who is granting the credit; and
- transactions, including negotiations, concerning deposit and current accounts, payments, transfers, debts, cheques and other negotiable instruments, but excluding debt collection and factoring.

The supply of services consisting of the management of any investment scheme, provided that these services are limited to those activities that are specific to and essential for the core activity of the scheme. The term "investment scheme" is defined as including a securitisation vehicle as defined under the Securitisation Act.

9.5 Purchaser Liability. If the seller is required to pay value-added tax, stamp duty or other taxes upon the sale of receivables (or on the sale of goods or services that give rise to the receivables) and the seller does not pay, then will the taxing authority be able to make claims for the unpaid tax against the purchaser or against the sold receivables or collections?

See question 9.3 above with regard to stamp duty in respect of the sale of receivables.

With regard to VAT, if the liability to account for VAT rests with the seller, the Maltese tax authorities should not be able to enforce any claims for unpaid tax against the purchaser or sold receivables or collections.

9.6 Doing Business. Assuming that the purchaser conducts no other business in your jurisdiction, would the purchaser's purchase of the receivables, its appointment of the seller as its servicer and collection agent, or its enforcement of the receivables against the obligors, make it liable to tax in your jurisdiction?

A non-Maltese purchaser's purchase of receivables or enforcement

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of the receivables against obligors will generally not make the purchaser liable to tax in Malta provided that:

- the purchaser is not resident in Malta;
- the income it is deriving is of a trading nature;
- all trade-earning activities are carried out outside of Malta; and
- it has no permanent establishment in Malta (whether through a physical branch or dependent agent).

9.7 Taxable Income. If a purchaser located in your jurisdiction receives debt relief as the result of a limited recourse clause (see question 7.3 above), is that debt relief liable to tax in your jurisdiction?

The limited recourse clause should not be deemed to give rise to debt relief for the purchaser, as from a contractual perspective the liability of the purchaser should be always limited by such a clause. The obligations themselves would be reduced as a result of the limited recourse clause and there would therefore be no relief or forgiveness of any obligations owed.

However, it is worth pointing out that the Securitisation Tax Rules enable securitisation vehicles established in Malta to eliminate tax leakage and achieve tax neutrality in Malta in respect of the securitisation transactions for which they are established.

Indeed, if the securitisation vehicle has any remaining income after deducting all allowable expenses, it may opt to claim a further deduction of an amount which is equal to the said remaining income to wipe out its profits. In this manner, the securitisation vehicle will end up with no chargeable income.

The residual profit deduction can only be claimed by the securitisation vehicle if the seller (the originator) has given its irrevocable written consent to the vehicle to do so.

As explained above, consent of the originator is required as the amount of the residual profit deduction will be deemed to be income of the originator for the purposes of Maltese income tax. Nevertheless, this income shall only be deemed to arise in Malta (and therefore taxable in Malta) if the control and management of the originator's business is exercised in Malta. Therefore, even if an originator consents to a securitisation vehicle claiming the residual profit deduction, there should be no Maltese tax liability for originators that are not managed and controlled in Malta.

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Netherlands

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1 Receivables Contracts

1.1 Formalities. In order to create an enforceable debt obligation of the obligor to the seller: (a) is it necessary that the sales of goods or services are evidenced by a formal receivables contract; (b) are invoices alone sufficient; and (c) can a binding contract arise as a result of the behaviour of the parties?

An enforceable debt obligation of an obligor to a seller does not need to be evidenced by a formal receivables contract. An enforceable debt obligation can be evidenced from other documentary sources such as an invoice issued by a seller for the supply of goods and/or services to an obligor, but without the need for a formal contract of sale and/or supply.

A binding receivables "contract" may exist solely as a result of the behaviour of the parties. A written contract is not necessary. However, in practice the vast majority of debt obligations governed by Dutch law are recorded in documents since the underlying receivables need to be "sufficiently identifiable" (see question 4.8) in order to transfer or create security over them. In addition, for evidentiary purposes a written record of the contract constituting the receivable is desirable for all parties.

1.2 Consumer Protections. Do your jurisdiction's laws: (a) limit rates of interest on consumer credit, loans or other kinds of receivables; (b) provide a statutory right to interest on late payments; (c) permit consumers to cancel receivables for a specified period of time; or (d) provide other noteworthy rights to consumers with respect to receivables owing by them?

Dutch law restricts the maximum rate of interest chargeable to consumers. For general consumer loans, these rules are laid down in the Dutch Civil Code (*Burgerlijk Wetboek*) (Section 7:76 and 7:77) and the Decree on Credit Compensation (*Besluit Kredietvergoeding*), which regulate the offering of the most common types of consumer credit to consumers. These rules, however, do not apply to mortgage loans under which there are in principle no limits on the rate of interest that may be charged to customers. However, in practice there are a number of rules and regulations as a result of which limitations do exist (please see below).

As a general proposition, interest rates that are judged to be unreasonably high may contravene Dutch law principles of "fairness" and "morality". If an interest rate is judged to be in breach of this principle of "fairness" and "morality", the interest rate will not be enforceable against a consumer. In addition, unreasonably high rates imposed on a consumer may contravene the Dutch law principle of "reasonableness and fairness". This is especially the case if there is insufficient clarity on the basis of which a rate is calculated or subsequently reset. Note that subject to the above, compound interest charged under consumer loans is permitted under Dutch law.

The principle of "reasonableness and fairness" mentioned above is a Dutch legal concept applicable to many aspects of Dutch law. In some respects it can create a degree of uncertainty in transactions, as the principle has the effect of giving a Dutch court the ability to clarify the effect of any right or obligation in favour of any party to a contract, however it is expressed on the basis that it must be exercised in way that is reasonable and fair. A Dutch court will take into account the facts and circumstances of the contract and wider transaction, when seeking to invoke the doctrine. These include the nature and content of the contract and the relationship between the parties. In respect of the latter, where the relationship is between a professional party (such as a financial institution) and a consumer, a court may be more likely to construe a provision in favour of the consumer on the basis of any unbalanced bargaining position. However, again, the application of the doctrine is fact-specific.

As to interest rate rules applicable to mortgage loans, which constitute an important product in the context of Dutch securitisation transactions, the Code of Conduct Mortgage Loans (*Gedragscode Hypothecaire Financieringen*) issued by the Dutch Bankers Association (*Nederlandse vereniging van banken*) provides rules to calculate the "effective rate of interest". In addition, the Dutch Financial Markets Authority (*Autoriteit Financiële Markten*) publishes the average interest rates for various mortgage loan products on its website on a quarterly basis. These disclosures provide Dutch mortgage originators with guidance on the interest rate that could be used for their mortgage loan products. Although not determinative, such disclosures will influence whether an interest rate is "reasonable and fair". Dutch courts have also held that borrowers are entitled to expect that the interest rate that a lender charges should be consistent with the general rates of interest being used by other participants for comparable products. Furthermore, Dutch regulations provide that, if an originator offers a mortgage loan with a floating interest rate, it must inform the consumer about the component (or components) of such interest rate, state whether the components are fixed or floating and provide information on the financial risks involved (e.g., if a rate switches from a fixed to a floating rate). Finally, Dutch regulations provide that, if a mortgage loan has been granted with a floating interest rate, the originator must inform the consumer of any change in the interest rate (and

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any resets) during the term of the mortgage loan. At the same time, the originator must inform the consumer about any consequential change to the annual percentage rate (*jaarlijks kostenpercentage*) and the component or components (e.g., rate and/or margin) that have changed the interest rate.

On 4 February 2014 the European Parliament and Council adopted Directive 2014/17/EU on credit agreements for consumers relating to residential immovable property, which also amends Directives 2008/48/EC and 2013/36/EU and Regulation (EU) No 1093/2010 (the ***Directive***). The Directive provides a comprehensive framework for advising on and the originating of mortgage loans to consumers. The main topics included in the Directive can be categorised as follows: (i) prudential rules; (ii) information obligations (including pre-contractual information); (iii) mortgage loan products and characteristics; (iv) advising on mortgage loans; and (v) mortgage loan origination. The provisions of the Directive needed to be converted into national legislation by 21 March 2016. The Netherlands implemented the Directive into national legislation on 14 July 2016 by effecting changes to both the Dutch Civil Code (*Burgerlijk Wetboek*) and the Dutch Financial Supervision Act (*Wet op het financieel toezicht*). It should be noted that the Directive (and the corresponding legislation in the Netherlands) only aims to cover mortgage loans that are originated after 21 March 2016.

Dutch legal commentators have acknowledged that the Directive will lead to certain changes to the Dutch mortgage market. However, the impact should not be substantial, since the Dutch mortgage market is already heavily regulated with a number of rules and regulations as well as self-regulating procedures. In addition, in practice many requirements of the Directive are already complied with by Dutch mortgage originators due to their compliance with the Code of Conduct Mortgage Loans (*Gedragscode Hypothecaire Financieringen*).

The implementation of the Directive into national legislation has not led to a repeal of the Temporary Regulation Mortgage Credit (*Tijdelijke regeling hypothecair krediet*) which, amongst others, purports to limit loan-to-value ratios. As an example, the maximum loan-to-value ratio as per 1 January 2018 is 100 per cent.

Section 6:119 or, as applicable, Section 6:119a of the Dutch Civil Code (*Burgerlijk Wetboek*), provides that statutory interest is payable on the unpaid part of a debt that is due and payable. Section 6:119a of the Dutch Civil Code (*Burgerlijk Wetboek*) applies to agreements between companies and/or persons acting in the course of their profession or business and which relate to commercial agreements. The statutory rate of interest is determined by a Dutch governmental decree. A creditor is entitled to the statutory interest, unless the parties agree on a higher interest rate. Note, however, the comment above regarding the potential non-enforceability of unreasonably high rates of interest.

As a general proposition, the Dutch Civil Code (*Burgerlijk Wetboek*) provides that a consumer has the right to cancel a contract without penalty or giving any reasons, during a period of 14 calendar days of entering into such contract. This period starts on (i) the day on which the contract was made or goods were received, or (ii) the day on which the consumer received the information that the lender was required to supply the consumer.

Note that if a consumer has a credit contract for an indefinite period of time, they have the right to terminate the contract free of charge and repay the outstanding amounts at any time. If, however, a notice period has been included, this notice period may not be longer than one month.

In addition, Dutch law provides a broad range of provisions protecting the interests of consumers. The provisions of the Dutch Consumer Credit Act (*Wet op het consumentenkrediet*) have as per 1 January 2017 largely been transposed to the Dutch Civil Code (*Burgerlijk Wetboek*) and have also been modernised. The Dutch Civil Code (*Burgerlijk Wetboek*) now provides for an extensive framework on consumer credit, and extensive rules on the information lenders must provide to consumers before entering into the contract and as to the specific contents of the contract. It also provides for a "black and grey" list of provisions that, if included in the general conditions applicable to a consumer credit contract, are considered to be (or deemed to be) unreasonably onerous towards a consumer and which will be void against such consumer. Each list contains specific contractual terms, including contractual provisions that purport to exclude a consumer's right to set off any amount it owes to the lender against any amount such consumer is owed by such lender.

1.3 Government Receivables. Where the receivables contract has been entered into with the government or a government agency, are there different requirements and laws that apply to the sale or collection of those receivables?

In principle, there are no different requirements applicable in a situation where an obligor has entered into a receivables contract with the government or a government agency.

The government and government agencies are, however, subject to restrictions through the operation of Dutch public law and this may apply in relation to activities concerning the sale and purchase of receivables. A key principle is the requirement that the government or government agencies need to act in accordance with the Dutch law principle of "good management" (*algemene beginselen van behoorlijk bestuur*). In addition, a government entity or agency may not exercise any right it has under a private law arrangement to serve a public interest, if and to the extent that sufficient powers are available under public law to serve such interest. If public law does not provide for the government or government agency a particular right, then such right may be exercised under private law but only to the extent it does not conflict or otherwise seek to circumvent public law in a manner contrary to public policy.

2 Choice of Law – Receivables Contracts

2.1 No Law Specified. If the seller and the obligor do not specify a choice of law in their receivables contract, what are the main principles in your jurisdiction that will determine the governing law of the contract?

Section 4 of the EC Regulation on the law applicable to contractual obligations of 17 June 2008 (the ***Rome I Regulation***) determines the governing law of an agreement absent of any express choice of law by the parties. Dutch law follows Section 4 of the Rome I Regulation. Specifically, a receivables contract will be governed by the law of the country where the party having to effect the "characteristic performance" of the contract has its habitual residence, unless it is clear from all the relevant circumstances of the matter that the receivables contract has a closer connection with another country, in which case the law of such other country applies. Sections 5 to 8 of the Rome I Regulation contain exceptions to the rule of Section 4, which includes consumer, insurance and individual employment contracts.

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2.2 Base Case. If the seller and the obligor are both resident in your jurisdiction, and the transactions giving rise to the receivables and the payment of the receivables take place in your jurisdiction, and the seller and the obligor choose the law of your jurisdiction to govern the receivables contract, is there any reason why a court in your jurisdiction would not give effect to their choice of law?

Dutch law will follow the general principle laid down in Section 3 of the Rome I Regulation in that the contract shall be governed by the law chosen by the parties. If the parties choose Dutch law as the law governing the contract, and all other elements of the matter are linked to the Netherlands, then other things being equal, there is no reason why the choice of Dutch law by the parties would not be upheld by a Dutch court.

2.3 Freedom to Choose Foreign Law of Non-Resident Seller or Obligor. If the seller is resident in your jurisdiction but the obligor is not, or if the obligor is resident in your jurisdiction but the seller is not, and the seller and the obligor choose the foreign law of the obligor/seller to govern their receivables contract, will a court in your jurisdiction give effect to the choice of foreign law? Are there any limitations to the recognition of foreign law (such as public policy or mandatory principles of law) that would typically apply in commercial relationships such as that between the seller and the obligor under the receivables contract?

In principle, yes. A Dutch court will in such a scenario give effect to the choice of foreign law. However, following the Rome I Regulation, Dutch courts: (i) may give effect to overriding mandatory provisions of the law of the country where the obligations arising out of the contract must be or have been performed, insofar as those overriding mandatory provisions render the performance of the contract unlawful; (ii) shall have regard to the law of the country in which the performance takes place in relation to the manner of performance and the steps to be taken in event of defective performance; and (iii) may refuse the application of a provision of the law of any country otherwise applicable to the contract, if such application is manifestly incompatible with the public policy ("*ordre public*") of the Netherlands. Furthermore, where all the other elements relevant to the situation at the time of the choice of the laws of the foreign jurisdiction (as the governing law of the contract) are located in a country other than the foreign jurisdiction, the choice of the parties shall not prejudice the application of provisions of the law of that other country which cannot be derogated from by agreement.

3 Choice of Law – Receivables Purchase Agreement

3.1 Base Case. Does your jurisdiction's law generally require the sale of receivables to be governed by the same law as the law governing the receivables themselves? If so, does that general rule apply irrespective of which law governs the receivables (i.e., your jurisdiction's laws or foreign laws)?

Dutch law permits the choice of foreign law as the governing law for transactions with a foreign element e.g., a transaction involving foreign parties or assets located outside the Netherlands. However, such choice of law is subject to limitations relating to public policy and certain mandatory rules as set out in the Rome I Regulation.

With respect to the question of which law governs the proprietary aspects of the assignment of receivables (such as the requirements for a valid and effective assignment, and issues relating to collection and enforcement), the Dutch Supreme Court has ruled that Article 12(1) of the (then) Rome Convention (now Article 14(1) of the Rome I Regulation) not only applies to the obligatory aspects but also to the proprietary aspects of the transfer. This is now set out in title 10, book 10 of the Dutch Civil Code (*Burgerlijk Wetboek*). This means that the parties are free to choose the governing law in respect of the proprietary aspects of an assignment subject to the limitations set out in the Rome I Regulation.

3.2 Example 1: If (a) the seller and the obligor are located in your jurisdiction, (b) the receivable is governed by the law of your jurisdiction, (c) the seller sells the receivable to a purchaser located in a third country, (d) the seller and the purchaser choose the law of your jurisdiction to govern the receivables purchase agreement, and (e) the sale complies with the requirements of your jurisdiction, will a court in your jurisdiction recognise that sale as being effective against the seller, the obligor and other third parties (such as creditors or insolvency administrators of the seller and the obligor)?

A Dutch court would recognise the sale and assignment of the receivable under the Dutch law-governed receivables purchase agreement. The sale and assignment will be effective against the seller, the obligor and other third parties (such as creditors and bankruptcy trustees of the seller and the obligor). However, the efficacy of the sale and assignment is subject to the following limitations, which if applicable, may render such sale and assignment ineffective or otherwise void, in whole or in part, against such seller, obligor or other such third parties. Firstly, any applicable bankruptcy, insolvency, moratorium, suspension of payments, emergency and other similar rules and laws of general application relating to or affecting generally the enforcement of creditors' rights and remedies from time to time in effect. Secondly, any legal act (*rechtshandeling*) by any party and the validity of a transaction is subject to and limited by the protection afforded by Dutch law to creditors whose interests have been adversely affected. These rules relate to (i) unlawful acts (*onrechtmatige daden*) based on Section 6:162 *et seq.* of the Dutch Civil Code (*Burgerlijk Wetboek*), and (ii) fraudulent conveyances or preferences (*actio pauliana*) within the meaning of Section 3:45 of the Dutch Civil Code (*Burgerlijk Wetboek*) and/or Section 42 *et seq.* of the Dutch Bankruptcy Act (*Faillissementswet*).

3.3 Example 2: Assuming that the facts are the same as Example 1, but either the obligor or the purchaser or both are located outside your jurisdiction, will a court in your jurisdiction recognise that sale as being effective against the seller and other third parties (such as creditors or insolvency administrators of the seller), or must the foreign law requirements of the obligor's country or the purchaser's country (or both) be taken into account?

A Dutch court would recognise the sale and assignment of the receivable under the Dutch law-governed receivables purchase agreement. The sale and assignment will be effective against the seller and other third parties (such as creditors and bankruptcy trustees of the seller). This is the case even if the requirements for an effective sale and assignment under the laws of the obligor or purchaser's country have not been complied with. However, the efficacy of such sale and assignment is subject to the limitations described in question 3.1.

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3.4 Example 3: If (a) the seller is located in your jurisdiction but the obligor is located in another country, (b) the receivable is governed by the law of the obligor's country, (c) the seller sells the receivable to a purchaser located in a third country, (d) the seller and the purchaser choose the law of the obligor's country to govern the receivables purchase agreement, and (e) the sale complies with the requirements of the obligor's country, will a court in your jurisdiction recognise that sale as being effective against the seller and other third parties (such as creditors or insolvency administrators of the seller) without the need to comply with your jurisdiction's own sale requirements?

A Dutch court would recognise the sale and assignment of the receivable under the law governing the receivables purchase agreement. The sale and assignment will be effective against the seller and other third parties (such as creditors and bankruptcy trustees of the seller). This is the case even if the requirements for an effective sale and assignment under Dutch law have not been complied with. However, under Dutch law the efficacy of such sale and assignment is subject to the limitations described in question 3.1.

3.5 Example 4: If (a) the obligor is located in your jurisdiction but the seller is located in another country, (b) the receivable is governed by the law of the seller's country, (c) the seller and the purchaser choose the law of the seller's country to govern the receivables purchase agreement, and (d) the sale complies with the requirements of the seller's country, will a court in your jurisdiction recognise that sale as being effective against the obligor and other third parties (such as creditors or insolvency administrators of the obligor) without the need to comply with your jurisdiction's own sale requirements?

A Dutch court would recognise the sale and assignment of the receivable under the law governing the receivables purchase agreement. The sale and assignment will be effective against the obligor and other third parties (such as creditors and bankruptcy trustees of the obligor). This is case even if the requirements for an effective sale and assignment under Dutch law have not been complied with. However, under Dutch law the efficacy of such sale and assignment is subject to the limitations described in question 3.1.

3.6 Example 5: If (a) the seller is located in your jurisdiction (irrespective of the obligor's location), (b) the receivable is governed by the law of your jurisdiction, (c) the seller sells the receivable to a purchaser located in a third country, (d) the seller and the purchaser choose the law of the purchaser's country to govern the receivables purchase agreement, and (e) the sale complies with the requirements of the purchaser's country, will a court in your jurisdiction recognise that sale as being effective against the seller and other third parties (such as creditors or insolvency administrators of the seller, any obligor located in your jurisdiction and any third party creditor or insolvency administrator of any such obligor)?

A Dutch court would recognise the sale and assignment of the receivable under the law governing the receivables purchase agreement. The sale and assignment will be effective against the seller, an obligor located in the Netherlands and other third parties (such as creditors and bankruptcy trustees of the seller and such obligor). However, under Dutch law the efficacy of such sale and assignment is subject to the limitations described in question 3.1.

4 Asset Sales

4.1 Sale Methods Generally. In your jurisdiction what are the customary methods for a seller to sell receivables to a purchaser? What is the customary terminology – is it called a sale, transfer, assignment or something else?

In the Netherlands, the customary method of transferring receivables from a seller to a purchaser is by way of a sale (*verkoop*) and assignment (*cessie*). Notwithstanding this, the terms "sale", "assignment" and "transfer" are used interchangeably.

The sale is usually recorded in a written contract, namely, a receivables sale and purchase agreement (or just a "receivables purchase agreement"). The contract of sale and purchase creates an acceptable "legal title" (*titel*) which is required under Dutch law for an effective transfer of a receivable. "Title" in this context means the method by which an asset is conveyed and not the strength of the interest of the seller in the receivable. In order to perfect the transfer and make the purchaser the legal owner of the receivables, valid delivery (*levering*) of the receivable is required. This is customarily achieved by the parties entering into a deed of assignment.

Such a transfer can either be structured as a disclosed assignment, meaning, a receivables transfer with notification to the underlying obligor (*openbare cessie*) or, in respect of receivables that exist or are arising from an existing legal relationship at the time of the transfer, as an undisclosed assignment (*stille cessie*), meaning a receivables transfer without notification to the underlying obligor. Any perfection requirements applicable to both forms of assignment are further described under question 4.2.

4.2 Perfection Generally. What formalities are required generally for perfecting a sale of receivables? Are there any additional or other formalities required for the sale of receivables to be perfected against any subsequent good faith purchasers for value of the same receivables from the seller?

For a valid transfer of receivables, Dutch law requires: (i) a seller which has all the required power to dispose of the receivables (*beschikkingsbevoegdheid*); (ii) a valid title for the transfer of the receivables (*geldige titel*), and which is customarily recorded in a receivables purchase agreement; and (iii) a valid delivery (*levering*) of the receivables. As set out under question 4.1, the delivery can be a disclosed assignment (*openbare cessie*) or, in respect of receivables that exist or are arising from an existing legal relationship at the time of the transfer, as an undisclosed assignment (*stille cessie*).

In order to perfect a disclosed assignment, notification of the sale and assignment to the underlying obligors is required at the time of the transfer.

For an undisclosed assignment to be effective, the underlying transfer deed (*cessie-akte*) should either be registered with the Dutch Tax Authorities or drawn up in a notarial format and executed in front of a Dutch civil law notary. In the case of an undisclosed assignment, in order to prevent a valid discharge (*bevrijdende betaling*) of the debt obligation under the receivable by the underlying obligor to the seller (as opposed to the purchaser), notification of the sale and assignment is required. Following such notification, the obligor

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can only validly discharge its payment obligations by making the relevant payment to the purchaser. This is particularly important in the case of an actual or potential insolvency of the seller where notification of the sale to the obligor would avoid payments being made by the obligor into the insolvent estate of the seller, to the detriment of the purchaser. See question 4.4 below.

There are no other formalities required for the perfection of the sale of receivables by a seller to a purchaser so as to bind any subsequent good faith purchasers for the value of the same receivables from the seller.

In the case of multiple sales of a receivable by the same seller, a subsequent purchaser of such a receivable will not be protected against any prior assignment so long as such prior assignment was perfected. This is irrespective of any good faith on the part of the subsequent assignee. A potential mitigant for the subsequent assignee is to invoke Section 3:36 of the Dutch Civil Code (*Burgerlijk Wetboek*) which provides certain protection to a third-party purchaser. However, the likelihood of success for the subsequent assignee may be small as it is not easy to comply with the requirements of this provision in the Dutch Civil Code (*Burgerlijk Wetboek*), in part due to the burden of proof on the purchaser. Instead, a subsequent assignee's main cause of action would be a damages claim against the seller, say, for breach of asset and title warranties.

4.3 Perfection for Promissory Notes, etc. What additional or different requirements for sale and perfection apply to sales of promissory notes, mortgage loans, consumer loans or marketable debt securities?

The law on negotiable instruments, such as a promissory note, is set out in the Code (*Wetboek van Koophandel*). The relevant provisions of the Dutch Commercial Code reflect, for the most part, the terms of the 1930 and 1931 Geneva Conventions to which the Netherlands is party. However, these provisions of the Dutch Commercial Code only apply to a promissory note payable to order and so long as the instrument qualifies as a negotiable instrument under the Dutch Commercial Code.

A promissory note payable to order must state the name of the person to whom or to whose order the relevant payment must be made. Under Dutch law a promissory note payable to order is transferred by means of physical delivery of the instrument to the endorsee (*geëndosseerde*) and an endorsement to be written on (the back of) the promissory note itself or on a slip affixed thereto (*verlengstuk*). Such delivery must be effected by a person under a valid title and with the requisite power to dispose of the instrument.

A promissory note payable to a bearer of the note is governed by Dutch law applicable to bearer instruments. A transfer of ownership of a bearer instrument requires delivery through the transfer of possession (*bezitsverschaffing*) of the instrument to the purchaser, by a person under a valid title and with the requisite power to dispose of the instrument.

Under Dutch law, the proprietary aspects (such as the transfer of ownership) of book entry securities (*girale effecten*) held in a securities account with an applicable bank or other entity, are governed by the laws of the state in whose territory the relevant bank maintains the securities account in which such securities are held. Under Dutch law, the laws of such state will determine (i) which proprietary rights can be vested in the securities as well as the nature and contents of such rights, (ii) the perfection requirements for a transfer of the securities or for the vesting of a proprietary right in such securities, (iii) which party is entitled to exercise any rights attached to the securities, (iv) the manner in which the contents of any proprietary rights in the securities can vary, the manner in which any proprietary rights in such securities may pass by operation of law (*overgaan*) and the manner in which any proprietary rights in the securities terminate and the nature of the relationship between the various proprietary rights in such securities, and (v) the method of foreclosure in respect of any applicable proprietary rights in the securities.

Under Dutch law, securities held through and registered with Euroclear Netherlands will be transferred in accordance with the Securities Giro Act (*Wet Giraal Effectenverkeer* or ***Wge***). The Wge provides for a transfer of the relevant securities by means of a book entry in the name of the purchaser at the bank where the securities are held.

4.4 Obligor Notification or Consent. Must the seller or the purchaser notify obligors of the sale of receivables in order for the sale to be effective against the obligors and/or creditors of the seller? Must the seller or the purchaser obtain the obligors' consent to the sale of receivables in order for the sale to be an effective sale against the obligors? Whether or not notice is required to perfect a sale, are there any benefits to giving notice – such as cutting off obligor set-off rights and other obligor defences?

As set out under question 4.2, a valid transfer of receivables can be achieved by a silent assignment or a disclosed assignment.

With respect to the enforceability of the assignment against the obligors under a disclosed and undisclosed assignment, notification of the assignment to the obligors is required in order to require the obligors to validly discharge their payment obligations under the receivables to the purchaser. Prior to such notification, obligors can only validly discharge their payment obligations under the receivables by paying the seller.

In the case of an undisclosed assignment, payments made by obligors to the seller prior to notification of the assignment to the purchaser, but after bankruptcy, (preliminary) suspension of payments or emergency regulations in respect of the seller having been declared, will form part of the seller's estate. In respect of such payments, the purchaser will become a creditor of the estate (*boedelschuldeiser*) and be entitled to receive payment from the seller's estate in priority to the seller's unsecured creditors, but after any preferred creditors. In addition, the purchaser will have to share in the general bankruptcy costs of the seller meaning that any enforcement proceeds will potentially be reduced as a result of such costs. After notification of the assignment is made to the obligors, such obligors can only validly discharge their payment obligations under the receivables by paying the purchaser.

Under Dutch law, the obligor's consent is not required for any sale and assignment of receivables, unless the contract or arrangement constituting or otherwise affecting the receivables contains a restriction or prohibition on any sale and assignment of such receivables. This is discussed under question 4.7 below.

In addition, note that under Section 7:69(2) of the Dutch Civil Code (*Burgerlijk Wetboek*), consumers under consumer credit agreements (but not mortgage loans) should be informed of any sale and assignment of the credit arrangement. There is an exception to this rule if the seller (as originator of the loan) continues to manage and service the credit relationship with the consumer following such sale and assignment.

In respect of set-off, under Dutch law, an obligor has a right of set-off against a counterparty if it has a counter-claim which corresponds to its debt to the same counterparty, and the debtor is entitled to pay its debt to the counterparty as well as being entitled to enforce its

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payment claim against such counterparty. If these requirements are met, an obligor is entitled to set off any amounts due by the seller to the obligor against the obligor's payment obligations to the seller under the receivable, but only prior to notification to the obligor of the sale and assignment of the receivables by the seller to the purchaser. As a result of the operation of the set-off the amount payable by the obligor to the seller under a receivable will be in whole or in part extinguished (*gaat teniet*).

After notification of the sale and assignment, an obligor will have a similar right of set-off against the purchaser provided that the legal requirements for set-off described above have been met. In addition, the following must also be satisfied; either (i) the counterclaim of the obligor against the seller results from the same legal relationship as between the obligor and seller under the transferred receivable; or (ii) the counterclaim of the obligor against the seller was originated and became due and payable prior to the sale and assignment and subsequent notification of such sale and assignment to the obligor.

The question as to whether a Dutch court will conclude that the receivable and the counterclaim of the obligor against the seller result from the same legal relationship will depend on the relevant facts and circumstances. However, even if a Dutch court came to the conclusion that the claim and counterclaim originate from a different set of legal relationships between the obligor and seller, the obligor may still be able to invoke a right of set-off against the seller or purchaser, as applicable, if the counterclaim of the obligor against the seller originated (*opgekomen*) and became due and payable prior to notification of the sale and assignment of the receivable to the purchaser. This is on the grounds of the Dutch law principle of "reasonableness and fairness", under which a Dutch court may conclude that it would not in such circumstances be appropriate to deny an obligor a right of set-off, even if the claim and counterclaim objectively originate from different legal relationships.

Finally, a seller may purport to limit by contract or otherwise the right of an obligor to invoke a right of set-off. If the obligor is a consumer such limitation would in principle contravene certain Dutch consumer protection law and, accordingly, is capable of being declared null and void by the relevant consumer.

4.5 Notice Mechanics. If notice is to be delivered to obligors, whether at the time of sale or later, are there any requirements regarding the form the notice must take or how it must be delivered? Is there any time limit beyond which notice is ineffective – for example, can a notice of sale be delivered after the sale, and can notice be delivered after insolvency proceedings have commenced against the obligor or the seller? Does the notice apply only to specific receivables or can it apply to any and all (including future) receivables? Are there any other limitations or considerations?

There are no formal requirements on the form or method of delivering a notice to an obligor. Oral notification is possible but this is not recommended as notification may be disputed due to a lack of evidence. Under Section 3:37 of the Dutch Civil Code (*Burgerlijk Wetboek*), a notice will only be duly delivered upon receipt by the counterparty except if non-receipt of such notification is deemed to be a risk borne by such counterparty. This could be the case if the address details of a Dutch company do not correspond with the information set out in the public registers or contract.

It is possible to notify an obligor by using a single notice of assignment in respect of a number of receivables. The notice should specify that any and all receivables which the seller has, or may originate in the future, under which that obligor has (or will have, as applicable) a payment obligation have been (or will be, as applicable) assigned to the purchaser.

Notification to an obligor after any insolvency of the seller (e.g., bankruptcy or a suspension of payments) is possible. There may, however, be consequences on the ability of the purchaser to recover the payments made by an obligor to the seller in respect of the relevant receivables.

In the case of an undisclosed assignment, and as discussed under question 4.2, payments made by an obligor to a seller prior to notification of the assignment to the purchaser, but after bankruptcy, (preliminary) suspension of payments or emergency regulations in respect of the seller having been declared, will form part of the seller's estate. In respect of these payments, the purchaser will be a creditor of the estate (*boedelschuldeiser*). However, notification to the obligors after the insolvency of the seller is still possible and will be effective.

The situation is different in the case of a disclosed assignment. In order to be valid, a disclosed assignment requires notification to the obligor. If such notification has not occurred prior to any insolvency of the seller, such sale and assignment will not be effective and legal title to the receivables will not have passed from the seller to the purchaser.

4.6 Restrictions on Assignment – General Interpretation. Will a restriction in a receivables contract to the effect that "None of the [seller's] rights or obligations under this Agreement may be transferred or assigned without the consent of the [obligor]" be interpreted as prohibiting a transfer of receivables by the seller to the purchaser? Is the result the same if the restriction says "This Agreement may not be transferred or assigned by the [seller] without the consent of the [obligor]" (i.e., the restriction does not refer to rights or obligations)? Is the result the same if the restriction says "The obligations of the [seller] under this Agreement may not be transferred or assigned by the [seller] without the consent of the [obligor]" (i.e., the restriction does not refer to rights)?

In answering this question, we have assumed that the relevant receivables contract is governed by Dutch law. Based on Dutch private international law and the relevant provisions of the Rome I Regulation, the interpretation of any contractual restriction will be in accordance with Dutch law.

When interpreting contracts, a Dutch court will not only look at the literal meaning of the clause, but also take into account all relevant facts and circumstances of the matter. It will also consider the meaning that the parties to the contract would have reasonably given to the specific clause, and what each party could have reasonably expected from each other, again in the particular circumstances.

A restriction stating that "None of the [seller's] rights or obligations under this Agreement may be transferred or assigned without the consent of the [obligor]" will likely be interpreted by a Dutch court as prohibiting a transfer of receivables by the seller. This assumes that there are no additional facts or circumstances that would affect this conclusion, for example, a subsequent written or oral variation of the restriction.

A restriction stating that "This Agreement may not be transferred or assigned by the [seller] without the consent of the [obligor]" (i.e., the restriction does not refer to rights or obligations), will likely be interpreted by a Dutch court in the same way as described above.

A restriction stating that "The obligations of the [seller] under this Agreement may not be transferred or assigned by the [seller] without

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the consent of the [obligor]" will likely not have a similar effect as the provisions described above. This is because the restriction does not restrict the transferability of rights (such as receivables) of the seller under the contract, rather the obligations of a seller. As mentioned above, this assumes that there are no additional facts or circumstances that would affect this conclusion. For example, there must be no subsequent written or oral variation of the restriction, or factors that suggest the parties intended to also prohibit an assignment of receivables and not merely obligations.

4.7 Restrictions on Assignment; Liability to Obligor. If any of the restrictions in question 4.6 are binding, or if the receivables contract explicitly prohibits an assignment of receivables or "seller's rights" under the receivables contract, are such restrictions generally enforceable in your jurisdiction? Are there exceptions to this rule (e.g., for contracts between commercial entities)? If your jurisdiction recognises restrictions on sale or assignment of receivables and the seller nevertheless sells receivables to the purchaser, will either the seller or the purchaser be liable to the obligor for breach of contract or tort, or on any other basis?

Under Dutch law, the general principle is that a party may assign its rights under a contract unless such assignment is restricted by law or contract. This is on the basis that the right is a proprietary right (so-called, *right in rem*) rather than a personal right (so-called, r*ight in personam*) which is not capable of being assigned to another party.

Parties can agree to restrict the assignment of receivables arising under a contract, e.g., making such a transfer or assignment subject to prior consent, written or otherwise. Depending on the wording of a contract, such a restriction can even have a proprietary effect (*goederenrechtelijk effect*). Whether or not a restriction has a proprietary effect will be a question of fact and dependent on the wording of the restriction. It should be clear from the face of the provision that the parties expressly intended to create a restriction on the transfer of the receivables.

Any assignment by a seller in contravention of a restriction that has a proprietary effect would be invalid. Furthermore, it would not be enforceable against the obligor under the receivable purported to be assigned.

4.8 Identification. Must the sale document specifically identify each of the receivables to be sold? If so, what specific information is required (e.g., obligor name, invoice number, invoice date, payment date, etc.)? Do the receivables being sold have to share objective characteristics? Alternatively, if the seller sells *all* of its receivables to the purchaser, is this sufficient identification of receivables? Finally, if the seller sells *all* of its receivables *other than* receivables owing by one or more specifically identified obligors, is this sufficient identification of receivables?

The receivables purported to be assigned under a deed of assignment should be sufficiently identifiable (*omschrijft met voldoende bepaaldheid*) within the meaning of Section 3:84(2) of the Dutch Civil Code (*Burgerlijk Wetboek*). Under Dutch law, a receivable is "sufficiently identifiable" if the deed of assignment contains such details of the receivables purported to be assigned, such that it can be determined which receivables the parties have intended to assign. The deed of assignment does not need to contain all the details of the assigned receivables. However, there needs to be sufficient data to enable it to be established which receivables were the subject of the assignment (e.g., details of the contract (e.g., an invoice or obligor number and corresponding principal amount outstanding on the applicable date of assignment) under which the relevant assigned receivables have been originated). It is also possible to use more generic wording, which is often used by banks and professional market parties. This method is used when the intention is to capture all relevant receivables in the books of the seller on the date of the assignment. To ensure that future originated receivables are also effectively assigned using such method, periodic updates of the list of receivables specified in the deed of assignment is desirable (and customary, for example, by using supplemental deeds of assignment) to satisfy the requirement that the assigned receivables are sufficiently identifiable so as to be effectively assigned. Please also see our answer to question 4.11.

4.9 Recharacterisation Risk. If the parties describe their transaction in the relevant documents as an outright sale and explicitly state their intention that it be treated as an outright sale, will this description and statement of intent automatically be respected or is there a risk that the transaction could be characterised by a court as a loan with (or without) security? If recharacterisation risk exists, what characteristics of the transaction might prevent the transfer from being treated as an outright sale? Among other things, to what extent may the seller retain any of the following without jeopardising treatment as an outright sale: (a) credit risk; (b) interest rate risk; (c) control of collections of receivables; (d) a right of repurchase/redemption; (e) a right to the residual profits within the purchaser; or (f) any other term?

Dutch law does not expressly provide for the recharacterisation of a transaction structured as an outright transfer as a secured loan. There is, however, academic debate as to whether or not this is possible.

The most important factor in the characterisation of the transaction is the intention of the parties. The parties must intend that the sale of the receivables is by way of an outright transfer and that the seller intends to sell, and the purchaser intends to purchase, the receivable, in both cases in a way that there is no residual ownership interest retained by the seller.

Without any express provisions or authority under Dutch law, jurisprudence of other jurisdictions may in our view be helpful (although it should be emphasised, not necessarily relevant or determinative) to support or discredit any recharacterisation analysis under Dutch law. For example, it is important that the purchaser is free to deal with the acquired receivables and capable of onselling them to a third party without any obligation to account for any profit to, or recover any loss from, the seller. Accordingly, any retention of credit risk in relation to a receivable by a seller (such that the seller remains exposed to the credit risk on the relevant receivable) is not itself necessarily helpful to the true-sale analysis. The same would apply in relation to any control the seller retains in relation to determining the interest rate payable under a receivable. It is often the case that a seller may only amend an interest rate with the consent of the purchaser, and that if the seller does retain a right to amend an interest rate, that the seller acts in its capacity as a servicer appointed by the purchase (see further below). Finally, (i) the existence of a repurchase obligation of the seller for receivables sold to the purchaser in breach of representations and warranties, or (ii) the existence of a repurchase option by the seller of the receivables sold to the purchaser, provided the repurchase is conducted on arm's length terms, including, the repurchase price, or the division of the purchase price payable by a purchaser to a seller into an initial and deferred purchase price, will not in itself be considered to be inconsistent with the existence of a true sale. The same applies to

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the seller retaining control of the collections, provided the seller acts for and on behalf of the purchaser (i.e., as a servicer), again, on arm's length terms.

Note that if there is any recharacterisation of a sale into a security interest, the sale would automatically be void under Section 3:84(3) of the Dutch Civil Code (*Burgerlijk Wetboek*) which provides that any agreement that purports to transfer an asset by way of security or which does not purport to transfer an asset, in a way such that it does not become part of the assets of a purchaser, is not a valid title. See question 4.1 on the requirement of a valid title.

Sellers often have a repurchase obligation in certain circumstances under Dutch RMBS transactions. Sellers also have the right to excess spread generated by the transaction in the form of deferred purchase price payable by the SPV to a seller. Both features do not in general adversely affect the true sale analysis as a matter of Dutch law.

4.10 Continuous Sales of Receivables. Can the seller agree in an enforceable manner to continuous sales of receivables (i.e., sales of receivables as and when they arise)? Would such an agreement survive and continue to transfer receivables to the purchaser following the seller's insolvency?

Yes, this is possible. A seller may agree to a sale of all of its current and future receivables. The efficacy of the sale will be subject to the limitations described in question 3.1.

4.11 Future Receivables. Can the seller commit in an enforceable manner to sell receivables to the purchaser that come into existence after the date of the receivables purchase agreement (e.g., "future flow" securitisation)? If so, how must the sale of future receivables be structured to be valid and enforceable? Is there a distinction between future receivables that arise prior to *versus* after the seller's insolvency?

Under Dutch law, it is possible to sell and assign receivables before they have come into existence (*bij voorbaat*), so that the purchaser automatically becomes the owner of such receivables when they do. Only future receivables that (i) exist at the time of the assignment, or (ii) arise under an existing legal relationship, can be validly transferred. This is the case irrespective of whether the assignment is disclosed or undisclosed.

The assignment of future receivables is perfected at the time the future receivable is acquired by the seller.

Any receivables acquired by the seller after the date of its insolvency would form part of its estate and would not be validly assigned.

4.12 Related Security. Must any additional formalities be fulfilled in order for the related security to be transferred concurrently with the sale of receivables? If not all related security can be enforceably transferred, what methods are customarily adopted to provide the purchaser the benefits of such related security?

Under Dutch law, security rights, such as mortgage rights and pledges (*pandrechten*), are considered both accessory rights (*afhankelijke rechten*) and ancillary rights (*nevenrechten*). These rights transfer automatically by operation of law, together with the receivables to which they are connected. So, upon assigning a receivable, the purchaser in principle also has the benefit of any security rights that are connected to it.

However, financial institutions or professional market parties often use security rights which do not only secure a specific loan granted to an obligor under its secured financing arrangement, but also other liabilities and monies that such a obligor, now or in the future, may owe to the seller (so-called "all-monies security" rights) (*bankzekerheidsrechten*).

The prevailing view amongst Dutch legal academics is that an all-monies security right (partially) follows the receivable as an accessory right upon assignment. Whether an all-monies security right remains with the original seller or (partially) transfers to the purchaser will be a matter of interpreting the relevant deed creating such security right.

If an all-monies security right has (partially) transferred to the purchaser, it will be jointly held by the relevant seller and purchaser and the rules applicable to a joint estate (*gemeenschap*) apply. On the basis of Section 3:166(2) of the Dutch Civil Code (*Burgerlijk Wetboek*), the shares of the co-owners are equal, unless their legal relationship provides otherwise. To mitigate against the potential for disputes as a result of jointly-held interests, the relevant receivables purchase agreement will often contain contractual arrangements between the seller and the purchaser in respect of the management, administration and foreclosure procedures in respect of any jointly-held rights.

It is noted that such a contractual agreement may not be effective as against the underlying obligors and may not be enforceable to the extent that such arrangement is inconsistent with Dutch legislation applying to jointly-held interests.

4.13 Set-Off; Liability to Obligor. Assuming that a receivables contract does not contain a provision whereby the obligor waives its right to set-off against amounts it owes to the seller, do the obligor's set-off rights terminate upon its receipt of notice of a sale? At any other time? If a receivables contract does not waive set-off but the obligor's set-off rights are terminated due to notice or some other action, will either the seller or the purchaser be liable to the obligor for damages caused by such termination?

Under Dutch law, an obligor will be entitled to set off amounts it owes to the seller against amounts owed to it by the seller, provided that the legal requirements for set-off, such as mutuality, are met. After an assignment of the receivable to the purchaser, and notification of such assignment to the obligor, the obligor will also be entitled to such set-off rights *vis-à-vis* the purchaser, provided that the legal requirements for set-off are met (but except for mutuality). The key requirements are that: (i) the counterclaim of the obligor results from the same legal relationship as the assigned receivable; or (ii) the counterclaim of the obligor came into existence and became due and payable prior to the assignment of the receivable and the notification of such assignment to the debtor.

Whether a court comes to the conclusion that the receivable and the claim of the obligor against the seller result from the same legal relationship will depend on all relevant facts and circumstances involved. However, even if these would be held to be different legal relationships, it cannot be ruled out, depending on the circumstances, that set-off will be possible if the counterclaim of the obligor came into existence and became due and payable prior to notification of the assignment, provided that all other requirements for set-off have been met.

This limitation of the obligor's set-off right does not lead to liability for either the seller or purchaser.

In the bankruptcy of a seller, an obligor will have broader set-off rights afforded to him pursuant to the Dutch Bankruptcy

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Act (*Faillissementswet*). Under the Dutch Bankruptcy Act (*Faillissementswet*), a person who is both an obligor and creditor of the bankrupt counterparty can set off his debt against his claim, if such claim (a) came into existence prior to the moment at which the bankruptcy has become effective, or (b) resulted from transactions with the bankrupt counterparty concluded prior to the bankruptcy being declared.

In relation to consumer loans (but excluding mortgages), consumers are entitled to invoke the same defences and rights (including set-off) against the purchaser as they would have had against the originator.

4.14 Profit Extraction. What methods are typically used in your jurisdiction to extract residual profits from the purchaser?

The principal method is excess spread payable to the seller as the holder of the most junior class of notes issued by the note issuing SPV. The excess spread is often attributable to the contingent deferred purchase price payable by the SPV to the seller for the receivables. In addition, under Dutch RMBS transactions involving a financial institution as the seller, the interest rate swap can be used by the seller to extract income from the securitised cashflows. This is done by the seller entering into a back-to-back interest rate swap with the swap counterparty that provides the interest rate hedging to the note issuing SPV.

5 Security Issues

5.1 Back-up Security. Is it customary in your jurisdiction to take a "back-up" security interest over the seller's ownership interest in the receivables and the related security, in the event that an outright sale is deemed by a court (for whatever reason) not to have occurred and have been perfected (see question 4.9 above)?

To avoid recharacterisation risk, it is customary in the Netherlands not to take back-up security when selling and assigning receivables. To take such security is generally not advisable.

5.2 Seller Security. If it is customary to take back-up security, what are the formalities for the seller granting a security interest in receivables and related security under the laws of your jurisdiction, and for such security interest to be perfected?

As provided for under question 5.1 above, it is not customary in the Netherlands to take back-up security.

5.3 Purchaser Security. If the purchaser grants security over all of its assets (including purchased receivables) in favour of the providers of its funding, what formalities must the purchaser comply with in your jurisdiction to grant and perfect a security interest in purchased receivables governed by the laws of your jurisdiction and the related security?

Under Dutch law, security over purchased receivables is created under a "right of pledge". There are two types of pledges over receivables: a "disclosed" right of pledge and an "undisclosed" right of pledge depending on whether the obligor of the claim has been given notice of the pledge. Given that notice is required for the perfection of a disclosed right of pledge, it should be sent shortly after the creation of the pledge itself. The disclosed pledge does not require notarisation or registration. However, an undisclosed right of pledge must either be drawn up in notarial deed form or otherwise registered with the tax authorities for the pledge to be valid. In the case of an undisclosed right of pledge, the lack of notification does not impact the validity of the pledge. It does, however, mean that the debtor can discharge its debt by paying the seller, not the purchaser.

In relation to the related security, no statutory provision exists under Dutch law to determine whether, upon the creation of a right of pledge over a receivable, and notification of the same to the obligor, the security holder (i.e. the purchaser) is entitled to exercise the accessory and ancillary rights granted under the right of pledge.

The prevailing view amongst Dutch academics is that security rights connected to a receivable can be exercised by the pledgee (i.e., the purchaser). This is either because (i) a right of pledge should be regarded as a partial transfer of the receivable (i.e., the accessory and ancillary rights follow the secured assets to the extent that they are connected to the rights transferred to the pledgee), or (ii) because the person that is entitled to collect the receivable is also deemed to be entitled to enforce the related security.

This view is supported by a decision of the Dutch Supreme Court (*Hoge Raad*) on the attachment of a receivable secured by a right of mortgage. Recently, the Dutch Supreme Court also confirmed that a pledgee who has a right of pledge over receivables is also entitled to any accessory and ancillary rights (i.e., security rights) that are connected to such pledged receivable. This is insofar as such pledged receivables themselves have the benefit of a pledge over receivables (such pledge granted by the obligor of the pledgor) over the claims such obligor has against third parties. In this example, the pledgee was authorised to also enforce the security rights that were deemed to be attached to (and form part of) the receivables.

5.4 Recognition. If the purchaser grants a security interest in receivables governed by the laws of your jurisdiction, and that security interest is valid and perfected under the laws of the purchaser's jurisdiction, will the security be treated as valid and perfected in your jurisdiction or must additional steps be taken in your jurisdiction?

The law used to determine whether the grant of a security interest over receivables is valid, is the applicable law under the contract purporting to grant such security.

The governing law of the receivables contract itself will determine: (i) whether the receivable is capable of being pledged; (ii) the legal relationship between the pledgor and the obligor; (iii) the conditions under which the granting of a security right over the receivable is enforceable against the obligor; and (iv) whether the obligations of the obligor have been paid in full and are validly discharged.

Subject to similar exceptions to the validity of the choice of law of the purchaser's country or any third country (other than the Netherlands) as set out under both question 2.3 and the above paragraph, a foreign security right will be recognised in the Netherlands, without any additional steps in relation to recognition being required.

Note that there is no conclusive case law in the Netherlands regarding the enforcement of security rights created under foreign law. The general view is that, if a foreign security right is recognised, such foreign security right will be enforced and will have the ranking that an equivalent security right under Dutch law would have. This means that a security holder will not have any more rights than it would have had if its security right would have been governed by Dutch law.

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5.5 Additional Formalities. What additional or different requirements apply to security interests in or connected to insurance policies, promissory notes, mortgage loans, consumer loans or marketable debt securities?

Under Dutch law, a right of pledge over a promissory note payable to the bearer is created by (i) the pledgor and the pledgee entering into a pledge agreement, and by the physical delivery of the instrument to the pledgee or a third party agreed upon by the pledgor and the pledgee, or (ii) a notarial or registered deed without physical delivery. A right of pledge over a promissory note payable to order is created in the manner mentioned under (i), provided that in addition to that, an endorsement is written on (the back of) the promissory note itself or on a slip affixed thereto (*verlengstuk*).

If the marketable debt securities held by the seller are cleared through and registered with Euroclear Netherlands pursuant to the Wge, then a pledge over these securities is effectuated by means of a simple book entry in the name of the pledgee in the relevant bank's records.

We note, however, that pursuant to Dutch private international law, the law governing the creation of a security interest in securities held in a securities account with a bank or other entity is the laws of the state in which the relevant bank maintains the account.

There are no additional or different requirements for the creation and perfection of a right of pledge over receivables resulting from consumer loans and mortgage loans.

5.6 Trusts. Does your jurisdiction recognise trusts? If not, is there a mechanism whereby collections received by the seller in respect of sold receivables can be held or be deemed to be held separate and apart from the seller's own assets (so that they are not part of the seller's insolvency estate) until turned over to the purchaser?

Dutch law does not have a concept equivalent to a trust.

Under the Hague Convention of the Law Applicable to Trusts and on their Recognition (*Haags Trustverdrag*), a trust created in accordance with the chosen law will be recognised by Dutch courts, provided that the chosen law allows for the creation of a trust. Pursuant to Section 13 of the Trust Convention, Dutch courts will not be bound to recognise a trust where the significant elements of the matter are closely connected with jurisdictions that do not allow for the creation of a trust.

To mitigate against commingling risk, under Dutch securitisation, security is usually granted to a special purpose vehicle (in the form of a bankruptcy remote foundation (*stichting*) or private limited liability company (*besloten vennootschap met beperkte aansprakelijkheid*)). The vehicle has independent directors and no other assets or business meaning that a high degree of asset isolation and separation is achieved.

In addition, the use of "collection foundations", again set up as bankruptcy remote special purpose vehicles, into which seller collections are paid, mitigates against cash commingling risk in any insolvency of the seller. Obligors are directed to pay collections into the collection foundation and not into an account of the seller. Collections are then periodically transferred from the collection foundation to the purchaser. This feature achieves a high degree of cash flow isolation from the risk of seller insolvency (and so analogous to the effect of a trust) and is a model accepted by rating agencies.

5.7 Bank Accounts. Does your jurisdiction recognise escrow accounts? Can security be taken over a bank account located in your jurisdiction? If so, what is the typical method? Would courts in your jurisdiction recognise a foreign law grant of security (for example, an English law debenture) taken over a bank account located in your jurisdiction?

Dutch law does not have a concept identical to escrow accounts because Dutch law has no concept of trust. However, standard bank accounts can be used for specific purposes with the practical effect of an escrow arrangement. For example, if a bank account is maintained by a notary, and it qualifies as a designated account (*kwaliteitsrekening*), it will be separate from the notary's own estate. For this reason, it is customary in the Netherlands to use such types of notarial accounts when escrow arrangements are required.

Security over a bank account is usually taken by way of a disclosed pledge (*openbaar pandrecht*) and we refer to the answer to question 5.3. An important qualification in relation to security over bank accounts is that pursuant to the general banking conditions (*algemene bankvoorwaarden*) in the Netherlands, the account bank retains a first ranking right of pledge in respect of the account, which it may waive if so requested by the beneficiary.

As to the recognition of a foreign law security right in respect of a bank account located in the Netherlands, we refer to the answer to question 5.4.

5.8 Enforcement over Bank Accounts. If security over a bank account is possible and the secured party enforces that security, does the secured party control all cash flowing into the bank account from enforcement forward until the secured party is repaid in full, or are there limitations? If there are limitations, what are they?

Whether the secured party controls all cash flowing into the bank account depends on the nature of the security right. If it is a disclosed right of pledge (*openbaar pandrecht*), all present and future account receivables are subject to the right of pledge, and the pledgee is entitled to collect payments and collect the account receivables without leave of the court.

If an undisclosed right of pledge is created (i.e., the account bank is not notified of the right of pledge), the right to demand payment and to collect the account receivables stays with the account owner until such notification.

A pledge over a bank account will not attach to any payments that are made into the bank account after bankruptcy (*faillissement*) or suspension of payments (*surseance van betaling*) of the account owner (i.e., the pledgor).

5.9 Use of Cash Bank Accounts. If security over a bank account is possible, can the owner of the account have access to the funds in the account prior to enforcement without affecting the security?

A distinction is made between a disclosed right of pledge and an undisclosed right of pledge. Whilst under a disclosed right of pledge the pledgee has control over the funds, the pledgee usually authorises the pledgor to collect payments and access the funds until an enforcement event (as described under the pledge arrangement) occurs.

In the case of an undisclosed pledge, the pledgor will have control of the funds in the account until the account bank is notified of the right of pledge. This does not affect the effectiveness of the security interest.

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6 Insolvency Laws

6.1 Stay of Action. If, after a sale of receivables that is otherwise perfected, the seller becomes subject to an insolvency proceeding, will your jurisdiction's insolvency laws automatically prohibit the purchaser from collecting, transferring or otherwise exercising ownership rights over the purchased receivables (a "stay of action")? If so, what generally is the length of that stay of action? Does the insolvency official have the ability to stay collection and enforcement actions until he determines that the sale is perfected? Would the answer be different if the purchaser is deemed to only be a secured party rather than the owner of the receivables?

Dutch law does not have a concept of an "automatic stay" following the insolvency of a seller of receivables. There is therefore no risk that the courts will prevent the purchaser from freely exercising its ownership right over the purchased receivables.

In the case of the assignment of future receivables, receivables created by the seller after it became insolvent would not be sold and assigned to the purchaser and so would remain part of the seller's estate.

If the assignment is undisclosed, notification of the assignment to the debtor is required to prevent a valid discharge (*bevrijdende betaling*) occurring upon payment by the debtor to the seller. Once notification is made, the debtor can only discharge its payment obligations under the receivable by paying the purchaser.

If no notification is made, payments made by debtors to an insolvent seller will form part of the seller's estate. In respect of these payments, the purchaser will be a creditor of the estate (*boedelschuldeiser*) and will receive payment prior to unsecured creditors, but after preferred ones. It will also have to contribute to the seller's bankruptcy costs.

If a security right is created over the receivables, a pledgee may exercise its rights as if there was no bankruptcy and foreclose the right of pledge. Foreclosure can be effected either by collection of the receivables or by otherwise selling them in compliance with the Dutch laws on enforcement.

If the security right is not created as a financial collateral agreement, a court can order a statutory stay of execution period of up to two months, extendable by another period of up to two months pursuant to Sections 63(a) and 241(a) of the Dutch Bankruptcy Act (*Faillissementswet*).

Finally, pursuant to Section 58(1) of the Dutch Bankruptcy Act (*Faillissementswet*), a bankruptcy trustee (*curator*) can force a secured party to foreclose its security interest within a reasonable time (as determined by the bankruptcy trustee), failing which the bankruptcy trustee will be entitled to sell the relevant rights or assets and distribute the proceeds to the relevant secured party.

6.2 Insolvency Official's Powers. If there is no stay of action, under what circumstances, if any, does the insolvency official have the power to prohibit the purchaser's exercise of its ownership rights over the receivables (by means of injunction, stay order or other action)?

Whilst there is no automatic stay under Dutch law, a bankruptcy trustee could seek to prohibit the purchaser from exercising its (ownership) rights if it is of the view that a fraudulent conveyance or preference (*actio pauliana*) has occurred (see also question 6.3 below). In addition, general defences under Dutch law can be invoked, such as transaction avoidance on the grounds of duress (*bedreiging*), deceit (*bedrog*), undue influence (*misbruik van omstandigheden*), or mistake (*dwaling*).

6.3 Suspect Period (Clawback). Under what facts or circumstances could the insolvency official rescind or reverse transactions that took place during a "suspect" or "preference" period before the commencement of the seller's insolvency proceedings? What are the lengths of the "suspect" or "preference" periods in your jurisdiction for (a) transactions between unrelated parties, and (b) transactions between related parties? If the purchaser is majority-owned or controlled by the seller or an affiliate of the seller, does that render sales by the seller to the purchaser "related party transactions" for purposes of determining the length of the suspect period? If a parent company of the seller guarantee's the performance by the seller of its obligations under contracts with the purchaser, does that render sales by the seller to the purchaser "related party transactions" for purposes of determining the length of the suspect period?

Under Dutch law, any legal act (*rechtshandeling*) and the validity of a transaction itself can be challenged by creditors whose interests have been adversely affected. This challenge is made under the laws relating to (i) fraudulent conveyance, or (ii) preferences (*actio pauliana*) within the meaning of Section 42 *et seq.* of the Dutch Bankruptcy Act (*Faillissementswet*). In respect of the latter, a distinction is made between a fraudulent preference risk as a result of voluntary legal acts (*onverplichte rechtshandeling*) and involuntary legal acts (*verplichte rechtshandelingen*).

A bankruptcy trustee can challenge a debtor's voluntary legal acts, (defined as acts carried out without a prior legal obligation (*onverplichte rechtshandeling*)), by invoking the doctrine of the "*actio pauliana*". This is possible in the following circumstances:

- the legal act must be voluntary. For example, carrying out a *pre-existing* contractual obligation to grant security would *not* be voluntary;
- the legal act must adversely affect one or more of the creditors and such adverse effect must have occurred at the time the challenge is made;
- the debtor must know (or ought to have known) that the legal act would adversely affect the possibility of recourse of one or more of its creditors (this is generally believed to be the case when the insolvency of the debtor was probable at the time of the legal act); and
- if the legal act was for consideration, the party must have known (or ought to have known) that the legal act would have such an adverse effect on the creditor(s) in question.

If a legal act occurs within one year of the seller becoming bankrupt, there is in certain circumstances a rebuttable presumption, that the pledgor knew or ought to have known that the creditors would be adversely affected as a result. The circumstances are that:

- the consideration of the transaction was at a significant undervalue;
- the transaction was entered into with members of the seller's management board or (if the seller is an individual) with relatives;
- the transaction was to provide security for a claim not yet due; and/or
- the transaction was between intra-group corporate members.

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The threshold for challenging *involuntary* legal acts (*verplichte rechtshandelingen*), i.e., legal acts for which there *is* a pre-existing legal obligation, is much higher.

The bankruptcy trustee can successfully challenge involuntary legal acts if the bankruptcy trustee can show that: (i) the debtor's counterparty knew that a petition for bankruptcy had already been filed at the time the act was performed and the seller is subsequently declared bankrupt; or (ii) the debtor and its counterparty colluded with the intention of advancing the counterparty's interests over other creditors.

6.4 Substantive Consolidation. Under what facts or circumstances, if any, could the insolvency official consolidate the assets and liabilities of the purchaser with those of the seller or its affiliates in the insolvency proceeding? If the purchaser is owned by the seller or by an affiliate of the seller, does that affect the consolidation analysis?

There is no doctrine of substantive consolidation under Dutch law. In a receivables purchase transaction, if the sale and transfer has been perfected prior to the seller becoming insolvent, the purchaser will obtain full legal title to the receivables and they will not form part of an insolvent seller's estate.

If the purchaser is owned by the Seller or by an affiliate of the Seller, other considerations may be relevant. For example, if the Seller pursuant to rules of Dutch corporate law (e.g., 403 declarations) has become jointly and severally liable for any financial obligations of the purchaser, this may impact the "true-sale analysis" and may in practice lead to a substantive consolidation.

6.5 Effect of Insolvency on Receivables Sales. If insolvency proceedings are commenced against the seller in your jurisdiction, what effect do those proceedings have on (a) sales of receivables that would otherwise occur after the commencement of such proceedings, or (b) on sales of receivables that only come into existence after the commencement of such proceedings?

Future receivables can be assigned in advance (*bij voorbaat*), even if the assignment is undisclosed, provided that such receivables directly result from a legal relationship existing at that time. In the case of a disclosed assignment, future receivables can only be assigned to the extent that notification to the relevant obligor can take place.

However, the assignment cannot be invoked against the estate of a bankrupt seller if the future receivables came into existence after the seller was declared bankrupt or was granted a suspension of payments. In such circumstances, the receivables fall within the estate of the seller.

6.6 Effect of Limited Recourse Provisions. If a debtor's contract contains a limited recourse provision (see question 7.3 below), can the debtor nevertheless be declared insolvent on the grounds that it cannot pay its debts as they become due?

If a creditor has a claim against the debtor which is due and payable and remains unpaid, such creditor can file for the insolvency of the debtor and the debtor can be declared insolvent, provided that the other requirements for a successful bankruptcy filing have been met. If, on the other hand, such a claim from a creditor is extinguished on the basis of any applicable limited recourse provisions, the claim no longer exists and the creditor cannot petition for the debtor's bankruptcy on the basis of such claim. The validity of limited recourse provisions under Dutch law is further described under question 7.3 below.

7 Special Rules

7.1 Securitisation Law. Is there a special securitisation law (and/or special provisions in other laws) in your jurisdiction establishing a legal framework for securitisation transactions? If so, what are the basics? Is there a regulatory authority responsible for regulating securitisation transactions in your jurisdiction?

The Netherlands has not adopted any specific laws that are applicable to securitisations. There are no specific legal limitations on how a securitisation transaction should be structured and there is also no regulator responsible for regulating securitisation transactions. As a result, securitisation transactions are effected under the general laws of the Netherlands, with the most important sources being the Dutch Civil Code (*Burgerlijk Wetboek*) and the Dutch Financial Supervision Act (*Wet op het financieel toezicht*).

7.2 Securitisation Entities. Does your jurisdiction have laws specifically providing for establishment of special purpose entities for securitisation? If so, what does the law provide as to: (a) requirements for establishment and management of such an entity; (b) legal attributes and benefits of the entity; and (c) any specific requirements as to the status of directors or shareholders?

There are no such laws in the Netherlands. The legal form of a special purpose vehicle (***SPV***) tends to be a private company with limited liability (*besloten vennootschap*) and the shares of such an entity are customarily held by a foundation (*stichting*) whose sole purpose is to hold the shares in the SPV. A Dutch notary is required to incorporate both the SPV and the foundation and both have to be registered with the Dutch Chamber of Commerce (*Kamer van Koophandel*).

The companies are usually managed by an independent corporate services provider and, to protect the insolvency remoteness of the entities, various structural protections are used, including but not limited to: (i) restrictions on employees; (ii) restrictions on the companies' objects (as set out in the articles of association) to the specific securitisation transaction for which they are incorporated; (iii) ensuring any contracts they conclude contain limited recourse and non-petition provisions; and (iv) restrictions on financial indebtedness and creation of security, other than in relation to the specific securitisation transaction.

7.3 Location and form of Securitisation Entities. Is it typical to establish the special purpose entity in your jurisdiction or offshore? If in your jurisdiction, what are the advantages to locating the special purpose entity in your jurisdiction? If offshore, where are special purpose entities typically located for securitisations in your jurisdiction? What are the forms that the special purpose entity would normally take in your jurisdiction and how would such entity usually be owned?

Participants establish Securitisation Entities both in the Netherlands and offshore.

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The advantage of using the Netherlands is the relatively quick and cost-effective way to establish and maintain a Securitisation Entity. The Netherlands also has a favourable corporate law environment and a well-understood, efficient tax regime.

Offshore alternatives are typically Luxembourg and Ireland.

The vast majority of special purpose entities used in the Netherlands are private limited companies (*besloten vennootschap met beperkte aansprakelijkheid*) – a so-called Dutch "B.V.". Such entities are usually owned exclusively by an orphan entity in the form of a foundation (*stichting*) which is a corporate entity with no members or share capital but incorporated for a specific purpose. A foundation will typically hold all the issued share capital in the Dutch B.V. that is the Securitisation Entity.

7.4 Limited-Recourse Clause. Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) limiting the recourse of parties to that agreement to the available assets of the relevant debtor, and providing that to the extent of any shortfall the debt of the relevant debtor is extinguished?

In general, limited recourse provisions are valid and enforceable under Dutch law. Section 3:276 of the Dutch Civil Code (*Burgerlijk Wetboek*) states that a creditor has recourse to all assets of an obligor, unless otherwise provided by law or contract.

If the contract is governed by foreign law, a Dutch court would give effect to such contractual provisions in accordance with the rules of the chosen law.

7.5 Non-Petition Clause. Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) prohibiting the parties from: (a) taking legal action against the purchaser or another person; or (b) commencing an insolvency proceeding against the purchaser or another person?

Non-petition clauses are in principle valid and enforceable in the Netherlands. However, under Dutch law, the fact that a party has contractually agreed not to commence, or not to join any person in commencing, insolvency proceedings against another party will not result in such party having no legal standing to commence or join such proceedings. It is therefore possible that a Dutch court would deal with a petition for bankruptcy (*faillissement*) or suspension of payments (*surseance van betaling*) or preliminary suspension of payments in respect of a company, notwithstanding that such petition has been presented in breach of a non-petition clause. When dealing with such a petition, the court may conclude that a company has ceased to pay its debts as they fall due and declare the company bankrupt.

If the contract is governed by foreign law, a Dutch court would give effect to such contractual provisions in accordance with the rules of the chosen law.

7.6 Priority of Payments "Waterfall". Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) distributing payments to parties in a certain order specified in the contract?

A contractual provision setting out a payment "Waterfall" is valid in the Netherlands and enforceable as between the parties to that contract.

If the contract is governed by foreign law, a Dutch court would give effect to such contractual provisions in accordance with the rules of the chosen law.

7.7 Independent Director. Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) or a provision in a party's organisational documents prohibiting the directors from taking specified actions (including commencing an insolvency proceeding) without the affirmative vote of an independent director?

Under Dutch law, such a limitation on the powers of the directors would, in principle, be enforceable. If the directors take any action without the vote of the independent director, it could (but will not necessarily) lead to a damages claim from the company against them, notwithstanding that they acted in accordance with their duty to act in the best interests of the company.

7.8 Location of Purchaser. Is it typical to establish the purchaser in your jurisdiction or offshore? If in your jurisdiction, what are the advantages to locating the purchaser in your jurisdiction? If offshore, where are purchasers typically located for securitisations in your jurisdiction?

It is not typical for the purchaser to be located outside the Netherlands, although Ireland and Luxembourg are also sometimes chosen primarily for tax reasons. The reasons why purchasers are established onshore in the Netherlands is: (i) ease of incorporation in terms of costs and speed; (ii) a benign tax environment (and the ability in certain situations to obtain a tax ruling on certain tax aspects of the purchaser and the relevant transaction from the Dutch tax authorities); and (iii) the strength and depth of expertise of Dutch-based corporate service providers that are selected to manage a purchaser (and purchaser shareholders and the relevant security trustee).

8 Regulatory Issues

8.1 Required Authorisations, etc. Assuming that the purchaser does no other business in your jurisdiction, will its purchase and ownership or its collection and enforcement of receivables result in its being required to qualify to do business or to obtain any licence or its being subject to regulation as a financial institution in your jurisdiction? Does the answer to the preceding question change if the purchaser does business with more than one seller in your jurisdiction?

The Dutch Financial Supervision Act (*Wet op het financieel toezicht*) requires financial service providers, such as offerors and brokers of financial products including consumer loans, mortgage loans and any form of credit (together, ***Regulated Activities***), to obtain a licence from the Dutch Financial Markets Authority (*Autoriteit Financiële Markten*), which supervises licensed entities.

By acquiring consumer receivables which qualify as financial products, a purchaser is deemed to provide consumer credit, which is a Regulated Activity. If the purchaser is not a licensed credit institution, it can rely on an exemption from the licence requirement if it outsources the servicing and administration of the receivables to an entity which is adequately licensed under the Dutch Financial Supervision Act (*Wet op het financieel toezicht*).

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A servicing contract is usually entered into by the purchaser (if it is an SPV) with the originator (or any other party to which the originator had already outsourced the servicing and administration of the consumer receivables) pursuant to which the purchaser outsources the servicing and administration of such receivables to such party.

The answer above is not different if the purchaser does business with other sellers in the Netherlands.

8.2 Servicing. Does the seller require any licences, etc., in order to continue to enforce and collect receivables following their sale to the purchaser, including to appear before a court? Does a third-party replacement servicer require any licences, etc., in order to enforce and collect sold receivables?

See the answer to question 8.1 above. No additional or separate licence is required in order to enforce receivables or to appear before a Dutch court.

8.3 Data Protection. Does your jurisdiction have laws restricting the use or dissemination of data about or provided by obligors? If so, do these laws apply only to consumer obligors or also to enterprises?

As per 25 May 2018 the General Data Protection Regulation (*Algemene verordening gegevensbescherming*) (GDPR) enters into force. As of that date the same privacy regulations are effective across Europe.

8.4 Consumer Protection. If the obligors are consumers, will the purchaser (including a bank acting as purchaser) be required to comply with any consumer protection law of your jurisdiction? Briefly, what is required?

To protect the interests of consumers, there are certain limitations and restrictions in relation to loans advanced to consumers and the terms of the underlying contracts. The regulatory requirements set out in our answer to question 8.1 above are examples of the regulators imposing requirements on lenders to enhance consumer protection.

There are also more general consumer protection laws. For example, there are rules setting the maximum interest rate that can be charged to consumers, as well as rules allowing borrowers to make prepayments on their loan (and if such prepayments are subject to penalty fees, such fees are also regulated). For general consumer loans these rules are contained in the Decree on Credit Compensation (*Besluit Kredietvergoeding*). Furthermore, specific rules with respect to cold-calling, door-to-door selling and tied-selling may apply. If a party has been involved in "cold-calling" of consumers who are registered in the "Do-not-call-me" register or the lender does not comply with the requirements of the "Do-not-call-me" register, fines may be imposed by the regulator.

8.5 Currency Restrictions. Does your jurisdiction have laws restricting the exchange of your jurisdiction's currency for other currencies or the making of payments in your jurisdiction's currency to persons outside the country?

Under the Dutch Financial Supervision Act, entities performing exchange transactions in the course of their business qualify as an exchange office (*wisselinstelling*) and must be licensed.

In addition, under the External Financial Relations Act 1994 (*Wet financiële betrekkingen buitenland 1994*) and the Balance of Payments Reporting Instructions 2003 (*Rapportagevoorschriften betalingsbelansrapportages 2003*), the Dutch Central Bank may require certain entities to report to it in order to allow it to compile the national balance of payments, to ensure that monetary transactions between the Netherlands and other countries are recorded.

8.6 Risk Retention. Does your jurisdiction have laws or regulations relating to "risk retention"? How are securitisation transactions in your jurisdiction usually structured to satisfy those risk retention requirements?

There are no specific Dutch laws in relation to risk retention. Typically, the rules and regulations of the EU Capital Requirements Regulation (CRR) (and related technical standards, and implementing guidelines) apply to Dutch securitisation transactions where the risk retention rules prescribed by the CRR apply. Less common in the Netherlands are the US risk retention rules prescribed by the US Dodd-Frank Act which (like the CRR) apply to Dutch securitisation transactions in the circumstances prescribed by the relevant legislation. In certain circumstances, both EU and US risk retention rules may apply.

The most common method of satisfying the EU risk retention rules is for the risk retaining entity (usually the "originator") to hold the first loss/most junior notes or debt issued by the Securitisation Entity of the required level. Retaining risk through random exposures and vertical slices have also been seen in the Dutch market.

8.7 Regulatory Developments. Have there been any regulatory developments in your jurisdiction which are likely to have a material impact on securitisation transactions in your jurisdiction?

There are various European legislative initiatives that impact on securitisation generally, but no specific Dutch law initiatives.

9 Taxation

9.1 Withholding Taxes. Will any part of payments on receivables by the obligors to the seller or the purchaser be subject to withholding taxes in your jurisdiction? Does the answer depend on the nature of the receivables, whether they bear interest, their term to maturity, or where the seller or the purchaser is located? In the case of a sale of trade receivables at a discount, is there a risk that the discount will be recharacterised in whole or in part as interest? In the case of a sale of trade receivables where a portion of the purchase price is payable upon collection of the receivable, is there a risk that the deferred purchase price will be recharacterised in whole or in part as interest? If withholding taxes might apply, what are the typical methods for eliminating or reducing withholding taxes?

Payments on receivables by the obligors to the seller or the purchaser are not subject to withholding taxes in the Netherlands (exceptions may apply if the receivables have equity-like characteristics, which is unlikely in cases of trade or mortgage receivables).

The Government has announced that it intends to introduce a withholding tax on interest as per 1 January 2021. It has been stated that such withholding tax will apply only to interest payments made

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to related entities that are tax resident in a low-tax jurisdiction, or a jurisdiction that is on the EU list of non-cooperative jurisdictions. Consequently, (deemed) interest payments received by seller or purchaser in respect of receivables from third-party obligors and interest (deemed to be) paid by the purchaser to third-party creditors are not expected to be subject to withholding tax if the new legislation is introduced.

9.2 Seller Tax Accounting. Does your jurisdiction require that a specific accounting policy is adopted for tax purposes by the seller or purchaser in the context of a securitisation?

No specific tax accounting policy is required. Depending on the structuring of the securitisation, the seller may treat the securitisation vehicle as an agent for corporate income tax (and VAT) purposes to avoid gain recognition (rather than being considered to act as principal counterparty under the receivables).

9.3 Stamp Duty, etc. Does your jurisdiction impose stamp duty or other transfer or documentary taxes on sales of receivables?

No stamp duty or other documentary taxes apply on sales of receivables.

9.4 Value Added Taxes. Does your jurisdiction impose value added tax, sales tax or other similar taxes on sales of goods or services, on sales of receivables or on fees for collection agent services?

Collection agent services are normally not subject to VAT. Where collection agent services (are deemed to) relate to non-performing receivables, such services may be subject to VAT. If the purchaser were to be considered to provide factoring services to the seller (which is normally not the case with securitisations), such factoring services would be subject to VAT.

It is noted that if the securitisation vehicle is considered an agent of the originator for VAT purposes, it should not be considered to receive any supply of (collection agent or other) services.

9.5 Purchaser Liability. If the seller is required to pay value-added tax, stamp duty or other taxes upon the sale of receivables (or on the sale of goods or services that give rise to the receivables) and the seller does not pay, then will the taxing authority be able to make claims for the unpaid tax against the purchaser or against the sold receivables or collections?

The purchaser cannot be held liable for any VAT due by the seller (exceptions apply in fraudulent situations).

The right to claim any bad debt relief for VAT purposes transfers to the purchaser upon transfer of the receivables.

The transfer of receivables from the seller to the purchaser should not normally affect the seller's rights to deduct input VAT.

9.6 Doing Business. Assuming that the purchaser conducts no other business in your jurisdiction, would the purchaser's purchase of the receivables, its appointment of the seller as its servicer and collection agent, or its enforcement of the receivables against the obligors, make it liable to tax in your jurisdiction?

If the purchaser is not a Netherlands tax resident entity and does not otherwise have a permanent establishment in the Netherlands, it is not liable to tax in the Netherlands. Netherlands tax resident purchasers will generally not become liable to tax, other than corporate income tax over a nominal fee.

9.7 Taxable Income. If a purchaser located in your jurisdiction receives debt relief as the result of a limited recourse clause (see question 7.3 above), is that debt relief liable to tax in your jurisdiction?

Any reduction of the purchaser's debt, including debt relief as set out in question 7.4 above, is in principle a taxable event for Netherlands corporate income tax purposes. As the purchaser normally suffers an equivalent (deductible) loss on its assets (triggering the debt relief under the limited recourse clause), the gain on the debt relief generally does not lead to a net tax liability for the purchaser.

Depending on the structuring of the securitisation, the seller may keep the underlying assets, and the notes, on its own tax balance sheet (in other words, treat the securitisation vehicle as an agent for corporate income tax purposes). Any debt relief as set out in question 7.4 above should in such case not have any corporate income tax consequences for the purchaser at all.

Acknowledgment

With thanks to tax partner Eelco van der Stok (Email: Eelco.vanderstok@freshfields.com) and senior tax associate Bob van Kasteren (Email: bob.vankasteren@freshfields.com), both at Freshfields Bruckhaus Deringer in Amsterdam, for providing answers to the tax sections of the article.

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The Amsterdam structured finance practice is a key name in the Dutch market. Mandeep advises participants on a variety of asset-based transactions, including ABS, CLOs, as well as various forms of corporate receivables financings and working capital solutions, often involving multiple jurisdictions. Recently, Mandeep has been advising on the acquisition, origination and/or funding of loan portfolio transactions, including standalone businesses, as well as discrete loan pools.

Mandeep started his career at the firm's London office as an English qualified lawyer, and moved to Amsterdam in 2004 and became a partner in 2012. He has built up an unusually high level of knowledge of the Benelux market on top of his UK experience. This combination of UK and continental expertise, together with his general banking and finance experience, makes Mandeep stand out.

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Our securitisation and structured finance team in the Netherlands is a key name in the Dutch structured finance market. It was recently awarded a Tier 1 ranking for Structured Finance and Securitisation by the *IFLR 1000*, 2017 Edition. The team focuses on innovative projects and a number of the recent deals we have been involved in have been recognised as benchmarks to the Dutch market. The team is also known for offering clients both a Dutch and English law structured finance capability on the ground in Amsterdam. We primarily act for Dutch, UK, European and US-based financial institutions, private equity houses and corporations, often with a multi-jurisdictional angle.

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Portugal

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1 Receivables Contracts

1.1 Formalities. In order to create an enforceable debt obligation of the obligor to the seller: (a) is it necessary that the sales of goods or services are evidenced by a formal receivables contract; (b) are invoices alone sufficient; and (c) can a binding contract arise as a result of the behaviour of the parties?

The legal requirements applicable to the form of a contract between a seller and an obligor depend to a large extent on the nature of the contract (e.g. if it is a loan agreement made by a bank to a customer, an agreement between a utility company and a customer, etc.). As an example, the general rule applicable to the granting of credit facilities to consumers is that the relevant contract has to be in writing.

The general civil law principle, however, (i.e. the rule which applies by default whenever there is no specific rule applicable to a certain type of contractual relationship), is that there is no generally prescribed applicable formality for contracts to be entered into, and therefore a valid contractual relationship for the sale of goods and services can even be established orally (unless otherwise stated in a specific legal provision), and in those circumstances the existence of an invoice is naturally also sufficient to document the relevant contract.

In order for a receivables contract to be deemed to exist as a result of the parties' behaviour alone, it has to be possible to conclude, based solely on the parties' actions, that their intention was to enter into a contract. In other words, the parties' behaviour has to be, for all purposes, equivalent to a contractual statement.

1.2 Consumer Protections. Do your jurisdiction's laws: (a) limit rates of interest on consumer credit, loans or other kinds of receivables; (b) provide a statutory right to interest on late payments; (c) permit consumers to cancel receivables for a specified period of time; or (d) provide other noteworthy rights to consumers with respect to receivables owing by them?

A. Interest Rate

As a general rule, the Portuguese Civil Code foresees a legal interest rate. This rate is currently set at 4 per cent. Any stipulation of an interest rate superior to the legal rate must be made in writing. Also, stipulated rates may not exceed the legal interest rate by more than three per cent (if the obligation is secured) and by more than five per cent (if it is not). Interest stipulated over these limits is deemed reduced to the aforementioned maximum rates.

The general rules described in the previous paragraph do not apply to credit institutions. However, in accordance with the Portuguese legal framework for consumer credit (Decree-Law no. 133/2009 of 2 June 2009 (as amended and currently in force), implementing Directive 2008/48/CE on consumer credit agreements), the Annual Percentage Rate of Charge charged by credit institutions to consumers (including in relation to leasing transactions) is limited to a three-month average disclosed by the Bank of Portugal plus a quarter of that average. For the first trimester of 2018, the maximum Annual Percentage Rate of Charge for consumer credit disclosed by the Bank of Portugal is: (i) 13.6 per cent for personal loans (other than loans for specific purposes such as health or education, or financial leases of equipment); (ii) 16.4 per cent for credit cards, credit lines, current accounts or overdraft facilities; (iii) between 5.2 and 6.3 per cent for leasing automobile loans (depending on whether the vehicle is new or used); and (iv) between 9.7 and 12.3 per cent for automobile loans with retention of title (depending on whether the vehicle is new or used). Decree-Law no. 133/2009, as amended from time to time, limits the maximum Annual Percentage Rate of Charge for consumer credit regarding (i) personal loans (other than loans for specific purposes such as health or education, or financial leases of equipment) to 17.9 per cent, and (ii) credit cards, credit lines, current accounts or overdraft facilities to 21.3 per cent.

B. Delay Interest

As a general rule, the Portuguese Civil Code applies delay interest. As per (A) above, the legal delay interest rate is set at four per cent, except if the remuneratory interest (i.e. interest charged under (A) above) is higher, or if the parties agree on a higher delay interest rate. Similar to (A) above, stipulated delay interest rates may not exceed the legal delay interest rate by more than seven per cent (if the obligation is secured) or by more than nine per cent (if it is not). Delay interest stipulated over these limits is deemed to be reduced accordingly.

However, under the Portuguese Commercial Code and Ministerial Order no. 277/2013 of 26 August 2013, where the creditor is a commercial company (which may be a legal or a natural person, for instance an individual merchant acting as such) a special delay interest rate applies. At the moment, this rate for the first semester 2018 is set at seven per cent. Also, under the new framework for payment delays in commercial transactions, approved by Decree-Law no. 62/2013 of 10 May 2013 and Ministerial Order no. 277/2013 of 26 August 2013, all payments made as remuneration of commercial transactions are subject to a special delay interest rate which, for the first semester 2017, is currently set at eight per cent.

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With regard to credit institutions, there is a special framework approved by Decree-Law no. 58/2013 of 8 May 2013, which also limits the delay interest rate which may be charged. In accordance with this special framework, credit institutions may stipulate delay interest rates of up to three per cent over the rate applicable to the transaction, which covers principal overdue and not yet paid.

C. Termination

There is, in most circumstances, an unconditional right to terminate the receivables contract during the initial 14 days after execution, in which case the advanced amount is given back to the lender and the contractual relationship terminates, but the financial institution may not charge any additional fees with regard to the termination.

D. Acceleration

Under the Portuguese consumer credit legal framework, financial institutions may only carry out the acceleration of defaulted loans (or terminate the relevant agreement) when more than two instalments (totalling more than 10 per cent of the entire amount outstanding) are due and only following notification to the debtor to that effect, granting him at least 15 days to pay the amounts due and expressly warning him of the possibility of accelerating the loan. Other rights mostly relate to information and contents obligations, the right to render the contract void or voidable if information is not provided, etc.

1.3 Government Receivables. Where the receivables contract has been entered into with the government or a government agency, are there different requirements and laws that apply to the sale or collection of those receivables?

Public procurement rules may apply. If the government is acting under private law, it should not have special prerogatives. In any case, specific rules may apply in relation to issues such as the validity of a delegation of powers.

2 Choice of Law – Receivables Contracts

2.1 No Law Specified. If the seller and the obligor do not specify a choice of law in their receivables contract, what are the main principles in your jurisdiction that will determine the governing law of the contract?

If the parties fail to specify the law chosen to govern the receivables contract, it should first be considered whether EC Regulation no. 593/2008 ("Rome I Regulation") or the Rome Convention on the law applicable to contractual obligations ("Rome Convention") apply to the relevant conflict.

If the Rome I Regulation or the Rome Convention apply, then Article 4 and, to the extent applicable, Articles 5 to 7 of the Rome I Regulation shall determine the governing law.

If neither the Rome I Regulation nor the Rome Convention apply, the main principles of Portuguese law in relation to the governing law of contracts determine that contracts are governed by the law which the parties considered when executing the contract (even if they have not expressly stated it), or, if this is impossible to determine (i.e. the parties' behaviour is not conclusive in this respect), the law applicable in the place where the parties have their domicile (or, if the parties are domiciled in different jurisdictions, the law of the place where the contract was entered into).

2.2 Base Case. If the seller and the obligor are both resident in your jurisdiction, and the transactions giving rise to the receivables and the payment of the receivables take place in your jurisdiction, and the seller and the obligor choose the law of your jurisdiction to govern the receivables contract, is there any reason why a court in your jurisdiction would not give effect to their choice of law?

If all of the relevant aspects of the receivables contract have a connection with Portugal, there is no reason why a Portuguese court would not give effect to the parties' choice of Portuguese law as the law governing the contract. Please note, however, that there may be mandatory provisions of law in other jurisdictions requiring certain aspects of a contract to be governed by such law (for instance, if the transaction at stake pertains to, or is secured by, real estate property located in another jurisdiction).

2.3 Freedom to Choose Foreign Law of Non-Resident Seller or Obligor. If the seller is resident in your jurisdiction but the obligor is not, or if the obligor is resident in your jurisdiction but the seller is not, and the seller and the obligor choose the foreign law of the obligor/seller to govern their receivables contract, will a court in your jurisdiction give effect to the choice of foreign law? Are there any limitations to the recognition of foreign law (such as public policy or mandatory principles of law) that would typically apply in commercial relationships such as that between the seller and the obligor under the receivables contract?

If the Rome I Regulation or the Rome Convention apply, then Article 3 of the Rome I Regulation and Article 3 of the Rome Convention would allow the parties to choose a governing law. This choice would be subject to the limitations set out in the Rome I Regulation. Of these limitations, we believe those applicable to consumer contracts are probably those which would be more likely to apply in the context of a receivables contract, i.e. if the obligor is a consumer. Limitations in relation to public policy and mandatory principles of law also apply, but they would be less typical.

If the Rome I Regulation or the Rome Convention do not apply, the general principle in Portugal is that the parties may elect the governing law applicable. However, there are certain circumstances in which the parties are not entirely free to choose the law applicable to the whole, or part, of the contract. The parties may not choose foreign law with the intent of fraudulently avoiding Portuguese law. Furthermore, the choice of foreign law may not offend Portuguese international public policy.

Also, regardless of the applicability of the Rome I Regulation or the Rome Convention, if the obligor is resident in Portugal and to the extent that the receivables agreement could be deemed to include general contractual clauses (i.e. those which the obligor may only accept without prior individual negotiation), the choice of foreign law is likely not to preclude the full application of the provisions of Portuguese law on general contractual clauses.

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3 Choice of Law – Receivables Purchase Agreement

3.1 Base Case. Does your jurisdiction's law generally require the sale of receivables to be governed by the same law as the law governing the receivables themselves? If so, does that general rule apply irrespective of which law governs the receivables (i.e., your jurisdiction's laws or foreign laws)?

Portuguese law does not generally require that an assignment of receivables is governed by the same law which governs the assigned receivables. However, in our experience (and that of the Portuguese authorities) assignment agreements for Portuguese-originated receivables have usually been governed by Portuguese law.

In any case, given Article 14 of the Rome I Regulation (and, when the Rome I Regulation does not apply, the risk that a Portuguese court would attempt to enforce a solution similar to that which is set out therein), the parties to an assignment of Portuguese-originated receivables should comply with the obligor notification procedures set out in the Portuguese Civil Code (to the extent not covered by the exemption of notification procedures set out in the Securitisation Law).

3.2 Example 1: If (a) the seller and the obligor are located in your jurisdiction, (b) the receivable is governed by the law of your jurisdiction, (c) the seller sells the receivable to a purchaser located in a third country, (d) the seller and the purchaser choose the law of your jurisdiction to govern the receivables purchase agreement, and (e) the sale complies with the requirements of your jurisdiction, will a court in your jurisdiction recognise that sale as being effective against the seller, the obligor and other third parties (such as creditors or insolvency administrators of the seller and the obligor)?

We see no reason for a Portuguese court not to recognise the effectiveness of the assignment in this scenario, be it against the seller or against the obligor. The same may be said with regard to effectiveness towards the relevant third parties.

3.3 Example 2: Assuming that the facts are the same as Example 1, but either the obligor or the purchaser or both are located outside your jurisdiction, will a court in your jurisdiction recognise that sale as being effective against the seller and other third parties (such as creditors or insolvency administrators of the seller), or must the foreign law requirements of the obligor's country or the purchaser's country (or both) be taken into account?

From a Portuguese law perspective, we understand that if the obligor and/or the purchaser were located outside Portugal it would not cause a Portuguese court to decide differently from Example 1. However, any mandatory foreign law requirements would need to be complied with.

3.4 Example 3: If (a) the seller is located in your jurisdiction but the obligor is located in another country, (b) the receivable is governed by the law of the obligor's country, (c) the seller sells the receivable to a purchaser located in a third country, (d) the seller and the purchaser choose the law of the obligor's country to govern the receivables purchase agreement, and (e) the sale complies with the requirements of the obligor's country, will a court in your jurisdiction recognise that sale as being effective against the seller and other third parties (such as creditors or insolvency administrators of the seller) without the need to comply with your jurisdiction's own sale requirements?

In this scenario, if the assignment is valid under its governing law, we believe that a Portuguese court would recognise the sale as effective against the seller and any relevant third parties.

3.5 Example 4: If (a) the obligor is located in your jurisdiction but the seller is located in another country, (b) the receivable is governed by the law of the seller's country, (c) the seller and the purchaser choose the law of the seller's country to govern the receivables purchase agreement, and (d) the sale complies with the requirements of the seller's country, will a court in your jurisdiction recognise that sale as being effective against the obligor and other third parties (such as creditors or insolvency administrators of the obligor) without the need to comply with your jurisdiction's own sale requirements?

In this scenario, we also believe that a Portuguese court would recognise the sale as being effective, subject to the considerations made in the next few paragraphs.

If the obligor is a consumer and either the Rome I Regulation or Rome Convention apply, the choice of the seller's country to govern the receivables agreement may not deprive the obligor of the protection granted by mandatory provisions of Portuguese law. We understand that the debtor notification requirements of the Portuguese Civil Code (when not waived by the application of the Securitisation Law) are mandatory provisions protecting the debtor and that, as such, the level of debtor protection enshrined in them must be met either by directly applying Portuguese law or provisions of the law of the seller's country which provide the same level of protection.

If the obligor is a consumer and the Rome I Regulation and Rome Convention do not apply, we still believe that the reasoning of the previous paragraph should apply, as we understand that there would be a risk that a Portuguese court may attempt to enforce a similar solution.

If the obligor is not a consumer, the assignment may be deemed valid if the obligor notification procedures mandated by the law governing the receivables agreement are followed.

In any case and from a risk mitigating perspective, we would recommend that all assignments of receivables owed by Portuguese resident entities be notified to the debtor in writing.

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3.6 Example 5: If (a) the seller is located in your jurisdiction (irrespective of the obligor's location), (b) the receivable is governed by the law of your jurisdiction, (c) the seller sells the receivable to a purchaser located in a third country, (d) the seller and the purchaser choose the law of the purchaser's country to govern the receivables purchase agreement, and (e) the sale complies with the requirements of the purchaser's country, will a court in your jurisdiction recognise that sale as being effective against the seller and other third parties (such as creditors or insolvency administrators of the seller, any obligor located in your jurisdiction and any third party creditor or insolvency administrator of any such obligor)?

If either the Rome I Regulation or Rome Convention apply, we believe that Portuguese courts would, under Articles 3 and 14 of the Rome I Regulation, recognise the choice of foreign law regarding the sale of the assets and would, as such, have no reason not to deem the sale effective against the seller. The same result would be achieved if neither the Rome I Regulation nor the Rome Convention applied, in this case through the application of the general principle of the Portuguese Civil Code under which the parties are free to elect a governing law.

As for effectiveness against the obligor, if the receivable is governed by Portuguese law then the obligor is entitled to the protection granted to debtors by the mandatory provisions of Portuguese law applicable to assignments of receivables. As such, we would recommend that the debtor notification requirements of the Portuguese Civil Code (when not waived by the application of the Securitisation Law) are met in relation to the obligor.

4 Asset Sales

4.1 Sale Methods Generally. In your jurisdiction what are the customary methods for a seller to sell receivables to a purchaser? What is the customary terminology – is it called a sale, transfer, assignment or something else?

In the context of securitisation, the customary method for a seller to sell receivables to a purchaser is under the framework of the Securitisation Law, approved by Decree-Law no. 453/99 of 5 November 1999, as amended from time to time (the "**Securitisation Law**"). The Securitisation Law has implemented a specific securitisation legal framework in Portugal, which contains a simplified process for the assignment of credits for securitisation purposes. In fact, the sale of credits for securitisation is effected by way of assignment of credits, such being the customary terminology, consisting of a true sale of receivables under the Securitisation Law as the purchaser is the new legal owner of the receivables. It corresponds to a perfected sale of receivables; however, please note the specifics relating to exercise of set-off against the securitisation vehicle below.

4.2 Perfection Generally. What formalities are required generally for perfecting a sale of receivables? Are there any additional or other formalities required for the sale of receivables to be perfected against any subsequent good faith purchasers for value of the same receivables from the seller?

There are no specific formality requirements for an assignment of credits under the Securitisation Law, a written private agreement between the parties being sufficient for a valid assignment to occur (including an assignment of loans with underlying mortgages or other guarantees subject to registration under Portuguese law). Transfer by means of a notarial deed is not required. In the case of an assignment of mortgage loans, the signatures to the assignment contract must be certified by a notary public, lawyer or the company secretary of each party under the terms of the Securitisation Law, such certification being required for the registration of the assignment at the relevant Portuguese Real Estate Registry Office.

Additionally, the assignment of any security over real estate, or of an asset subject to registration, in Portugal is only effective against third parties acting in good faith further to the registration of such assignment with the competent registry by, or on behalf of, the assignee. The assignee is entitled under the Securitisation Law to effect such registration.

In accordance with Article 6 of the Securitisation Law, the assignment of the relevant assets becomes immediately valid and effective between the parties upon the execution of the relevant assignment agreement and, when the assignor is, *inter alia*, a credit institution or a financial company, irrespective of the debtor's consent, notification or awareness.

When such is not the case, and in relation to the effectiveness of the assignment as far as the relevant debtors are concerned, the general rule is that a notification is required for the assignment to become effective, following the general principle under Article 583 of the Portuguese Civil Code.

In what concerns securitisation transactions, we should also mention that the Portuguese Securities Market Commission (the "**CMVM**") also grants an approval to the sale and allocates a 20-digit asset code to the bulk of receivables which constitute the asset portfolio being securitised. Please refer to our answers to questions 7.1 and 7.2 below.

4.3 Perfection for Promissory Notes, etc. What additional or different requirements for sale and perfection apply to sales of promissory notes, mortgage loans, consumer loans or marketable debt securities?

As mentioned in the answer to question 4.2 above, in order to perfect an assignment of mortgage loans and ancillary mortgage rights which are capable of registration at a public registry against third parties, the assignment must be followed by the corresponding registration of the transfer of such mortgage loans and ancillary mortgage rights in the relevant Real Estate Registry Office.

The Portuguese real estate registration provisions allow for the registration of the assignment of any mortgage loan at any Portuguese Real Estate Registry Office, even if the said Portuguese Real Estate Registry Office is not the office where such mortgage loan is registered, given the existence of a centralised and integrated registration system. The registration of the transfer of the mortgage loans requires the payment of a fee for each such mortgage loan.

In what concerns promissory notes ("*livranças*"), the usual practice is for these to be blank promissory notes in relation to which the originator has obtained from a borrower a completion pact ("*pacto de preenchimento*"), which grants the originator the power to complete the promissory note. In order to perfect the assignment of such promissory notes to the assignee, the assignor will have to endorse and deliver these instruments to the assignee.

The assignment of marketable debt instruments is perfected by the update of the corresponding registration entries in the relevant securities accounts, in accordance with the Portuguese Securities Code.

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4.4 Obligor Notification or Consent. Must the seller or the purchaser notify obligors of the sale of receivables in order for the sale to be effective against the obligors and/or creditors of the seller? Must the seller or the purchaser obtain the obligors' consent to the sale of receivables in order for the sale to be an effective sale against the obligors? Whether or not notice is required to perfect a sale, are there any benefits to giving notice – such as cutting off obligor set-off rights and other obligor defences?

As to the effectiveness of the assignment between the parties, please refer to our answer to question 4.2 above.

Article 6/1 of the Securitisation Law establishes a general rule pursuant to which the assignment of the receivables becomes effective towards the obligors upon notification of the sale of the receivables. However, a relevant exception applies under Article 6/4 of the Securitisation Law, whereby the assignment of receivables becomes immediately valid and effective between the parties and towards the obligors upon the execution of the relevant assignment agreement, irrespective of the obligor's consent, notification or awareness, when the assignor is, *inter alia*, a credit institution or a financial company.

Please note that notification to the obligors is generally required, even in the case of Article 6/4 of the Securitisation Law (as described above), when the servicer of the receivables is not the assignor of the receivables.

Please note that in cases where the relevant receivables contract expressly requires the consent or notification of the obligors, then such consent or notice is required in order for the assignment to be effective against such obligors.

Under Article 6/6 of the Securitisation Law, any set-off rights or other means of defence exercisable by the obligors against the assignee are crystallised or cut-off on the relevant date the assignment becomes effective, (i) regardless of notification when such notice is dispensed as above, or (ii) upon notification or awareness of the debtor when such is required.

4.5 Notice Mechanics. If notice is to be delivered to obligors, whether at the time of sale or later, are there any requirements regarding the form the notice must take or how it must be delivered? Is there any time limit beyond which notice is ineffective – for example, can a notice of sale be delivered after the sale, and can notice be delivered after insolvency proceedings have commenced against the obligor or the seller? Does the notice apply only to specific receivables or can it apply to any and all (including future) receivables? Are there any other limitations or considerations?

When applicable, notification to the debtor is required to be made by means of a registered letter (to be sent to the debtor's address included in the relevant receivables contract) and such notification will be deemed to have occurred on the third business day following the date of posting of the registered letter.

An exception to this requirement applies when the assignment of credits is made under the Securitisation Law as described in the answer to question 4.2 above.

There is no applicable time limit to the delivery of notice to the obligors, taking into account in any case that, if no exception applies, the assignment shall only be effective towards the obligors upon delivery of the relevant notice. The notice can be delivered after commencement of any insolvency proceedings against the obligor or against the seller, and the contractual documents for securitisation transactions usually include provisions to allow the assignee to be able to notify all the obligors in case the seller/assignor does not do so.

When required, notice of assignment of credits must be given to each obligor, even though notice may be given for future credits.

4.6 Restrictions on Assignment – General Interpretation. Will a restriction in a receivables contract to the effect that "None of the [seller's] rights or obligations under this Agreement may be transferred or assigned without the consent of the [obligor]" be interpreted as prohibiting a transfer of receivables by the seller to the purchaser? Is the result the same if the restriction says "This Agreement may not be transferred or assigned by the [seller] without the consent of the [obligor]" (i.e., the restriction does not refer to rights or obligations)? Is the result the same if the restriction says "The obligations of the [seller] under this Agreement may not be transferred or assigned by the [seller] without the consent of the [obligor]" (i.e., the restriction does not refer to rights)?

In the first example, we are addressing an assignment of receivables and such assignment is dependent on obtaining the obligor's consent. Unless the consent of the obligor is obtained, the receivables are not eligible for securitisation purposes under Portuguese law, given that Article 4/1/a) of the Securitisation Law establishes that receivables subject to restrictions on their transferability or assignment are not eligible for securitisation purposes. This is the case due to the true sale nature of the assignment of receivables under the Securitisation Law. If such obligor's consent is not obtained, this means that the receivables contracts governing the receivables to be assigned cannot include such receivables or subject them to restrictive provisions as to their ownership transferability. Please refer to our answer to question 4.9 below.

On the other hand, the wording of the second example addresses a situation of assignment of contractual position (in accordance with Article 424 of the Portuguese Civil Code) and not merely an assignment of credits arising thereunder. The assignment of a contractual position requires the consent of the other counterparty, and if such consent has been given prior to the assignment, it requires notification thereof to the counterparty.

If the restriction refers only to the seller's obligations under the receivables contract, the receivables are also not eligible for securitisation purposes under Portuguese law, given that Article 4/1/a) of the Securitisation Law establishes that receivables subject to restrictions on the transferability or assignment are not eligible for securitisation purposes.

4.7 Restrictions on Assignment; Liability to Obligor. If any of the restrictions in question 4.6 are binding, or if the receivables contract explicitly prohibits an assignment of receivables or "seller's rights" under the receivables contract, are such restrictions generally enforceable in your jurisdiction? Are there exceptions to this rule (e.g., for contracts between commercial entities)? If your jurisdiction recognises restrictions on sale or assignment of receivables and the seller nevertheless sells receivables to the purchaser, will either the seller or the purchaser be liable to the obligor for breach of contract or tort, or on any other basis?

Restrictions on assignment existing in the underlying receivables contracts, including the restrictions mentioned in the answer to

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question 4.6 above, are enforceable in Portugal. However, in relation to any contractual prohibitions for assignment of credits, these can only be effective towards the assignee if it was aware of such prohibition on the assignment date, as set out in Article 577 of the Portuguese Civil Code. If a given receivables contract comprises such a contractual prohibition on assignment and nevertheless the seller assigns the receivables to a third party, then the seller will be liable towards the obligor for breach of contract, i.e., wilful default ("*incumprimento culposo*") of an obligation, in accordance with the provisions of the Portuguese Civil Code.

4.8 Identification. Must the sale document specifically identify each of the receivables to be sold? If so, what specific information is required (e.g., obligor name, invoice number, invoice date, payment date, etc.)? Do the receivables being sold have to share objective characteristics? Alternatively, if the seller sells *all* of its receivables to the purchaser, is this sufficient identification of receivables? Finally, if the seller sells *all* of its receivables *other than* receivables owing by one or more specifically identified obligors, is this sufficient identification of receivables?

The assignment agreement must identify, specifically, the receivables which are being assigned under a given contract, given that the object of the assignment must be determinable in accordance with the Portuguese Civil Code, such usually being done by listing the relevant receivables in a schedule to the assignment agreement. Such list of assigned receivables refers to standard characteristics of the relevant credits, without disclosing personal data of the obligors which would allow their identification, in accordance with the applicable data protection rules.

Under the Securitisation Law, bulk assignments are not considered and the seller will not assign all of its undetermined receivables to a given purchaser (or all of its receivables other than a few identified receivables), rather identifying those receivables to be actually assigned and which comply with the Securitisation Law eligibility criteria.

4.9 Recharacterisation Risk. If the parties describe their transaction in the relevant documents as an outright sale and explicitly state their intention that it be treated as an outright sale, will this description and statement of intent automatically be respected or is there a risk that the transaction could be characterised by a court as a loan with (or without) security? If recharacterisation risk exists, what characteristics of the transaction might prevent the transfer from being treated as an outright sale? Among other things, to what extent may the seller retain any of the following without jeopardising treatment as an outright sale: (a) credit risk; (b) interest rate risk; (c) control of collections of receivables; (d) a right of repurchase/redemption; (e) a right to the residual profits within the purchaser; or (f) any other term?

The assignment of the receivables under a receivables sale agreement is generally construed to constitute a valid and true assignment of receivables from an originator to the assignee, being effective between the parties as from the envisaged effective date and whereby the seller is discharged of all its obligations with respect to the receivables comprised in the securitisation pool.

We note that the Securitisation Law requires a true and complete assignment, not being subject to any term or condition. Furthermore, neither the originating entity, nor any of its group companies, may provide any guarantees or enhancement in the context of the assignment or undertake responsibility for payments made by the underlying obligors. As such, the seller retaining credit risk, interest rate risk or control of collections (for its own benefit) or a right of repurchase or a right to residual profits, could be seen as colliding with such true sale concept.

In what concerns the control of collections, we would note additionally that, where the seller is a credit institution in the context of a securitisation, usually the purchaser mandates such seller to act as collection account bank and servicer of the receivables and ensure receipt of collections from the borrowers on behalf of the purchaser, it being clear, however, that any amounts so held by the servicer do not pertain to the servicer (even in a servicer event) and rather belong to the purchaser, in accordance with the Securitisation Law. In this sense, an assignment under the Securitisation Law will typically be a perfected assignment. In terms of repurchase, we would note that the seller would typically have an obligation under the Securitisation Law of repurchase in case of hidden defects or false representations and warranties relating to the assets.

4.10 Continuous Sales of Receivables. Can the seller agree in an enforceable manner to continuous sales of receivables (i.e., sales of receivables as and when they arise)? Would such an agreement survive and continue to transfer receivables to the purchaser following the seller's insolvency?

Without prejudice to the answer to question 4.11 below regarding future receivables, continuous sales would be possible under the Securitisation Law, provided they are in compliance with the answer to question 4.7 above. However, sellers have rather opted to carry out securitisation transactions with revolving periods for assignment of additional receivables on a periodic basis, against payment out of collections and additional funding by the issuance of further notes, rather than continuous sales.

4.11 Future Receivables. Can the seller commit in an enforceable manner to sell receivables to the purchaser that come into existence after the date of the receivables purchase agreement (e.g., "future flow" securitisation)? If so, how must the sale of future receivables be structured to be valid and enforceable? Is there a distinction between future receivables that arise prior to *versus* after the seller's insolvency?

Pursuant to Article 4/3 of the Securitisation Law, future receivables may be assigned for securitisation purposes, provided such receivables (i) arise from existing relationships, and (ii) are quantifiable (a confirmation of the estimations made by the originator in respect of the quantum of the future receivables that are being securitised usually being sought). In terms of structure, the originator will assign to the purchaser certain rights over the future receivables, in an amount equivalent to a given overcollateralised percentage of the debt service and the originator will guarantee that the future receivables generated during each collection period will be sufficient to cover the agreed debt service and, accordingly, for each interest period it will transfer to the purchaser an amount equivalent to 100 per cent of the debt service in respect of such interest period. Furthermore, in case the originator is unable to originate sufficient future receivables to meet its obligations for a given interest period, it will, in any event, pay to the purchaser an amount equal to such shortfall of future receivables, in order to ensure an amount equal to 100 per cent of the relevant debt service.

In respect of insolvency, we refer to our answer to question 6.5 below.

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4.12 Related Security. Must any additional formalities be fulfilled in order for the related security to be transferred concurrently with the sale of receivables? If not all related security can be enforceably transferred, what methods are customarily adopted to provide the purchaser the benefits of such related security?

Under the Portuguese Civil Code, the general rule is that the assignment of credits also implies the transfer of any kind of security or other form of guarantee, unless the relevant assignment agreement provides otherwise. If certain formalities apply to the creation of security, such formalities also usually need to be complied with for a valid transfer of security. Please see our answers to questions 4.2 and 4.3 regarding the transfer of mortgages under the Securitisation Law and the answer to question 5.5.

4.13 Set-Off; Liability to Obligor. Assuming that a receivables contract does not contain a provision whereby the obligor waives its right to set-off against amounts it owes to the seller, do the obligor's set-off rights terminate upon its receipt of notice of a sale? At any other time? If a receivables contract does not waive set-off but the obligor's set-off rights are terminated due to notice or some other action, will either the seller or the purchaser be liable to the obligor for damages caused by such termination?

Under the Securitisation Law and the general rule of the Portuguese Civil Code, an obligor may claim any right of set-off (and, in general, any means of defence) against the purchaser of the receivables in the same terms it could be claimed against the seller, if such right of set-off arises from a fact which has occurred prior to the assignment of the relevant receivable. Such right of set-off is not terminated by any notice of assignment. However, where the right of set-off arises from a fact occurring after the assignment of the relevant underlying receivable, the obligor cannot claim the set-off against the amounts owed and neither the purchaser nor the seller shall be liable towards the obligor for damages. As such, the date of assignment is the cut off or crystallisation date for the purposes of defining which are the exercisable set-off or any other means of defence.

4.14 Profit Extraction. What methods are typically used in your jurisdiction to extract residual profits from the purchaser?

There are several methods used in Portuguese securitisation transactions for the extraction of residual profits from the transaction and the purchaser/issuer of securitised securities, all being related to the use of the so-called payments waterfall to be paid from the transaction account (opened with an accounts bank in the name of the SPV) to the relevant receiver.

We would say the most usual method for profit extraction is the establishment of a junior note that covers, under the payments waterfall, all amounts remaining in the transaction account after payment of all transaction expenses, issuer expenses and interest and principal on the outstanding senior notes until they are redeemed in full. In this case, the junior noteholder is entitled to all remaining and residual amounts standing to the credit of the SPV. Another common way for profit extraction is the establishment, under the relevant transaction documents, of fees to be paid to the relevant receiver for their role/commitment within the context of the securitisation transaction.

If no profit extraction mechanics are put in place and agreed between the parties under the securitisation transaction documents, any excess and residual amounts are paid out in the payments waterfall, by a return amount concept with a catch-all nature.

5 Security Issues

5.1 Back-up Security. Is it customary in your jurisdiction to take a "back-up" security interest over the seller's ownership interest in the receivables and the related security, in the event that an outright sale is deemed by a court (for whatever reason) not to have occurred and have been perfected (see question 4.9 above)?

Back-up security in the context of the Securitisation Law is not customary in Portugal, considering that noteholders and secured creditors benefit from the legal creditors' privilege set forth in Article 63 of the Securitisation Law, which covers the transactions assets located in and outside of Portugal.

5.2 Seller Security. If it is customary to take back-up security, what are the formalities for the seller granting a security interest in receivables and related security under the laws of your jurisdiction, and for such security interest to be perfected?

Under Portuguese securitisation transactions, the sellers do not provide security interests to the receivables, given that such could be considered as jeopardising the true sale nature of the transaction.

5.3 Purchaser Security. If the purchaser grants security over all of its assets (including purchased receivables) in favour of the providers of its funding, what formalities must the purchaser comply with in your jurisdiction to grant and perfect a security interest in purchased receivables governed by the laws of your jurisdiction and the related security?

Purchasers in Portuguese securitisation transactions do not usually provide additional security to the noteholders and secured creditors of a given transaction, given that these entities benefit from the legal creditors' privilege mentioned in the answer to question 5.1 above. Other than obtaining the relevant approval for incorporation of the fund or asset digit code approval from the CMVM, which confirms the applicability of the legal creditors' privilege in respect of a given portfolio of receivables pertaining to certain notes issued, no additional formalities are required in order to perfect such legal creditors' privilege, given that it is not subject to registration, in accordance with the Securitisation Law. Additionally, in some transactions, namely those using a securitisation fund, it is usual to create security over the foreign bank accounts of the vehicle – see the answer to question 5.7 below.

5.4 Recognition. If the purchaser grants a security interest in receivables governed by the laws of your jurisdiction, and that security interest is valid and perfected under the laws of the purchaser's jurisdiction, will the security be treated as valid and perfected in your jurisdiction or must additional steps be taken in your jurisdiction?

The security interest would be recognised as valid and effective in Portugal provided that any applicable Portuguese formalities relating to the protection of interested third parties are followed (we refer to the answer to question 5.5 below). For instance, it would be possible to grant an English law pledge over bank accounts (as

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mentioned above) or over Portuguese law receivables; however, the debtor of those receivables should be notified of such security interest in accordance with Portuguese law in order for it to be effective against said debtor.

5.5 Additional Formalities. What additional or different requirements apply to security interests in or connected to insurance policies, promissory notes, mortgage loans, consumer loans or marketable debt securities?

In respect of additional formalities for validly creating security interests in respect to assets above-mentioned, we note that formalities regarding evidence to third parties must be followed, such as: (a) security over insurance policies needs to be notified to the relevant insurance provider; (b) security over promissory notes needs to be endorsed by the security grantor to the benefit of the security beneficiary on the relevant title; (c) creation of mortgages or subsequent transfers of entitlements in respect thereof need to be registered with the competent registry office; and (d) security in respect of marketable debt securities needs to be registered either in the relevant securities account (in respect of book-entry securities) or in the relevant title and securities register (in respect of physical securities).

5.6 Trusts. Does your jurisdiction recognise trusts? If not, is there a mechanism whereby collections received by the seller in respect of sold receivables can be held or be deemed to be held separate and apart from the seller's own assets (so that they are not part of the seller's insolvency estate) until turned over to the purchaser?

In general, Portuguese law does not recognise the legal concept of a trust. However, in terms of collections received by the seller pertaining to a given securitisation transaction, we refer to the segregation principle and autonomous estate nature as set out in question 7.2 below. Furthermore, in respect of collections held by the servicing entity, we would also refer to our answer to question 4.9.

5.7 Bank Accounts. Does your jurisdiction recognise escrow accounts? Can security be taken over a bank account located in your jurisdiction? If so, what is the typical method? Would courts in your jurisdiction recognise a foreign law grant of security (for example, an English law debenture) taken over a bank account located in your jurisdiction?

Portuguese law does not expressly govern escrow accounts; however, similar types of arrangements can be contractually set up and are commonly used by Portuguese banks. Security interests can be taken over bank accounts in Portugal and the typical method to do so would be by granting a pledge over such bank account. A reference should be made to the form of financial pledges which are the customary method of taking security over bank accounts by financial institutions, financial pledges being governed by the regime of Decree-Law no. 105/2004, of 8 May 2004 (as amended), in line with Directive 2002/47/EC of the European Parliament and of the Council of 6 June 2002 on financial collateral arrangements. The important characteristic of such financial pledges is that the collateral taker may have the possibility to use and dispose of financial collateral provided as the owner of it. English law pledges over Portuguese bank accounts are possible, but the relevant Portuguese bank (as debtor in relation to the balance of that account from time to time) should be notified of the granting of the pledge.

5.8 Enforcement over Bank Accounts. If security over a bank account is possible and the secured party enforces that security, does the secured party control all cash flowing into the bank account from enforcement forward until the secured party is repaid in full, or are there limitations? If there are limitations, what are they?

The Bank Accounts of the transaction may naturally be subject to security to the benefit of the transaction creditors. No specific or autonomous security is usually required as, in fact, Portuguese securitisation transactions have the benefit of a legal special creditor's privilege ("*privilégio creditório especial*"), as described in our answer to question 7.2 below, existing in respect of all assets forming part of the portfolio allocated to each transaction related to an issuance of notes (including the transaction bank accounts) and, therefore, having effect over those assets existing at any given moment in time for the benefit of the credit securitisation company and being allocated to the relevant issuance of securitisation notes (including the transaction bank accounts, even when located abroad). Upon enforcement, the common representative of the noteholders or the trustee will control the cash flowing into the bank accounts on behalf of the secured creditors and noteholders and will ensure that they are repaid in full (to the extent there are sufficient available funds in the transaction accounts for full payment of the notes).

5.9 Use of Cash Bank Accounts. If security over a bank account is possible, can the owner of the account have access to the funds in the account prior to enforcement without affecting the security?

The Bank Accounts of the transaction may be subject to security to the benefit of the transaction creditors, as set out in our answer to question 5.8 above. In such context, the owner of the transaction is the issuer as securitisation vehicle and it can access the funds standing to the credit of such accounts subject to security prior to enforcement thereof. However, we would note that the issuer is contractually bound to apply the funds in such accounts exclusively in the manner set out in the transaction documents, i.e., by applying such available funds in accordance with the agreed priorities of payments and such utilisation is monitored by the common representative or trustee to the benefit of the holders of the securitisation notes.

6 Insolvency Laws

6.1 Stay of Action. If, after a sale of receivables that is otherwise perfected, the seller becomes subject to an insolvency proceeding, will your jurisdiction's insolvency laws automatically prohibit the purchaser from collecting, transferring or otherwise exercising ownership rights over the purchased receivables (a "stay of action")? If so, what generally is the length of that stay of action? Does the insolvency official have the ability to stay collection and enforcement actions until he determines that the sale is perfected? Would the answer be different if the purchaser is deemed to only be a secured party rather than the owner of the receivables?

In accordance with Article 6 of the Securitisation Law, the general rule is that the assignment of receivables (described in the answer to question 4.2 above) becomes immediately valid and effective between the parties upon the execution of the relevant assignment agreement, irrespective of the debtor's consent, notification or awareness.

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This means that the assignment of the receivables under the Securitisation Law constitutes a valid and true assignment of receivables from the seller to the purchaser; namely to the extent that the insolvency of the seller will not cause the sale or assignment to be declared void from a legal standpoint, and neither any insolvency official, any borrower, nor any creditor of the seller would be able to have set aside such assignment unless it could provide evidence as to the fact that the assignment had been made in bad faith (*vide* Article 8 of the Securitisation Law). To set aside the assignment conducted on these terms, this would have to be made either, and subject to the applicable law, in the context of the insolvency proceedings where the insolvency administrator on behalf of the insolvent estate may, in the terms predicted in the Insolvency Law and further explained in our answer to question 6.3, challenge the assignment performed within two years prior to the opening of the insolvency proceedings that is qualified as detrimental to the insolvent estate or, within a period of five years following completion of the sale of the receivables, through an application for an unenforceability judgment ("*impugnação pauliana*") of such assignment and providing that the claiming party is capable of proving that: (i) the sale of the receivables has decreased the assets or increased the liabilities of the originator; (ii) the claim of the relevant creditor has arisen before completion of the sale of the receivables (although claims arising after completion of the date of receivables may also be affected to the extent that the relevant creditor provides evidence that such sale has been entered into for the specific purpose of avoiding the payment satisfaction of the creditors' claim); (iii) completion of the sale of the receivables has caused or worsened the insolvency situation of the originator; and (iv) both the originator and the purchaser acted in bad faith, that is, both of them were aware that completion of the sale of the receivables would have the effect described in subparagraph (iii) above.

6.2 Insolvency Official's Powers. If there is no stay of action, under what circumstances, if any, does the insolvency official have the power to prohibit the purchaser's exercise of its ownership rights over the receivables (by means of injunction, stay order or other action)?

Other than as indicated in our answer to question 6.3 below, and on the assumption that a true sale is in place, the only means to prohibit the exercise of rights by the purchaser would be through an injunction ("*providência cautelar não especificada*") followed by the competent main court action.

6.3 Suspect Period (Clawback). Under what facts or circumstances could the insolvency official rescind or reverse transactions that took place during a "suspect" or "preference" period before the commencement of the seller's insolvency proceedings? What are the lengths of the "suspect" or "preference" periods in your jurisdiction for (a) transactions between unrelated parties, and (b) transactions between related parties? If the purchaser is majority-owned or controlled by the seller or an affiliate of the seller, does that render sales by the seller to the purchaser "related party transactions" for purposes of determining the length of the suspect period? If a parent company of the seller guarantee's the performance by the seller of its obligations under contracts with the purchaser, does that render sales by the seller to the purchaser "related party transactions" for purposes of determining the length of the suspect period?

Acts that may be qualified as detrimental to the insolvent estate, performed within two years prior to the opening of the insolvency proceedings, may be challenged by the insolvency administrator on behalf of the insolvent estate. The relevant acts for this purpose are those that diminish, frustrate, aggravate, put in danger or delay the rights of the debtor's creditors. These acts can only be challenged if it is proved that they were motivated by the parties' bad faith (where the counterparty to the act or the beneficiary of the act is a person or entity related to the insolvent entity, the relevant act will be deemed to be motivated by bad faith if carried out within a period of two years prior to the opening of the insolvency proceedings).

The parties' bad faith is defined as knowledge of any of the following circumstances on the date of the relevant act:

(a) that the debtor was insolvent, i.e., unable to fulfil its obligations as they fall due or the debtor's liabilities exceed its assets;

(b) that the act was of a detrimental nature and that the debtor was in a situation of imminent insolvency; or

(c) that insolvency proceedings had commenced.

Where the counterparty to the act or the beneficiary of the act is a person or entity related to the insolvent entity, a legal presumption of bad faith applies if the relevant act was carried out within a period of two years prior to the opening of the insolvency proceedings.

There are also certain acts and transactions which are legally deemed to be detrimental to the insolvent company's estate without the need for any additional proof (such as proof of bad faith of any party). This is the case where:

(a) the division of legacy made less than one year before the date of commencement of insolvency proceedings in which the insolvency's share has been essentially fulfilled with easily evicted property, while the other co-stakeholders kept the major part of the real estate property and nominative securities;

(b) gratuitous acts (i.e. those for which the debtor did not receive any consideration) were performed less than two years before the commencement of the insolvency proceedings where the act results in a reduction in the assets of the debtor;

(c) security was granted within a period of six months prior to the commencement of insolvency proceedings (where such security was granted in respect of pre-existing obligations);

(d) security was granted simultaneously with the secured obligations, within a period of 60 days prior to the commencement of the insolvency proceedings;

(e) surety, sub-surety, guarantee and credit mandates are given, provided they were issued by the insolvent debtor in the six months preceding the date of the commencement of the insolvency proceedings and do not relate to transactions with any real benefit to the debtor;

(f) payment of debts or the performance of other acts occur, which have the effect of performing obligations (for example, set-off) which would become due after the date on which insolvency proceedings are commenced (if such payment or set-off occurs during the six months before the opening of the insolvency proceedings);

(g) payment of debts or the performance of other acts occur, which have the effect of performing obligations (for example, set-off) during the six months prior to the opening of the insolvency proceedings if such payment or set-off is considered unusual according to standard commercial practices and the creditor was not able to demand payment;

(h) acts are performed by the debtor less than a year before the opening of the insolvency proceedings in which the obligations assumed by the debtor significantly exceed those of the counterparty (i.e. transactions at an undervalue); and

(i) reimbursement of shareholder loans occurs, if made in the year that precedes the commencement of the insolvency proceedings.

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In any event, it must be noted that, should an assignment of receivables have been made under the Securitisation Law, the burden of proving bad faith is reversed as the assumption that the above typified acts were made in bad faith will not apply. If an assignment of receivables has been made under the Securitisation Law, the relevant interested parties must always prove bad faith in order for the assignment to be declared void. To date, there has been no court decision or insolvency officer's proceeding unwinding a securitisation transaction.

In case the SPV is majority-owned or controlled by the seller or an affiliate of the seller, the SPV would be deemed as the beneficiary of the act (as a person or entity related to the insolvent entity) and a legal presumption of bad faith would apply if the relevant act was carried out within a period of two years prior to the opening of the insolvency proceedings.

6.4 Substantive Consolidation. Under what facts or circumstances, if any, could the insolvency official consolidate the assets and liabilities of the purchaser with those of the seller or its affiliates in the insolvency proceeding? If the purchaser is owned by the seller or by an affiliate of the seller, does that affect the consolidation analysis?

This is not applicable in the context of the Securitisation Law.

6.5 Effect of Insolvency on Receivables Sales. If insolvency proceedings are commenced against the seller in your jurisdiction, what effect do those proceedings have on (a) sales of receivables that would otherwise occur after the commencement of such proceedings, or (b) on sales of receivables that only come into existence after the commencement of such proceedings?

If the assignment of any assets as described in (a) or (b) above (herein referred as "Future Receivables") is made under the Securitisation Law then the indications provided under question 6.1 above will also apply and therefore such Future Receivables will not form part of the insolvency estate of the seller even when they only become due and payable or come into existence after the date of declaration of insolvency of the seller, provided that the requirements for assignment of such Future Receivables, as set out in our answer to question 4.10, are duly complied with prior to the date of declaration of insolvency of the seller.

In cases where the assignment is not made under the Securitisation Law and the seller becomes insolvent, then the insolvency official may, at its discretion, choose between executing or not executing the receivables sale agreement, as this agreement will be suspended by virtue of the declaration of insolvency.

6.6 Effect of Limited Recourse Provisions. If a debtor's contract contains a limited recourse provision (see question 7.3 below), can the debtor nevertheless be declared insolvent on the grounds that it cannot pay its debts as they become due?

Limited recourse provisions exist on a contractual basis and in accordance with Articles 60 *et seq.* of the Securitisation Law. However, remote a securitisation vehicle's insolvency may be, such a possibility would need to be assessed on a case-by-case basis. In general terms, the debtor is declared insolvent by a Portuguese court where there are no assets to pay debts as they become due. Please note that an insolvency proceeding can be started with a Portuguese court by any creditor of the insolvent entity or by the debtor itself (the debtors board of directors has a duty to file for insolvency); however, insolvency is only declared after the analysis of the debtor's assets and the court's realisation that in fact there are no debtor's assets to pay debts.

7 Special Rules

7.1 Securitisation Law. Is there a special securitisation law (and/or special provisions in other laws) in your jurisdiction establishing a legal framework for securitisation transactions? If so, what are the basics? Is there a regulatory authority responsible for regulating securitisation transactions in your jurisdiction?

Generally, the Securitisation Law provides for: (i) the establishment of a standard and specific securitisation legal framework by regulating the establishment and activity of the securitisation vehicles, the type of credits that may be securitised, and the entities who may assign credits for securitisation purposes; (ii) a simplification of the assignment process by providing for specific rules on the assignment of credits; and (iii) the expansion of the class of eligible assets to include mortgage loans by providing for a simplified mechanism of assignment of this type of credits.

A special securitisation tax regime is also in place. It was established through Decree-Law no. 219/2001 of 4 August 2011 (as amended from time to time) (the "Securitisation Tax Law").

In Portugal, securitisation transactions fall within the regulatory competence of the CMVM, which not only approves the transaction itself by awarding an asset digit code to each issuance, but is also responsible for the approval of the incorporation and supervision of the securitisation vehicles (please refer to our answers to questions 4.2 and 7.2). The asset digit code awarded allows for the identification of the autonomous pool of assets at any given time. Also, the Bank of Portugal, the Portuguese central bank, must be notified by the originators of the securitisation transactions being carried out.

7.2 Securitisation Entities. Does your jurisdiction have laws specifically providing for establishment of special purpose entities for securitisation? If so, what does the law provide as to: (a) requirements for establishment and management of such an entity; (b) legal attributes and benefits of the entity; and (c) any specific requirements as to the status of directors or shareholders?

A flexibility concern seems to have led to the establishment of two different types of securitisation vehicles: credit securitisation funds ("FTCs"); and credit securitisation companies ("STCs").

The FTC structure is necessarily a tripartite one – (a) the fund, which must be managed by (b) a Fund Manager, pursuant to the terms of the applicable fund regulation and one sole (c) depository, qualifying as a credit institution, who must hold the assets of the Fund.

Fund Managers (*Sociedades Gestoras*), are financial companies who are required to: (i) hold registered offices and effective management in Portugal; (ii) qualify as a *sociedade anónima* (public limited liability company) whose share capital is represented by nominative or registered bearer shares; (iii) be exclusively engaged in the management of one or more funds on behalf of the holders of Securitisation Units; and (iv) include in its name the expression "SGFTC".

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As Fund Managers are financial companies, their incorporation is subject to approval by the Bank of Portugal and their activity is generally subject to supervision by this regulatory authority.

One same Fund Manager may have a number of different funds under management and it is the Fund Manager who is responsible for the application for approval of incorporation of each new fund, by filing the relevant approval request with the CMVM – the entity responsible for approving the incorporation of each new fund through the approval of the relevant fund regulation. The incorporation of a fund is deemed to occur upon payment of the subscription price for the relevant securitisation units, something that may only occur upon the CMVM's approval having been obtained.

As the FTC itself has no legal personality (it is an autonomous pool of assets held jointly by a different number of entities), its management is entrusted to the Fund Manager who must manage the fund in accordance with the fund regulation and with certain legal limitations on the management of the FTC such as, for example, the requirement that the Funds' funds are used for the initial or subsequent acquisition of credits (for securitisation purposes) and that such credits represent at least 75 per cent of the securitisation funds' assets.

It is also relevant to note the fact that Fund Managers are subject to specific capital adequacy requirements. A minimum share capital requirement of EUR 250,000 applies while they must have own funds which are equal to, or higher than, a certain percentage of the net value of all funds managed: up to EUR 75 million – 0.5 per cent; and in excess of EUR 75 million – 0.1 per cent.

Securitisation companies are companies who are required to: (i) qualify as a public limited liability company whose share capital is represented by nominative shares; (ii) include in its name the expression "STC"; and (iii) be exclusively engaged in the carrying out of securitisation transactions by means of acquiring, managing and transferring receivables and of issuing notes as a source of financing such acquisitions.

The incorporation of STCs is subject to an approval process near the CMVM and, although they do not qualify as financial companies, this process imposes compliance with a number of requirements that are similar to those arising under all relevant Banking Law requirements. These requirements may be said to have an impact in terms of the shareholding structure an STC is to have, to the extent that full disclosure of both direct and indirect ownership is required for the purposes of allowing the CMVM to assess the reliability and soundness of the relevant shareholding structure. The same applies in respect of the members of corporate bodies, namely directors who must be persons whose reliability and availability must ensure the capacity to run the STC business in a sound and prudent manner.

STCs are also subject to specific capital adequacy requirements. A minimum share capital requirement of EUR 250,000 applies while they must have own funds which are equal to, or higher than, a certain percentage of the net value of issued outstanding securitisation notes: up to EUR 75 million – 0.5 per cent; and in excess of EUR 75 million – 0.1 per cent.

In terms of legal attributes and benefits, we believe it is fair to say that both vehicles are quite similar as they both allow for a full segregation of the relevant portfolios and their full dedication to the issued securities. While in a fund structure this is achieved through the structure itself, as the assets of each fund are only available to meet the liabilities of such fund in a company structure, certain relevant legal provisions establish a full segregation principle and a creditors' privileged entitlement over the assets that are so segregated and which collateralise a certain issue of notes.

This segregation principle means that the receivables and other related assets and amounts existing at a given moment for the benefit of an STC, and which are related to a certain issuance of notes, constitute an autonomous and ring-fenced pool of assets ("*património autónomo*") which is exclusively allocated to such issuance of notes and which is not, therefore, available to creditors of the STC other than the noteholders, and to the services providers existing specifically in the context of such issuance of notes until all the amounts due in respect of the notes have been repaid in full. To this effect, the assets integrated in each *património autónomo* are listed and filed with the CMVM and subject to an asset identification code that is also granted by the CMVM.

In addition to the above, and in order to render this segregation principle effective, the noteholders and the other creditors relating to each series of securitisation notes issued by the STC are further entitled to a legal creditor's privilege (equivalent to a security interest) over all of the assets allocated to the relevant issuance of securitisation notes, including assets located outside Portugal. In fact, according to Article 63 of the Securitisation Law, this legal special creditor's privilege ("*privilégio creditório especial*") exists in respect of all assets forming part of the portfolio allocated to each transaction related to an issuance of notes and therefore has effect over those assets existing at any given moment in time for the benefit of the STC that are allocated to the relevant issuance of securitisation notes.

7.3 Location and form of Securitisation Entities. Is it typical to establish the special purpose entity in your jurisdiction or offshore? If in your jurisdiction, what are the advantages to locating the special purpose entity in your jurisdiction? If offshore, where are special purpose entities typically located for securitisations in your jurisdiction? What are the forms that the special purpose entity would normally take in your jurisdiction and how would such entity usually be owned?

The Securitisation Law establishes two types of securitisation vehicles as set out in question 7.2, subject to different forms of incorporation but very similar in legal attributes and benefits, as they both allow for a full segregation of the relevant portfolios and their exclusive allocation to the issued securities. On the one hand, in a fund structure, this is achieved through the structure itself, as the assets of each fund are only available to meet the liabilities of such fund. On the other hand, in a company structure (which works as a multi compartment entity) certain relevant legal provisions establish a full segregation principle and a creditor's privileged entitlement over the assets that are so segregated and that collateralise each transaction and the corresponding issue of notes. From an operation perspective, the timing and documentation package for both alternatives under the Securitisation Law are very similar (see question 7.2).

The choice of using an FTC or an STC structure in a given securitisation transaction was essentially the investor's, being historically, and initially, more familiar with the fund structure (which then used a foreign SPV to issue the notes to market investors).

Initially, in securitisation transactions in the Portuguese market:

- the FTC acquired the assets and issued securities (securitisation units); and
- an SPV (generally in Ireland or Luxembourg) subscribed for the securitisation units and issued notes, which were purchased by the final investors.

This was essentially investor-driven, as it was felt that it would be difficult to place units with investors (as they are not pure debt instruments but quasi-capital instruments).

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Since the first Portuguese securitisation with an STC in 2004, under which tax claims and social security claims credits were assigned by the Portuguese state to Sagres STC, S.A., the STC has spread in the market and generally been accepted by institutional investors. In recent years, securitisations have essentially adopted STCs, with a direct issuance out of Portugal.

In any case, when using both STCs or FTCs, Portuguese securitisations are subject to the Securitisation Law, whereby the relevant SPV is required to be incorporated in Portugal and the assignment of loans is fully governed by Portuguese law and subject to full supervision of the CMVM. One of the benefits of this regime is the tax neutrality, as set out in section 9.

7.4 Limited-Recourse Clause. Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) limiting the recourse of parties to that agreement to the available assets of the relevant debtor, and providing that to the extent of any shortfall the debt of the relevant debtor is extinguished?

Yes. The Portuguese general rule on limited recourse provided by Article 602 of the Portuguese Civil Code establishes that a limited recourse provision may be contractually agreed between the debtor and the creditor, limiting the debtor's liability to certain available assets. Under this general rule, a Portuguese court would enforce and give effect to such a limited recourse provision. Also, limited recourse provisions are specifically valid and binding under the provisions of Articles 60 *et seq*. of the Securitisation Law. Insofar as limited recourse arrangements are concerned, we would furthermore take the view that they correspond to an application in a specific context (that of securitisation) of a possibility of having a contractual limitation on the assets which are liable for certain obligations or debts, which is provided for by Portuguese law on general terms (namely Article 602 of the Portuguese Civil Code). Once they result from the quoted provisions of the law, limited recourse shall not be affected by the issuer's insolvency; however, remote, such event may be in the context of the Portuguese securitisation vehicles.

7.5 Non-Petition Clause. Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) prohibiting the parties from: (a) taking legal action against the purchaser or another person; or (b) commencing an insolvency proceeding against the purchaser or another person?

Non-petition, limited recourse and priority of payments arrangements, as usually contained in the securitisation transactions documentation, are valid under Portuguese law, deriving directly from the provisions of Articles 60 *et seq*. of the Securitisation Law.

7.6 Priority of Payments "Waterfall". Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) distributing payments to parties in a certain order specified in the contract?

Priority of payments provisions are standard contractual provisions included in Portuguese securitisation transactions (both governed by Portuguese law, when the vehicle is a securitisation company and governed by a foreign law, usually English law, when the vehicle at stake is a securitisation fund, as in this case, the issuer is usually an Irish SPV) and are valid under Portuguese law and would be given effect by a Portuguese court (but if governed by a foreign law, in the context of a judicial recognition of a foreign court decision – *reconhecimento de sentença estrangeira*).

7.7 Independent Director. Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) or a provision in a party's organisational documents prohibiting the directors from taking specified actions (including commencing an insolvency proceeding) without the affirmative vote of an independent director?

As per the Portuguese Insolvency Code, the commencement of insolvency proceedings is an obligation of the board of directors of any given company that is found to be insolvent and therefore there should not be a limitation as to the fulfilment of this legal obligation.

7.8 Location of Purchaser. Is it typical to establish the purchaser in your jurisdiction or offshore? If in your jurisdiction, what are the advantages to locating the purchaser in your jurisdiction? If offshore, where are purchasers typically located for securitisations in your jurisdiction?

As mentioned above, the Securitisation Law establishes two types of securitisation vehicles, subject to different forms of incorporation – the FTCs and the STCs, which act as issuers and purchasers. When using any of these entities or vehicles, securitisation transactions are subject to the Securitisation Law, whereby the relevant SPV is incorporated in Portugal and the assignment of loans is fully governed by Portuguese law and subject to full supervision of the CMVM (for more details, please refer to our answer under 7.3 above).

8 Regulatory Issues

8.1 Required Authorisations, etc. Assuming that the purchaser does no other business in your jurisdiction, will its purchase and ownership or its collection and enforcement of receivables result in its being required to qualify to do business or to obtain any licence or its being subject to regulation as a financial institution in your jurisdiction? Does the answer to the preceding question change if the purchaser does business with more than one seller in your jurisdiction?

The mere purchase and management of a certain portfolio of receivables does not, in itself, qualify as a banking or financial activity (unless it is to be carried out on a professional and regular basis, or includes any form of credit granting) and should therefore not give rise to the need for any kind of authorisation or licence being obtained.

8.2 Servicing. Does the seller require any licences, etc., in order to continue to enforce and collect receivables following their sale to the purchaser, including to appear before a court? Does a third-party replacement servicer require any licences, etc., in order to enforce and collect sold receivables?

No. When the seller remains in charge of the collection of receivables (as, in fact, is foreseen in the Securitisation Law, for example, when the seller is a bank, credit institution or other financial company) no licence or authorisation is required for the seller to continue to

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enforce and collect receivables, including to appear before a court (assuming the debtors are not aware of the assignment). However, should the assignment of the receivables have been notified to the debtors then the servicer will need to show sufficient title to appear in court, like a power of attorney, in case its legitimacy is challenged by the relevant debtor as, in fact, only a fully-fledged creditor has the relevant legitimacy ("*legitimidade processual*") to claim a certain credit in court.

In cases where another entity is chosen to perform the role of servicer, a third-party replacement servicer is appointed to replace the seller as original servicer or a back-up servicer is required to be put in place, CMVM's approval to this effect is required, as set out under Article 5 of the Securitisation Law.

8.3 Data Protection. Does your jurisdiction have laws restricting the use or dissemination of data about or provided by obligors? If so, do these laws apply only to consumer obligors or also to enterprises?

There are, indeed, applicable data protection laws, but exclusively in respect of consumer obligors or individuals and not to enterprises. However, the use or dissemination of personal data in respect of directors of enterprises who are individuals will also be subject to restrictions.

Portugal is currently subject to the Law no. 67/98 of 26 October on personal data protection, which will be replaced on 25 May 2018 by the EU Regulation 2016/679 (the General Data Protection Regulation or "GDPR").

GPDR will apply to the processing of personal data by entities located in EU territory (regardless of whether or not the processing takes place in the EU) and to entities located outside EU territory (whenever they provide goods and services to or monitor EU citizens).

Pursuant to the GDPR, personal data may be processed if: (a) it is carried out with the data subject's consent; (b) it is necessary for the performance of a contract with the data subject; (c) it is necessary for compliance with a legal obligation; (d) it is necessary in order to protect the vital interests of the data subject; (e) it is necessary for the public interest or in the exercise of official authority; or (f) it is necessary for the controller's or recipient's legitimate interests, except where overridden by the interests of the data subject. Specific rules are established as to the validity of consent and additional data subject rights and obligations.

The GDPR will render it unnecessary to notify or obtain authorisation (depending on the intended terms of processing) from the national data protection authority (the *Comissão Nacional de Proteção de Dados*), although additional obligations will apply – for example, data breach notifications, mandatory privacy impact assessments, additional data subject rights, the obligation to keep internal data processing records, possible Data Protection Officer appointment and privacy by design and privacy by default principles.

8.4 Consumer Protection. If the obligors are consumers, will the purchaser (including a bank acting as purchaser) be required to comply with any consumer protection law of your jurisdiction? Briefly, what is required?

Portuguese law (namely the Portuguese Constitution, the Civil Code and the Consumer Protection Law) contains general provisions in relation to consumer protection. These provisions cover general principles of information disclosure, information transparency (contractual clauses must be clear, precise and legible) and a general duty of diligence, neutrality and good faith in the negotiation of contracts.

Decree-Law no. 446/85 of 25 October 1985, as amended from time to time and Decree-Law no. 249/99 of 7 July 1999 (which implemented Directive 93/13/CEE of 5 April 1993) and Decree-Law no. 323/2001 of 17 December 2001, known as the *Lei das Cláusulas Contratuais Gerais* (the Law of General Contractual Clauses), prohibits, in general terms, the introduction of abusive clauses in contracts entered into with consumers. Pursuant to this law, a clause is deemed to be abusive if such clause has not been specifically negotiated by the parties and leads to an unbalanced situation insofar as the rights and obligations of the consumer (regarded as the weaker party) and the rights and obligations of the counterparty (regarded as the stronger party) are concerned and the law provides for an extended list of prohibited clauses. The use of such clauses that are prohibited will cause the relevant clauses to be considered null and void.

There are many legal and regulatory diplomas setting forth protection measures to the benefit of consumers, notably Decree-Law no. 220/94 of 23 August 1994 states the minimum level of information to be included in loans, such as the annual effective rate and information related thereto. Recently, Decree-Law no. 74-A/2017, of 23 June on credit agreements for consumers relating to residential immovable property (which implemented Directive 2017/17/EU) established a number of requisites for ensuring consumer protection and transparency, namely as in relation to the provision of pre-contractual information.

8.5 Currency Restrictions. Does your jurisdiction have laws restricting the exchange of your jurisdiction's currency for other currencies or the making of payments in your jurisdiction's currency to persons outside the country?

Other than in international embargo circumstances, there are no laws in Portugal restricting foreign exchange transactions or free international capital movements.

We would note, in addition, that if the debt securities issued by the funding vehicle are cleared through *Interbolsa – Sociedade Gestora de Sistemas de Liquidação e de Sistemas Centralizados de Valores Mobiliários, S.A.* ("Interbolsa"), as operator of the Portuguese centralised securities system, then payments can only be made in the currencies accepted by Interbolsa. For the time being, Interbolsa will only settle and clear notes denominated in euros, Canadian dollars, Swiss francs, US dollars, Sterling and Japanese yen and notes denominated in any other currency upon prior request and approval.

8.6 Risk Retention. Does your jurisdiction have laws or regulations relating to "risk retention"? How are securitisation transactions in your jurisdiction usually structured to satisfy those risk retention requirements?

Yes. Articles 405 to 410 of Regulation (EU) No 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012, as amended from time to time, the CRR Regulation (directly applicable in Portugal), and Bank of Portugal's Notice 9/2010 which impose an obligation on originators (amongst others) to retain of a material net economic interest of no less than five per cent which can be achieved through several alternatives:

(a) Retention of no less than five per cent of the nominal value of each of the tranches sold or transferred to the investors.

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(b) In the case of securitisations of revolving exposures, retention of the originator's interest of no less than five per cent of the nominal value of the securitised exposures.

(c) Retention of randomly selected exposures, equivalent to no less than 5 per cent of the nominal value of the securitised exposures, where such exposures would otherwise have been securitised in the securitisation, provided that the number of potentially securitised exposures in no less than 100 at origination.

(d) Retention of the first lost tranche and, if necessary, other tranches having the same or a more severe risk profile than those transferred or sold to investors and not maturing any earlier than those transferred or sold to investors, so that the retention equals in total no less than five per cent of the nominal value of the securitised exposures.

(e) Retention of a first loss exposure not less than five per cent of every securitised exposure in the securitisation.

We note that Portugal's Notice 9/2010 also sets out the same requirements as items (a) to (d) above and there are no limitations under Portuguese law for such requirements to be implemented.

Please note that with the entrance into force of the STS Regulation (as defined below under 8.7) risk retention rules are also addressed, imposing risk retention rules on originators, sponsors and original lenders, albeit keeping the five per cent minimum level.

8.7 Regulatory Developments. Have there been any regulatory developments in your jurisdiction which are likely to have a material impact on securitisation transactions in your jurisdiction?

From a regulatory standpoint, we must note that there were no major national regulatory developments with material impact on securitisation transactions. In any case, we must note that EU Regulation 2017/2402, which aims at establishing a general securitisation framework at the EU level (STS Regulation), entered into force on 17 January 2018 and will become applicable to all securitisation products from 1 January 2019 onwards. Besides creating a new framework for simple, standard and transparent securitisations, the regulation will affect due diligence requirements, risk-retention requirements and transparency rules.

In case of retail securitisation transactions, although not common in Portugal, we would highlight that Regulation 1286/2014, on Packaged Retail and Insurance-based Investment Products ("PRIIPs Regulation") entered into force on 1 January 2018. This regulation applies to PRIIPs products and services purchased by an EEA Resident Retail Investor, regardless of their nationality, being applicable worldwide, irrespective of where a PRIIP is purchased, as long as it is purchased by an EEA Resident Retail Investor. The PRIIPs Regulation, which is applicable to structured products (i.e. securitised bonds) foresees, amongst others, the issue of a standardised short form disclosure document – the PRIIPs Key Information Document ("KID"), thereby making it easier for retail investors to understand and compare the key features, risk and costs of different products within the PRIIPs scope.

9 Taxation

9.1 Withholding Taxes. Will any part of payments on receivables by the obligors to the seller or the purchaser be subject to withholding taxes in your jurisdiction? Does the answer depend on the nature of the receivables, whether they bear interest, their term to maturity, or where the seller or the purchaser is located? In the case of a sale of trade receivables at a discount, is there a risk that the discount will be recharacterised in whole or in part as interest? In the case of a sale of trade receivables where a portion of the purchase price is payable upon collection of the receivable, is there a risk that the deferred purchase price will be recharacterised in whole or in part as interest? If withholding taxes might apply, what are the typical methods for eliminating or reducing withholding taxes?

The Securitisation Tax Law has established the tax regime applicable to the securitisation transactions carried out under the Securitisation Law. Its main goal was to ensure a tax neutral treatment to the securitisation transactions set up by each one of the securitisation vehicles provided for in the Securitisation Law. Therefore, under Articles 2/5 and 3/4 of the Securitisation Tax Law, there is no withholding tax on (i) the payments made by the purchaser (an STC and FTC) to the seller in respect of the purchase of the receivables, (ii) the payments by the obligors under the loans, and (iii) the payments of collections by the servicer (who is usually also the seller) to the purchaser are not subject to Portuguese withholding tax. The nature or the characteristics of the receivables and the location of the seller do not have any influence on the tax regime referred to above. However, the purchaser must be an STC or FTC resident for tax purposes in Portugal in order to benefit from the special tax regime. There is no recharacterisation risk of the deferred purchase price as payments of collections are not subject to withholding tax.

On the other hand, under Article 4/1 of Securitisation Tax Law, income generated by the holding (distributions) or transfer (capital gains) of the notes and units is generally subject to the Portuguese tax regime established for debt securities.

Accordingly to Circular no. 4/2014 issued by the Portuguese Tax Authorities and to the Order issued by the Secretary of State for Tax Affairs, dated 14 July 2014, in connection with tax ruling no. 7949/2014 disclosed by tax authorities, the general tax regime on debt securities (as established in Decree-Law no. 193/2005, of 7 November ("Decree-Law 193/2005")) also applies on income generated by the holding or the transfer of securitisation notes issued by STCs under securitisation transactions. Decree-Law 193/2005 is therefore applicable to securitisation notes, notably regarding the requirements on registration of securitisation notes in the relevant clearing systems and on the exemption applicable to income obtained by non-resident holders of such securitisation notes. In this regard, payment of interest and principal on securitisation notes are exempt from Portuguese income tax, including withholding tax, provided the relevant noteholder qualifies as a non-Portuguese resident having no permanent establishment in Portugal. Such exemption does not apply to non-resident individuals or companies if the individual's or company's country of residence is any jurisdiction listed as a tax haven in Ministerial Order no. 150/2004, of 13 February 2004 (as amended from time to time) and with which Portugal does not have a double tax treaty or a tax information exchange agreement in force, provided the requirements and procedures for evidencing the non-residence status are complied with. To qualify for the exemption, noteholders will be required to provide the direct registry entity with adequate evidence of non-residence status prior to the relevant interest payment date, according to procedures required under Decree-Law 193/2005. If for any reason withholding tax on interest

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payments is applied and the relevant noteholder is able to benefit from the income tax exemption, a reimbursement procedure is available under Decree-Law 193/2005.

9.2 Seller Tax Accounting. Does your jurisdiction require that a specific accounting policy is adopted for tax purposes by the seller or purchaser in the context of a securitisation?

No specific tax accounting requirements need to be complied with by the seller under the securitisation tax regime. However, CMVM Regulation no. 1/2002, of 5 February 2002, sets forth the specific accountancy regime for FTCs, and CMVM Regulation no. 12/2002, of 18 July 2002, establishes specific accountancy rules for STCs (although the accounting procedure of this type of corporate entity follows the general Portuguese Accountancy Standards).

9.3 Stamp Duty, etc. Does your jurisdiction impose stamp duty or other transfer or documentary taxes on sales of receivables?

Pursuant to the Securitisation Tax Regime, no stamp duty is due on: (i) the sale of receivables being securitised; or (ii) the fees and commissions which fall under Article 5 (i.e. referring to required acts to ensure a good management of the receivables and, if applicable, of the respective guarantees, and to ensure collection services, the administrative services relating to the receivables, all relations with the debtors and also maintaining, modifying and extinguishing acts related to guarantees, if any) and under Article 24 (i.e. as to any of the described attributions of the depositary), both of the Securitisation Law, that may be charged by the servicer to the purchaser. In addition, no documentary taxes are due in Portugal.

9.4 Value Added Taxes. Does your jurisdiction impose value added tax, sales tax or other similar taxes on sales of goods or services, on sales of receivables or on fees for collection agent services?

The sale of receivables is VAT-exempt under Articles 9(27)(a) and (c) of the Portuguese VAT Code, which are in line with Article 135(a) and (c) of the VAT Directive (EC Directive 2006/112/EC). Pursuant to the Securitisation Tax Regime, no value added tax is due on the administration or management of securitisation funds and also on the fees and commissions regarding management services falling under Article 5 and transactions undertaken by depositary entities pursuant to Article 24 of the Securitisation Law, as described in our answer to question 9.3 above.

9.5 Purchaser Liability. If the seller is required to pay value-added tax, stamp duty or other taxes upon the sale of receivables (or on the sale of goods or services that give rise to the receivables) and the seller does not pay, then will the taxing authority be able to make claims for the unpaid tax against the purchaser or against the sold receivables or collections?

This is not applicable since the assignment of the receivables benefits from a stamp tax and a VAT exemption.

9.6 Doing Business. Assuming that the purchaser conducts no other business in your jurisdiction, would the purchaser's purchase of the receivables, its appointment of the seller as its servicer and collection agent, or its enforcement of the receivables against the obligors, make it liable to tax in your jurisdiction?

Considering the above, it is important to highlight that the purchase of the receivables is qualified as a true sale transaction under the Securitisation Law, the purchaser being the legal owner of the receivables and therefore the purchaser is subject to tax in Portugal (namely in respect of income arising from the receivables). However, despite being viewed as an ordinary taxpayer, in order to ensure a tax neutral treatment on the securitisation transactions, the taxable income of the purchaser tends to be equivalent to zero for tax purposes since the income payments made to the noteholders are tax-deductible.

9.7 Taxable Income. If a purchaser located in your jurisdiction receives debt relief as the result of a limited recourse clause (see question 7.3 above), is that debt relief liable to tax in your jurisdiction?

The provisions of Article 60 *et seq*. of the Securitisation Law specifically provides for limited recourse provisions that are valid and binding on the noteholders. Insofar as limited recourse arrangements are concerned, we would take the view that they correspond to an application in a specific context (that of securitisation) of a possibility of having a contractual limitation on the assets that are liable for certain obligations or debts, which is provided for by Portuguese law on general terms (namely Article 602 of the Portuguese Civil Code). Once they result from the quoted provisions of the law, limited recourse shall not be affected by the issuer's insolvency, however remote, such event may be in the context of the Portuguese securitisation vehicles. As to these matters, we refer to question 7.3 above.

This being said, the fact that the noteholders have a limited recourse to the pool of receivables backing the securitisation notes does not have an impact on the tax regime applicable to their status as noteholders under the Securitisation Tax Law and Decree-Law 193/2005. Taxation on the notes shall occur exactly on the same terms as, and with no exceptions from, what is described in question 9.1 above.

Acknowledgment

The authors would like to thank Maria Carrilho for her invaluable assistance in the preparation of this chapter.
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Russia

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LECAP

1 Receivables Contracts

1.1 Formalities. In order to create an enforceable debt obligation of the obligor to the seller: (a) is it necessary that the sales of goods or services are evidenced by a formal receivables contract; (b) are invoices alone sufficient; and (c) can a binding contract arise as a result of the behaviour of the parties?

Under Russian law, the sale of goods or services between two legal entities or between a legal entity and a private individual shall be performed in a plain written form. Breach of the plain written form requirement deprives the transaction's parties of the ability to refer to the proof of witness in order to confirm the transaction in case of a potential dispute. In certain cases stipulated by law or agreements between the parties, non-compliance with the plain written form requirement may trigger a transaction's invalidity.

Plain written form requirements are generally observed via signing a formal receivables agreement. However, in practice, formalising, for example, consignment bills or similar documents, may be treated as sufficient evidence of an agreement's execution.

1.2 Consumer Protections. Do your jurisdiction's laws: (a) limit rates of interest on consumer credit, loans or other kinds of receivables; (b) provide a statutory right to interest on late payments; (c) permit consumers to cancel receivables for a specified period of time; or (d) provide other noteworthy rights to consumers with respect to receivables owing by them?

Consumer protection of retail lenders is regulated mainly by the Federal Law No. 353-FZ "On Consumer Loan" dated 21 December 2013 (the "Consumer Loan Law").

According to the Consumer Loan Law, the overall cost of credit (loan), including all types of the interest payments, commissions, etc. shall be communicated to the consumer by the retail bank. Such overall cost may not exceed an average market cost of the respective category of consumer credit by more than one third.

Average market costs of consumer credit (loan) per category are calculated and published by the Central Bank of Russia (CBR) on a quarterly basis.

The Consumer Loan Law also sets forth a maximum default interest rate which shall not exceed 20% *per annum* or, with respect to interest-free loans, 0.1% of the loan principal for each day the default is ongoing.

The obligor has the right to cancel the loan within 14 days (or 30 days if the loan was extended for a specific purpose) after a consumer loan was granted without any prior notice to the lender.

The obligor is also entitled to repay the consumer loan in full at any time during its term, although in this case the obligor shall give 30 days' prior notice to the creditor.

If a consumer loan is cancelled or repaid in full or in part earlier than agreed, the obligor shall pay the creditor the interest accrued on the loan principal up to the date of the factual return of the respective loan amount, inclusive.

The creditor under a consumer loan is also required to provide the obligor with, or enable access to, information on:

- the outstanding loan amount;
- the dates and amount of the effected and upcoming payments;
- the amount of overdue debt; and
- any other data specified in the consumer loan agreement.

1.3 Government Receivables. Where the receivables contract has been entered into with the government or a government agency, are there different requirements and laws that apply to the sale or collection of those receivables?

In general, under Russian law the assignment of receivables under agreements on sale of goods or services with the Russian government and municipalities ("government contract") is allowed, since for the purpose of repayment of debts under the government contract that has already been performed, the creditor's personality does not have a substantial importance for the debtor. But it should be noted that, as a rule, such assignment of receivables is possible only with the consent of the debtor (government).

However, the assignment of receivables could be restricted or prohibited, for example, in the case of assignment of tax rights and obligations or a military confidential contract.

2 Choice of Law – Receivables Contracts

2.1 No Law Specified. If the seller and the obligor do not specify a choice of law in their receivables contract, what are the main principles in your jurisdiction that will determine the governing law of the contract?

Under Russian conflict of laws rules, with certain limited exceptions,

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in the absence of an explicit choice of law, the agreement will be governed by the law of the state where the party providing a characteristic performance under such agreement is domiciled. This principle is applicable to all consumer loans, other loans granted by Russian banks, etc.

There are certain exemptions from this rule in relation to certain types of contracts.

In particular, if it is clear from the law, the terms of the agreement or the circumstances of the case that the agreement is closely tied to a different jurisdiction, the law of such jurisdiction shall be applied.

2.2 Base Case. If the seller and the obligor are both resident in your jurisdiction, and the transactions giving rise to the receivables and the payment of the receivables take place in your jurisdiction, and the seller and the obligor choose the law of your jurisdiction to govern the receivables contract, is there any reason why a court in your jurisdiction would not give effect to their choice of law?

In this case, a Russian court will invariably give effect to a choice of Russian law.

2.3 Freedom to Choose Foreign Law of Non-Resident Seller or Obligor. If the seller is resident in your jurisdiction but the obligor is not, or if the obligor is resident in your jurisdiction but the seller is not, and the seller and the obligor choose the foreign law of the obligor/seller to govern their receivables contract, will a court in your jurisdiction give effect to the choice of foreign law? Are there any limitations to the recognition of foreign law (such as public policy or mandatory principles of law) that would typically apply in commercial relationships such as that between the seller and the obligor under the receivables contract?

Generally, a Russian court would recognise the choice of law and apply the foreign governing law to the agreement. There is a positive court practice illustrating the recognition of contractual choice of foreign law as the governing law by the Russian courts. However, foreign law would not be applied to the extent that it conflicts with Russian public policy or the mandatory rules of law.

In order to apply provisions of foreign law, Russian courts should receive satisfactory proof of the existence and meaning of the relevant provisions of the applicable foreign law. If a dispute arises through commercial relations, a court may impose a duty to provide such evidence on the parties. Should a Russian court fail to receive such evidence, it may apply Russian law instead.

3 Choice of Law – Receivables Purchase Agreement

3.1 Base Case. Does your jurisdiction's law generally require the sale of receivables to be governed by the same law as the law governing the receivables themselves? If so, does that general rule apply irrespective of which law governs the receivables (i.e., your jurisdiction's laws or foreign laws)?

The parties to a receivables purchase agreement are free to choose the law governing their contract, irrespective of the law governing the receivables transferred. However, the possibility of the receivables assignment, the relationship between the new creditor and the obligor and the terms for discharge of obligations shall be governed by the law applicable to the transferred receivables.

3.2 Example 1: If (a) the seller and the obligor are located in your jurisdiction, (b) the receivable is governed by the law of your jurisdiction, (c) the seller sells the receivable to a purchaser located in a third country, (d) the seller and the purchaser choose the law of your jurisdiction to govern the receivables purchase agreement, and (e) the sale complies with the requirements of your jurisdiction, will a court in your jurisdiction recognise that sale as being effective against the seller, the obligor and other third parties (such as creditors or insolvency administrators of the seller and the obligor)?

Yes, in this case the sale will be recognised by a Russian court.

3.3 Example 2: Assuming that the facts are the same as Example 1, but either the obligor or the purchaser or both are located outside your jurisdiction, will a court in your jurisdiction recognise that sale as being effective against the seller and other third parties (such as creditors or insolvency administrators of the seller), or must the foreign law requirements of the obligor's country or the purchaser's country (or both) be taken into account?

Yes, in this case the sale will be recognised by a Russian court.

3.4 Example 3: If (a) the seller is located in your jurisdiction but the obligor is located in another country, (b) the receivable is governed by the law of the obligor's country, (c) the seller sells the receivable to a purchaser located in a third country, (d) the seller and the purchaser choose the law of the obligor's country to govern the receivables purchase agreement, and (e) the sale complies with the requirements of the obligor's country, will a court in your jurisdiction recognise that sale as being effective against the seller and other third parties (such as creditors or insolvency administrators of the seller) without the need to comply with your jurisdiction's own sale requirements?

Generally, in such circumstances a sale governed by foreign law would be recognised by the Russian court.

As indicated above, however, foreign law would not be applied to the extent it conflicts with Russian public policy or the mandatory rules of law, which could, at least theoretically, hinder the recognition of the sale.

3.5 Example 4: If (a) the obligor is located in your jurisdiction but the seller is located in another country, (b) the receivable is governed by the law of the seller's country, (c) the seller and the purchaser choose the law of the seller's country to govern the receivables purchase agreement, and (d) the sale complies with the requirements of the seller's country, will a court in your jurisdiction recognise that sale as being effective against the obligor and other third parties (such as creditors or insolvency administrators of the obligor) without the need to comply with your jurisdiction's own sale requirements?

The answer to this question is the same as the answer to question 3.4 above.

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3.6 Example 5: If (a) the seller is located in your jurisdiction (irrespective of the obligor's location), (b) the receivable is governed by the law of your jurisdiction, (c) the seller sells the receivable to a purchaser located in a third country, (d) the seller and the purchaser choose the law of the purchaser's country to govern the receivables purchase agreement, and (e) the sale complies with the requirements of the purchaser's country, will a court in your jurisdiction recognise that sale as being effective against the seller and other third parties (such as creditors or insolvency administrators of the seller, any obligor located in your jurisdiction and any third party creditor or insolvency administrator of any such obligor)?

Generally, the answer to this question is the same as the answer to question 3.4 above. As indicated in our answer to question 3.1, the possibility of the receivables assignment, the relationship between the new creditor and the obligor and the terms for discharge of obligations shall be governed by the law applicable to the transferred receivables. In particular, in this case, Russian perfection and the notice requirements as described in our answers to questions 4.1 to 4.5 will apply.

4 Asset Sales

4.1 Sale Methods Generally. In your jurisdiction what are the customary methods for a seller to sell receivables to a purchaser? What is the customary terminology – is it called a sale, transfer, assignment or something else?

In terms of terminology, when the Russian Civil Code and court practice mention a transfer of receivables (including by way of sale, donation or compensation for release from obligations), they are usually referring to an agreement on the voluntary transfer of rights or assignment (cession/*tsessiya*). An agreement on the cession of rights may be signed or otherwise entered into separately from the agreement of sale, donation of such rights, etc.; however, in practice this is usually not the case.

Agreements on the sale of rights are subject to the civil law provisions on assignment or transfer of rights and on sale of goods.

Receivables may also be transferred under a factoring agreement, which is, in practice, less common for securitisation purposes.

In cases of both sale and factoring it is possible to transfer existing receivables and receivables which may arise in the future.

4.2 Perfection Generally. What formalities are required generally for perfecting a sale of receivables? Are there any additional or other formalities required for the sale of receivables to be perfected against any subsequent good faith purchasers for value of the same receivables from the seller?

Generally, Russian law does not require any formalities to be observed for perfecting a sale of receivables apart from the observation of the form of the respective agreement (please refer to question 1.1 above) and the notification of the obligor (please refer to question 4.4 below).

If a receivables agreement is in plain written form, is notarised or state registered, then the sale agreement shall also be concluded in the same form.

4.3 Perfection for Promissory Notes, etc. What additional or different requirements for sale and perfection apply to sales of promissory notes, mortgage loans, consumer loans or marketable debt securities?

Assignment of promissory notes shall be done in a written form on a promissory note or an additional sheet attached to it. Alternatively this can be done by way of executing a separate assignment contract.

In order to facilitate transfers of mortgage loans, a mortgage certificate may be issued. Mortgage certificates are commonly used in Russian securitisation. Generally, such certificates are assigned similarly to promissory notes. Furthermore, mortgage certificates may be put into custody of a depository or "immobilised". Assignment of "immobilised" mortgage certificates shall be carried out by making entries in the books of the particular depository.

Mass issue debt securities are generally issued in documentary form with mandatory centralised custody of their certificates with a depository. Such securities may be assigned only by way of making entries in the books of depositories on the basis of the instructions of their holders.

4.4 Obligor Notification or Consent. Must the seller or the purchaser notify obligors of the sale of receivables in order for the sale to be effective against the obligors and/or creditors of the seller? Must the seller or the purchaser obtain the obligors' consent to the sale of receivables in order for the sale to be an effective sale against the obligors? Whether or not notice is required to perfect a sale, are there any benefits to giving notice – such as cutting off obligor set-off rights and other obligor defences?

Notice to the obligor on the transfer of the receivables is not required for the perfection of such transfer. However, in cases where no such notice is given, the purchaser of the rights bears the risk of unfavourable consequences. In particular, until transfer notice is given, the obligor may perform the obligation in favour of the seller which will constitute due discharge of its respective obligation. The obligor is also entitled to raise objections against the claims of the purchaser that result from relations between the obligor and the seller until the receipt of the relevant transfer notice.

The sale of receivables where the identity of the creditor has substantial importance to the obligor (e.g. obligations out of simple partnership agreement) or the sale of non-monetary receivables which may significantly increase the burden of the obligor are not permissible without the consent of such obligor.

4.5 Notice Mechanics. If notice is to be delivered to obligors, whether at the time of sale or later, are there any requirements regarding the form the notice must take or how it must be delivered? Is there any time limit beyond which notice is ineffective – for example, can a notice of sale be delivered after the sale, and can notice be delivered after insolvency proceedings have commenced against the obligor or the seller? Does the notice apply only to specific receivables or can it apply to any and all (including future) receivables? Are there any other limitations or considerations?

To be effective, the notice has to be made in plain written form. The notice can be delivered after the sale. There is no time limit beyond which notice is ineffective, but the parties of a receivables purchase agreement could determine time limit in their agreement.

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4.6 Restrictions on Assignment – General Interpretation. Will a restriction in a receivables contract to the effect that "None of the [seller's] rights or obligations under this Agreement may be transferred or assigned without the consent of the [obligor]" be interpreted as prohibiting a transfer of receivables by the seller to the purchaser? Is the result the same if the restriction says "This Agreement may not be transferred or assigned by the [seller] without the consent of the [obligor]" (i.e., the restriction does not refer to rights or obligations)? Is the result the same if the restriction says "The obligations of the [seller] under this Agreement may not be transferred or assigned by the [seller] without the consent of the [obligor]" (i.e., the restriction does not refer to rights)?

A breach of a contractual restriction prohibiting the transfer of monetary receivables does not lead to invalidity of the transfer of such receivables. Sale of non-monetary contractual rights in breach of contractual prohibition on transfer may be declared void by a court if it is proven that the purchaser knew, or should have known, of the prohibition.

According to Russian court practice, a sale of rights out of an agreement does not lead to the transfer of obligations under such an agreement, unless the contrary is indicated by the terms of the sale. Hence, each language indicated above has a similar effect in relation to the sale of rights.

4.7 Restrictions on Assignment; Liability to Obligor. If any of the restrictions in question 4.6 are binding, or if the receivables contract explicitly prohibits an assignment of receivables or "seller's rights" under the receivables contract, are such restrictions generally enforceable in your jurisdiction? Are there exceptions to this rule (e.g., for contracts between commercial entities)? If your jurisdiction recognises restrictions on sale or assignment of receivables and the seller nevertheless sells receivables to the purchaser, will either the seller or the purchaser be liable to the obligor for breach of contract or tort, or on any other basis?

The seller of monetary receivables acting in breach of a contractual prohibition will bear contractual liability before the obligor for such a breach.

4.8 Identification. Must the sale document specifically identify each of the receivables to be sold? If so, what specific information is required (e.g., obligor name, invoice number, invoice date, payment date, etc.)? Do the receivables being sold have to share objective characteristics? Alternatively, if the seller sells *all* of its receivables to the purchaser, is this sufficient identification of receivables? Finally, if the seller sells *all* of its receivables *other than* receivables owing by one or more specifically identified obligors, is this sufficient identification of receivables?

According to Russian court practice, in order for the transfer of rights to be effective, the particular transferred rights should be identified by the agreement of the parties or, at least, be identifiable from the context of such agreement and relations of the parties. In cases where all of the receivables of a seller are sold, each of them should still be identified to exclude risks related to such court practice.

In relation to the identification of future receivables, please refer to question 4.11 below.

4.9 Recharacterisation Risk. If the parties describe their transaction in the relevant documents as an outright sale and explicitly state their intention that it be treated as an outright sale, will this description and statement of intent automatically be respected or is there a risk that the transaction could be characterised by a court as a loan with (or without) security? If recharacterisation risk exists, what characteristics of the transaction might prevent the transfer from being treated as an outright sale? Among other things, to what extent may the seller retain any of the following without jeopardising treatment as an outright sale: (a) credit risk; (b) interest rate risk; (c) control of collections of receivables; (d) a right of repurchase/redemption; (e) a right to the residual profits within the purchaser; or (f) any other term?

A court, while considering a dispute in relation to a sale of receivables, might inquire into the economic characteristics of the transaction, the intent of the parties, etc. However, in the absence of bankruptcy, this will not normally lead to substantial risks to a sale of receivables in the course of securitisation.

In relation to effects of bankruptcy, please refer to questions 6.3 and 6.5 below.

4.10 Continuous Sales of Receivables. Can the seller agree in an enforceable manner to continuous sales of receivables (i.e., sales of receivables as and when they arise)? Would such an agreement survive and continue to transfer receivables to the purchaser following the seller's insolvency?

There are no specific provisions of Russian law in relation to the continuous sale of receivables. In our view, an agreement on the sale of receivables, as and when they arise, will be likely treated as an agreement on the sale of future receivables. As indicated in our answer to question 4.11 below, the future rights should be identifiable under the terms of the sale agreement. The latter may hinder or pose risks to some arrangements on the continuous sale of receivables.

4.11 Future Receivables. Can the seller commit in an enforceable manner to sell receivables to the purchaser that come into existence after the date of the receivables purchase agreement (e.g., "future flow" securitisation)? If so, how must the sale of future receivables be structured to be valid and enforceable? Is there a distinction between future receivables that arise prior to *versus* after the seller's insolvency?

Russian law allows for the sale of future receivables. However, the terms of sale should allow for identification of the receivables at the moment of their acquisition by the seller.

The operation of the sale of future receivables in bankruptcy remains untested. In relation to general claw-back risks under Russian bankruptcy law, please refer to question 6.3.

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4.12 Related Security. Must any additional formalities be fulfilled in order for the related security to be transferred concurrently with the sale of receivables? If not all related security can be enforceably transferred, what methods are customarily adopted to provide the purchaser the benefits of such related security?

Security, in relation to receivables in the form of pledge of receivables and movables, is generally transferred concurrently with the sale of such receivables. It should be noted, however, that a pledge of movables or receivables is not effective against third parties until it is recorded in a public registry of such pledges. Thus, it is necessary for a purchaser of secured receivables to submit a notification on the transfer of a pledge or a charge of movables to a notary in order for the transfer to be recorded in the registry.

Transfer of mortgages over immovables, as well as ships, aircrafts and other types of property which is treated similarly to immovables requires state registration to become effective. The transfer of a pledge over securities has to be recorded in the books of a registrar or depository that maintains custody of such securities.

4.13 Set-Off; Liability to Obligor. Assuming that a receivables contract does not contain a provision whereby the obligor waives its right to set-off against amounts it owes to the seller, do the obligor's set-off rights terminate upon its receipt of notice of a sale? At any other time? If a receivables contract does not waive set-off but the obligor's set-off rights are terminated due to notice or some other action, will either the seller or the purchaser be liable to the obligor for damages caused by such termination?

Assuming that a set-off right against due claims of the seller of receivables has occurred before a sale of receivables, such set-off right does not terminate on the grounds of a sale of receivables or receipt of the notice of such sale.

It is worth noting that, once insolvency proceedings are initiated, a set-off that violates statutory priority of insolvency creditors is not permitted.

4.14 Profit Extraction. What methods are typically used in your jurisdiction to extract residual profits from the purchaser?

In most cases, the so-called junior tranche (or junior debt) is used to extract excess spread from the purchaser. This junior tranche is normally structured as a contractually subordinated loan or a junior class of notes. It should be noted that in some transactions, among other things, preferred shares are used.

5 Security Issues

5.1 Back-up Security. Is it customary in your jurisdiction to take a "back-up" security interest over the seller's ownership interest in the receivables and the related security, in the event that an outright sale is deemed by a court (for whatever reason) not to have occurred and have been perfected (see question 4.9 above)?

It is not customary to provide for a "back-up" security interest in Russia, unless a special credit enhancement is provided in the transaction structure, though even in the latter case a back-up security would be an exotic option.

5.2 Seller Security. If it is customary to take back-up security, what are the formalities for the seller granting a security interest in receivables and related security under the laws of your jurisdiction, and for such security interest to be perfected?

Back-up security is not customary in Russian law. Please refer to question 5.1.

5.3 Purchaser Security. If the purchaser grants security over all of its assets (including purchased receivables) in favour of the providers of its funding, what formalities must the purchaser comply with in your jurisdiction to grant and perfect a security interest in purchased receivables governed by the laws of your jurisdiction and the related security?

If the purchaser plans to grant security over all of its assets (including purchased receivables) in favour of a third party (pledgee), the purchaser and the pledgee shall enter into a pledge agreement providing for a pledge over all assets of the purchaser in favour of the pledgee. In this case, no additional formalities would apply in order for a pledge of the newly purchased receivables to arise.

However, as indicated in our answer to question 4.12, a pledge of movables or receivables is not effective against third parties until it is recorded in a public registry of such pledges.

Please note that a pledge of all assets of a pledgor is quite new and remains untested in Russian courts.

5.4 Recognition. If the purchaser grants a security interest in receivables governed by the laws of your jurisdiction, and that security interest is valid and perfected under the laws of the purchaser's jurisdiction, will the security be treated as valid and perfected in your jurisdiction or must additional steps be taken in your jurisdiction?

If the purchaser grants a security interest in receivables, and that security interest is valid and perfected under the laws of the country where the purchaser is located, it will be generally treated as valid and perfected under Russian law as well.

There may be exceptions in cases where this conflicts with the mandatory rules of Russian law or Russian public policy.

5.5 Additional Formalities. What additional or different requirements apply to security interests in or connected to insurance policies, promissory notes, mortgage loans, consumer loans or marketable debt securities?

Security interests in insurance policies and promissory notes are not customary in Russia. Russian law does not provide for any specific requirements applying to such security interests.

Requirements applying to a pledge of marketable debt securities vary depending on the type of securities: for instance, a pledge of non-documentary securities becomes effective after entry on such pledge has been made into the account where the rights of the owner of the securities are registered.

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There are no additional requirements for a pledge of rights under mortgage loans. However, if the rights under such loans are certified by mortgage certificates the requirements on a pledge of securities will apply.

5.6 Trusts. Does your jurisdiction recognise trusts? If not, is there a mechanism whereby collections received by the seller in respect of sold receivables can be held or be deemed to be held separate and apart from the seller's own assets (so that they are not part of the seller's insolvency estate) until turned over to the purchaser?

Russian law does not recognise trusts.

Cash proceeds received by the seller from obligors in respect of sold receivables may be held in a separate bank account of the seller, pledged in favour of the purchaser until turned over to the purchaser.

However, in practice, separation of the proceeds out of the sold receivables from the seller's assets is usually achieved via instructing the obligors to make payments under the respective receivables directly to the purchaser's account.

5.7 Bank Accounts. Does your jurisdiction recognise escrow accounts? Can security be taken over a bank account located in your jurisdiction? If so, what is the typical method? Would courts in your jurisdiction recognise a foreign law grant of security (for example, an English law debenture) taken over a bank account located in your jurisdiction?

Yes, Russian law recognises escrow accounts.

Under Russian law, security over a bank account is taken via entering into a pledge agreement with the holder of such account. It should be noted that for the pledge to become effective the bank account has to be specifically designated as a "pledge account" in the bank's books. The bank also has to be notified on creation of a pledge.

Notably, Russian law directly prescribes that the receivables serving as collateral under the bonds (issued in the course of a non-mortgage securitisation, repack or similar transaction) must be credited to a bank account pledged in favour of the bondholders.

Under Russian law, parties are free to choose a foreign law grant of security unless it conflicts with public order and/or the mandatory laws of Russia. However, security of bank accounts under foreign legislation is still untested in Russian courts. It is also possible that enforcement of such a pledge in Russia may be more challenging compared to the use of Russian law to govern such pledge.

5.8 Enforcement over Bank Accounts. If security over a bank account is possible and the secured party enforces that security, does the secured party control all cash flowing into the bank account from enforcement forward until the secured party is repaid in full, or are there limitations? If there are limitations, what are they?

Enforcement over pledged bank accounts is carried out in court unless an agreement between the pledgor and the pledgee stipulates for an out-of-court enforcement procedure.

Russian law provides for a number of instances when enforcement is only possible upon court decision.

The claims of the pledgee are satisfied by debiting the pledged account of the pledgor upon written request of the pledgee, and further payment/transfer of funds to the pledgee.

The claims of the pledgee enjoy priority over the claims of other creditors to be satisfied out of the value of the security.

5.9 Use of Cash Bank Accounts. If security over a bank account is possible, can the owner of the account have access to the funds in the account prior to enforcement without affecting the security?

Yes, the owner of the pledged account is free to manage funds in the pledge account unless otherwise stipulated by the pledge agreement or the law.

Under the Russian law, the owner has no access to the funds in the pledged account in the following instances:

- the pledge agreement contains a provision on a fixed amount, and the amount of funds in the account would fall below the defined amount as a result of the pledgor's actions; or
- the bank has received a written notification on non-performance/inappropriate performance of the secured obligations by the pledgor, and the amount of funds on the pledge account would fall below an amount equivalent to the obligations secured by the account.

6 Insolvency Laws

6.1 Stay of Action. If, after a sale of receivables that is otherwise perfected, the seller becomes subject to an insolvency proceeding, will your jurisdiction's insolvency laws automatically prohibit the purchaser from collecting, transferring or otherwise exercising ownership rights over the purchased receivables (a "stay of action")? If so, what generally is the length of that stay of action? Does the insolvency official have the ability to stay collection and enforcement actions until he determines that the sale is perfected? Would the answer be different if the purchaser is deemed to only be a secured party rather than the owner of the receivables?

The imposition of bankruptcy procedures against the seller does not prohibit the seller from collecting, transferring or otherwise exercising ownership rights over the purchased receivables.

To the contrary, under Russian law, the insolvency estate of a bankrupt debtor may consist only of the assets owned by such debtor. After the purchase of receivables is effected, such receivables are no longer owned by their seller, hence, the imposition of bankruptcy against the seller would not restrict the ownership rights of their purchaser, unless the sale of receivables is challenged and declared void. In relation to general claw-back risks under Russian bankruptcy law please refer to question 6.3.

Under Russian law, a transaction that intends to have an effect of receivables sale or a similar effect, generally, would not be structured so that the purchaser of receivables is deemed to be only a secured party rather than owner of the receivables.

6.2 Insolvency Official's Powers. If there is no stay of action, under what circumstances, if any, does the insolvency official have the power to prohibit the purchaser's exercise of its ownership rights over the receivables (by means of injunction, stay order or other action)?

An insolvency official does not have the power to prohibit the purchaser's exercise of rights. However, an insolvency administrator

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is entitled to challenge the insolvent debtor's transactions, including sales of receivables (please refer to question 6.3).

6.3 Suspect Period (Clawback). Under what facts or circumstances could the insolvency official rescind or reverse transactions that took place during a "suspect" or "preference" period before the commencement of the seller's insolvency proceedings? What are the lengths of the "suspect" or "preference" periods in your jurisdiction for (a) transactions between unrelated parties, and (b) transactions between related parties? If the purchaser is majority-owned or controlled by the seller or an affiliate of the seller, does that render sales by the seller to the purchaser "related party transactions" for purposes of determining the length of the suspect period? If a parent company of the seller guarantee's the performance by the seller of its obligations under contracts with the purchaser, does that render sales by the seller to the purchaser "related party transactions" for purposes of determining the length of the suspect period?

Assets that were disposed of by the insolvent debtor may be returned into its insolvency estate as a result of challenging "suspect" or "preference" transactions of the debtor before a respective bankruptcy court.

Such transactions may be challenged by an insolvency administrator acting on behalf of the insolvent debtor at the administrator's own discretion or under a decision of a general assembly or committee of creditors.

"Suspect" transactions include:

- transactions that do not envisage equal consideration from the insolvent debtor's counter-agent ("suspect" period: one year before the proper receipt of a bankruptcy application by the bankruptcy court); and
- transactions entered into with a purpose of harming property rights of creditors ("suspect" period: three years before the proper receipt of a bankruptcy application by the bankruptcy court).

A "preference" transaction means a transaction that may lead to one creditor being privileged as compared to other creditors in relation to the satisfaction of its claims. In general a "preference" period is one month before the receipt of a bankruptcy application.

However, a "preference" period is prolonged to six months before the above-mentioned date in relation to transactions that:

- are aimed at securing an obligation before a particular creditor of the insolvent debtor and effectively lead to a change to the creditors' order of priority; or
- were entered into when a counterparty to such transaction knew of the insolvency or insufficiency of assets.

In each case the "suspect" and "preference" periods continue from receipt of a bankruptcy application until liquidation of the insolvent debtor or dismantling of the bankruptcy proceedings.

Whether the parties to "suspect" or "preference" transactions are affiliated does not, in itself, influence treatment of such transactions.

6.4 Substantive Consolidation. Under what facts or circumstances, if any, could the insolvency official consolidate the assets and liabilities of the purchaser with those of the seller or its affiliates in the insolvency proceeding? If the purchaser is owned by the seller or by an affiliate of the seller, does that affect the consolidation analysis?

As indicated in our response to question 6.1, the insolvency estate of an insolvent debtor consists only of the assets owned by such debtor.

Hence, the insolvency administrator or bankruptcy court cannot consolidate the assets and liabilities of the insolvency official with those of any other person, including a seller of receivables or its affiliates.

6.5 Effect of Insolvency on Receivables Sales. If insolvency proceedings are commenced against the seller in your jurisdiction, what effect do those proceedings have on (a) sales of receivables that would otherwise occur after the commencement of such proceedings, or (b) on sales of receivables that only come into existence after the commencement of such proceedings?

Commencement of bankruptcy proceedings does not, in itself, have any effect on the sales of receivables that would otherwise occur after the commencement of such proceedings or receivables that only come into existence after the commencement of such proceedings.

However, a bankruptcy administrator may terminate (accelerate) agreements (including agreements on sales of receivables) entered into by the insolvent debtor in the cases similar to "executory contract" of English law.

The Russian law provisions on executory contracts apply to transactions which: (i) have not been performed in full or in part; and (ii) preclude the reinstatement of the debtor's solvency; or (iii) would result in damages to the debtor when compared to analogous transactions concluded in similar circumstances.

Also from the moment of imposition of bankruptcy proceedings, the insolvent debtor is prohibited from disposing of its assets, including receivables, comprising more than 5% of its total assets.

6.6 Effect of Limited Recourse Provisions. If a debtor's contract contains a limited recourse provision (see question 7.3 below), can the debtor nevertheless be declared insolvent on the grounds that it cannot pay its debts as they become due?

Russian law explicitly recognises limited recourse provisions in relation to special purpose entities (SPEs). In relation to this, please refer to question 7.4 below.

Limited recourse provisions in other relationships are not directly recognised by Russian law or court practice.

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7 Special Rules

7.1 Securitisation Law. Is there a special securitisation law (and/or special provisions in other laws) in your jurisdiction establishing a legal framework for securitisation transactions? If so, what are the basics? Is there a regulatory authority responsible for regulating securitisation transactions in your jurisdiction?

There is a special law regulating the securitisation of mortgage loans – Federal Law, No. 152-FZ, "On Mortgage-Backed Securities", dated 11 November 2003. Since 1 July 2014, Russia has had a special legal framework for non-mortgage securitisation assets, which was introduced by adopting Federal Law, No. 379-FZ, "On introducing amendments into certain legislative acts of the Russian Federation", dated 21 December 2013.

Central Bank of Russia is the regulatory authority responsible for regulating securitisation transactions in Russia.

7.2 Securitisation Entities. Does your jurisdiction have laws specifically providing for establishment of special purpose entities for securitisation? If so, what does the law provide as to: (a) requirements for establishment and management of such an entity; (b) legal attributes and benefits of the entity; and (c) any specific requirements as to the status of directors or shareholders?

Russian laws explicitly provide for the establishment of SPEs for securitisation purposes:

- "mortgage agents" ("MAs") for the purposes of mortgage loans securitisation;
- "special financial organisations" ("SFOs") for non-mortgage securitisations; and
- "special organisations for project finance" ("SOPFs") for the issuance of project finance bonds.

Regulations for all types of SPEs are quite similar.

An SPE of any type shall have a separate management company and a separate accounting company which shall not be affiliated with the SPE and/or the originator. Shareholders of the SFOs and SOPFs cannot be owned by legal entities registered in states or territories where it is not required to disclose information on financial operations.

All types of SPEs are prohibited to have employees and have restrictions on their liquidation.

The above-mentioned requirements are aimed at compliance with the concept of SPE bankruptcy remoteness.

7.3 Location and form of Securitisation Entities. Is it typical to establish the special purpose entity in your jurisdiction or offshore? If in your jurisdiction, what are the advantages to locating the special purpose entity in your jurisdiction? If offshore, where are special purpose entities typically located for securitisations in your jurisdiction? What are the forms that the special purpose entity would normally take in your jurisdiction and how would such entity usually be owned?

Given that the demand for securitisation notes originated in Russia lies presently in the local market, the transactions are mostly structured onshore and use a Russian SPV set up as a mortgage agent or specialised financial entity – in each case as an SPV with the capacity restricted by law and its constitutive documents. In transactions with a foreign SPV, the parties usually choose the Netherlands and Luxembourg.

7.4 Limited-Recourse Clause. Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) limiting the recourse of parties to that agreement to the available assets of the relevant debtor, and providing that to the extent of any shortfall the debt of the relevant debtor is extinguished?

Yes, based on Russian law, a decision on the issuance of bonds or agreement(s) between an SPE and its creditor may contain provisions on the release of such SPE from liabilities under any obligations which remain unsatisfied after enforcement of all available securities.

Provisions on limited-recourse clauses are applicable to all types of SPEs.

It should be noted, however, that the provision of limited-recourse is quite new and remains untested in courts.

7.5 Non-Petition Clause. Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) prohibiting the parties from: (a) taking legal action against the purchaser or another person; or (b) commencing an insolvency proceeding against the purchaser or another person?

Yes, according to Clause 2 of Article 230.1 of the Bankruptcy Law, no creditor of an SPE (except the Bondholders) will be able to claim the SPE's bankruptcy if there is necessary non-petition language in the agreements between such creditor and the SPE. The SPE is not prohibited from entering into agreements that do not contain non-petition language, though it is advisable to include such language in all significant agreements of the SPE.

7.6 Priority of Payments "Waterfall". Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) distributing payments to parties in a certain order specified in the contract?

Russian law explicitly allows creditors to enter into agreements regulating the order of priority of their claims having obligatory effect among such creditors. It should be noted, however, that such agreements have not been tested in a bankruptcy court. There is a risk that a bankruptcy court would not recognise a change in a creditor's order of priority envisaged by the inter-creditor agreements. In this case the creditors would be contractually obliged to compensate one another for losses occurred due to breach of priority arrangements provided by an inter-creditor agreement.

Moreover, Russian law directly allows for the subordination of claims of an SPE's creditors (including bondholders) in relation to a common collateral.

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7.7 Independent Director. Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) or a provision in a party's organisational documents prohibiting the directors from taking specified actions (including commencing an insolvency proceeding) without the affirmative vote of an independent director?

Russian law does not specifically provide for the existence of independent directors for SPEs since they are managed by separate management companies.

We should note that a bonds issuer under current regulations must appoint a bondholders' representative in relation to each secured bond issuance starting from July 1 2016.

A bondholders' representative shall act in the name and interest of the bondholders of a particular bond issue and protect their rights.

In particular, a bondholders' representative may be entitled to give consent to certain actions of an issuer (including an SPE) in the interest of the bondholders.

7.8 Location of Purchaser. Is it typical to establish the purchaser in your jurisdiction or offshore? If in your jurisdiction, what are the advantages to locating the purchaser in your jurisdiction? If offshore, where are purchasers typically located for securitisations in your jurisdiction?

Given that the demand for securitisation notes originated in Russia lies presently in the local market, the transactions are mostly structured onshore and use a Russian SPV set up as a mortgage agent or specialised financial entity – in each case as an SPV with the capacity restricted by law and its constitutive documents. In transactions with a foreign SPV, the parties usually choose the Netherlands and Luxembourg.

8 Regulatory Issues

8.1 Required Authorisations, etc. Assuming that the purchaser does no other business in your jurisdiction, will its purchase and ownership or its collection and enforcement of receivables result in its being required to qualify to do business or to obtain any licence or its being subject to regulation as a financial institution in your jurisdiction? Does the answer to the preceding question change if the purchaser does business with more than one seller in your jurisdiction?

No licence or authorisation is required to do business.

8.2 Servicing. Does the seller require any licences, etc., in order to continue to enforce and collect receivables following their sale to the purchaser, including to appear before a court? Does a third-party replacement servicer require any licences, etc., in order to enforce and collect sold receivables?

Enforcing and collecting sold receivables does not in itself require a licence according to Russian law.

However, from a practical standpoint, for certain types of securitisations (mainly, consumer loans and credit cards) it is advisable for a servicer to possess a banking or similar licence to service the sold receivables.

8.3 Data Protection. Does your jurisdiction have laws restricting the use or dissemination of data about or provided by obligors? If so, do these laws apply only to consumer obligors or also to enterprises?

Federal Law, No. 152-FZ, "On Personal Data", dated 27 July 2006 (the "Data Protection Law") restricts the use and dissemination of data of private individuals. As a general rule, to satisfy the requirements of the Data Protection Law a purchaser acquiring the receivables of individuals must receive consent from such individuals to process their data. It is customary to include respective consent into the set of documents signed before extension of a particular retail loan.

A notable exception to this rule is provided by the Consumer Loan Law which explicitly allows the retail lenders to communicate the personal data of consumer lenders to the purchasers of the consumer loan receivables.

The Data Protection Law does not apply to the data of legal entities.

Notably, banks are also subject to regulations on banking secrecy which may apply to the dissemination of information in the course of sale of receivables to non-banking organisations. An issue of application of these regulations to securitisation is still not fully resolved.

Also worth mentioning is that the Consumer Loan Law explicitly obliges the purchasers of consumer loan receivables to protect personal data, information covered by banking secrecy and other confidential information obtained as a result of purchase of such receivables.

8.4 Consumer Protection. If the obligors are consumers, will the purchaser (including a bank acting as purchaser) be required to comply with any consumer protection law of your jurisdiction? Briefly, what is required?

The purchaser of consumer loan receivables will have to comply with the provisions of the Consumer Loan Law applicable to creditors under consumer loans. Most significant provisions of the Consumer Loan Law have already been indicated in our answers to questions 1.2 and 8.3 above.

8.5 Currency Restrictions. Does your jurisdiction have laws restricting the exchange of your jurisdiction's currency for other currencies or the making of payments in your jurisdiction's currency to persons outside the country?

Currency exchange operations in Russia may only be carried out with Russian banks.

Under Russian law, payments between Russian residents may only be made in local currency (Russian Roubles – RUB). Foreign currency can be used to determine the price of contracts/instruments but the payment and settlement shall be generally effected in RUB.

Payments in RUB to non-residents are, mostly, unrestricted. It should be noted, however, that payments in RUB between Russian residents from or to accounts outside of Russia are subject to various currency restrictions.

8.6 Risk Retention. Does your jurisdiction have laws or regulations relating to "risk retention"? How are securitisation transactions in your jurisdiction usually structured to satisfy those risk retention requirements?

Yes, there are regulations relating to risk retention.

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Federal Law 39-FZ "On the Securities Market" governs the main provisions relating to risk retention. Bank of Russia Ordinance № 3309-U, dated 7 July 2014, "On the Forms and Methods of Accepting Risks on Bonds Pledged with Collateral of the Special Finance Vehicles and Special Project Vehicles" clarifies Federal Law 39-FZ and establishes functions performed by the credit institution (initial lender, subsequent lender, surety, guarantor, pledger), or other functions that lead to acceptance by the credit institution of risks in the framework of assignment of receivables transactions, depending on the type of assets (mortgage loans, consumer loans, SME loans, claims under leasing agreements).

There are different ways to structure securitisation transactions to satisfy risk retention requirements in Russia, but surety or mezzanine tranches are the most common.

8.7 Regulatory Developments. Have there been any regulatory developments in your jurisdiction which are likely to have a material impact on securitisation transactions in your jurisdiction?

No, there have not been any regulatory developments in Russia relating to the assignment of receivables, but law enforcement practice does not stand still and every year new types of receivables are used for securitisation. Nevertheless, regulations of the so-called STC (simple, transparent and comparable) securitisation will soon change, which can significantly affect the purchase of securitisation assets.

Also, the changes in rating regulations, including establishment of The Analytical Credit Rating Agency (ACRA), strongly influenced the market as new methodology appeared (for more details, see: https://www.acra-ratings.com/).

9 Taxation

9.1 Withholding Taxes. Will any part of payments on receivables by the obligors to the seller or the purchaser be subject to withholding taxes in your jurisdiction? Does the answer depend on the nature of the receivables, whether they bear interest, their term to maturity, or where the seller or the purchaser is located? In the case of a sale of trade receivables at a discount, is there a risk that the discount will be recharacterised in whole or in part as interest? In the case of a sale of trade receivables where a portion of the purchase price is payable upon collection of the receivable, is there a risk that the deferred purchase price will be recharacterised in whole or in part as interest? If withholding taxes might apply, what are the typical methods for eliminating or reducing withholding taxes?

In general, repayment of principal on receivables by a Russian obligor to a non-resident legal entity should not be subject to Russian withholding tax.

Income in the form of interest, accreted notional and fines or penalties for breach of contractual obligations paid by Russian legal entities (but not private individuals) to non-resident legal entities are generally levied with a withholding tax in accordance with the Russian Tax Code. The tax rate is generally 20% though it may be reduced depending on the sphere of business and territory within Russia where the receivables originated. The tax rate may also be reduced under an applicable double tax treaty between Russia and the relevant foreign jurisdiction.

There is some risk that income originated due to purchase of the receivables of a legal entity at a discount can be treated as interest income subject to withholding tax.

Payment of the purchase price upon collection of the receivable, i.e. deferred purchase price, should not be requalified as interest payments and, thus, should not lead to withholding tax in Russia.

It is worth noting that income generated by non-resident legal entities that conduct business in Russia via permanent establishment, including income from purchased receivables, is taxed at the level of such permanent establishment and is not subject to withholding tax.

9.2 Seller Tax Accounting. Does your jurisdiction require that a specific accounting policy is adopted for tax purposes by the seller or purchaser in the context of a securitisation?

In accordance with Russian law, there is no specific accounting policy which has to be adopted by the seller or purchaser in the context of a securitisation transaction and in connection to Russian tax law.

9.3 Stamp Duty, etc. Does your jurisdiction impose stamp duty or other transfer or documentary taxes on sales of receivables?

No stamp duty or other transfer or documentary taxes are imposed on sales of receivables.

9.4 Value Added Taxes. Does your jurisdiction impose value added tax, sales tax or other similar taxes on sales of goods or services, on sales of receivables or on fees for collection agent services?

As a general rule, the sale of receivables performed by the seller registered for tax purposes in Russia is subject to Russian value added tax (VAT). VAT exemptions are in place depending on the nature of the receivables, e.g. the sale of receivables arising from monetary loan agreements is VAT exempt along with the sale of securities (shares, bonds, promissory notes, etc.) and certain derivatives.

9.5 Purchaser Liability. If the seller is required to pay value-added tax, stamp duty or other taxes upon the sale of receivables (or on the sale of goods or services that give rise to the receivables) and the seller does not pay, then will the taxing authority be able to make claims for the unpaid tax against the purchaser or against the sold receivables or collections?

Generally, based on the Russian VAT law, the tax authorities shall not make such claims in respect of VAT unless the purchaser is recognised as liable to act in the capacity of tax agent. The liability to act as a tax agent arises for the purchaser if it is registered for tax purposes in Russia and purchases goods, works, services or receivables subject to Russian VAT from the seller which is not registered for tax purposes in Russia.

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9.6 Doing Business. Assuming that the purchaser conducts no other business in your jurisdiction, would the purchaser's purchase of the receivables, its appointment of the seller as its servicer and collection agent, or its enforcement of the receivables against the obligors, make it liable to tax in your jurisdiction?

The purchase of receivables by the purchaser, appointment of the seller as its servicer or collecting agent or enforcement of receivables against the obligors should not, in itself, make the purchaser subject to Russian profits tax, provided the purchaser does not have a permanent establishment in Russia. In order to minimise the risk of permanent establishment the following should, among other things, be observed:

- managerial functions, including making strategic and operational decisions relating to the purchaser's activities, should be performed outside Russia; and
- any party of the transaction should not represent the purchaser's interests in Russia based on contractual agreements, or have, and regularly exercise, the authority to conclude contracts or negotiate material terms of such contracts in the name of the purchaser.

If a purchaser of a receivable does not conduct its business in Russia via a permanent establishment, the proceeds from purchased receivables may be subject to withholding tax (please refer to question 9.1).

9.7 Taxable Income. If a purchaser located in your jurisdiction receives debt relief as the result of a limited recourse clause (see question 7.3 above), is that debt relief liable to tax in your jurisdiction?

Russian SPVs are carved out of income tax. The issue has not been specifically addressed in practice, but we believe that these provisions allow excluding tax consequences associated with debt relief, when such debt relief occurs in connection with the SPV's core business activities related to the issuance of notes.

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LECAP is a leading legal adviser on capital markets, corporate/M&A and finance projects with a proven track record of:

- 400+ bond issuances;
- 200+ share issuances;
- 50+ debt restructurings;
- 45+ M&A and reorganisations;
- 17 concession agreements; and
- 45+ drafts of laws.

The firm provides turnkey securitisation services to originators, arrangers, investors and other parties to a transaction. LECAP securitisation includes three partners and advises on the first and ground-breaking transactions in the Russian market. Legal opinions issued by LECAP are recognised by international rating agencies (Moody's, Fitch, Standard & Poor's) as well as local ones.

LECAP has been recognised as Best DCM Law Firm for six years in a row (2012–2017) based on the survey of market professionals conducted by Cbonds. The firm's expertise in capital markets, corporate law and PPP is regularly acknowledged by leading international legal directories.

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Scotland

Bruce Stephen

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1 Receivables Contracts

1.1 Formalities. In order to create an enforceable debt obligation of the obligor to the seller: (a) is it necessary that the sales of goods or services are evidenced by a formal receivables contract; (b) are invoices alone sufficient; and (c) can a binding contract arise as a result of the behaviour of the parties?

It is generally not necessary for the sale of goods or services to be evidenced by a formal receivables contract. Certain types of contract are required to be in writing in order to be binding between the parties. An invoice in conjunction with the actings of the parties may be sufficient to establish a contract between the parties and evidence a debt.

1.2 Consumer Protections. Do your jurisdiction's laws: (a) limit rates of interest on consumer credit, loans or other kinds of receivables; (b) provide a statutory right to interest on late payments; (c) permit consumers to cancel receivables for a specified period of time; or (d) provide other noteworthy rights to consumers with respect to receivables owing by them?

In consumer credit arrangements, there are statutory restrictions which may affect interest chargeable. Excessive interest could be challenged if, prior to 6 April 2007, it constituted an extortionate credit transaction under s.137 of the Consumer Credit Act 1974 (the CCA) and from 6 April 2007 it constituted an unfair relationship under s.140A of the CCA. Default interest provisions which are penalties may be unenforceable. Certain provisions in consumer contracts may be unenforceable as being unfair under the Unfair Terms in Consumer Contracts Regulations 1999, in relation to consumer contracts entered into prior to 1 October 2015, and the Consumer Rights Act 2015 in respect of consumer contracts entered into from 1 October 2015.

The Late Payment of Commercial Debts (Interest) Act 1998 provides for payment of interest in commercial transactions where the parties have not specified that interest is payable following late payment under the contract. The Act applies to commercial contracts for the sale of goods and services but does not apply to consumer contracts.

The CCA contains consumer protections regarding certain forms of consumer credit arrangement, including the ability for the consumer to cancel receivables contracts within a specified period of time.

1.3 Government Receivables. Where the receivables contract has been entered into with the government or a government agency, are there different requirements and laws that apply to the sale or collection of those receivables?

With the exception of potential immunity issues associated with state entities, there are no different requirements and laws applicable to the sale or collection of receivables from the government or government agencies in Scotland.

2 Choice of Law – Receivables Contracts

2.1 No Law Specified. If the seller and the obligor do not specify a choice of law in their receivables contract, what are the main principles in your jurisdiction that will determine the governing law of the contract?

The choice of law is determined with reference to the Contracts (Applicable Law) Act 1990 (the 1990 Act), the Rome I Regulation (Regulation (EC) 593/2008, dated 17 June 2008) or Scots common law. The 1990 Act applies the Rome Convention on contractual obligations (the Rome Convention) in respect of contracts entered into before 17 December 2009 and the Rome I Regulation (implemented in Scotland by The Law Applicable to Contractual Obligations (Scotland) Regulations 2009/410) applies to contracts entered into as from that date.

Under the Rome Convention, in the absence of an express choice of law, the principle of closest connection is applied in determining the law of the contract. Closest connection is presumed to be: the country where a party who is to effect the performance of the contract has its habitual residence (or equivalent), unless the contract is entered into in the course of a party's trade or profession in which case the closest connection is presumed to be the country in which the party's principal business is located; or if performance is in another place of business, the country where that other place is located.

Under the Rome I Regulation the position is similar, save that habitual residence is a fixed rule with exceptions for particular contract classes where specific rules apply. If, however, it is clear that the contract is more closely connected with the law of a different country, the law of that country is the applicable law.

To the extent the relevant contract is beyond the scope of the 1990 Act or the Rome I Regulation, Scots common law will determine the choice of law where the contract is silent. Scots common law

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applies the 'proper law' to the contract, this being the law which the parties intended or may fairly be presumed to have intended to invoke in creating the contractual relationship.

2.2 Base Case. If the seller and the obligor are both resident in your jurisdiction, and the transactions giving rise to the receivables and the payment of the receivables take place in your jurisdiction, and the seller and the obligor choose the law of your jurisdiction to govern the receivables contract, is there any reason why a court in your jurisdiction would not give effect to their choice of law?

No, there is not.

2.3 Freedom to Choose Foreign Law of Non-Resident Seller or Obligor. If the seller is resident in your jurisdiction but the obligor is not, or if the obligor is resident in your jurisdiction but the seller is not, and the seller and the obligor choose the foreign law of the obligor/seller to govern their receivables contract, will a court in your jurisdiction give effect to the choice of foreign law? Are there any limitations to the recognition of foreign law (such as public policy or mandatory principles of law) that would typically apply in commercial relationships such as that between the seller and the obligor under the receivables contract?

The parties may expressly choose the governing law relating to the contract and such choice will be recognised by the Scottish courts under certain exceptions specified under the 1990 Act or the Rome I Regulation. For contracts beyond the scope of the 1990 Act or the Rome I Regulation, the Scottish courts are likely, subject to issues of public policy, to recognise the express choice of law of the parties, provided such choice of law coincides with the intention of the parties. It should be noted that, to the extent a law other than Scots law is expressly applied to the contract, such choice of law would need to be pled in order for it to be recognised by the Scottish courts.

3 Choice of Law – Receivables Purchase Agreement

3.1 Base Case. Does your jurisdiction's law generally require the sale of receivables to be governed by the same law as the law governing the receivables themselves? If so, does that general rule apply irrespective of which law governs the receivables (i.e., your jurisdiction's laws or foreign laws)?

The parties are generally permitted to choose the law to govern contractual obligations between them including those arising under a receivables purchase agreement.

It is common for portfolios of Scottish receivables to be sold under a contract governed by a law other than Scots law. It is not necessary for the contract of sale to be governed by the same law as the underlying receivables. To the extent that the sale contract creates rights to the underlying receivables beyond mere contractual rights (for example, the purchaser acquiring an equitable proprietary interest in the underlying receivables by execution of the sale contract only), it is unlikely that such additional rights would be effective in respect of Scottish receivables without further action being required.

3.2 Example 1: If (a) the seller and the obligor are located in your jurisdiction, (b) the receivable is governed by the law of your jurisdiction, (c) the seller sells the receivable to a purchaser located in a third country, (d) the seller and the purchaser choose the law of your jurisdiction to govern the receivables purchase agreement, and (e) the sale complies with the requirements of your jurisdiction, will a court in your jurisdiction recognise that sale as being effective against the seller, the obligor and other third parties (such as creditors or insolvency administrators of the seller and the obligor)?

Yes, the Scottish courts will recognise the express choice of Scots law.

3.3 Example 2: Assuming that the facts are the same as Example 1, but either the obligor or the purchaser or both are located outside your jurisdiction, will a court in your jurisdiction recognise that sale as being effective against the seller and other third parties (such as creditors or insolvency administrators of the seller), or must the foreign law requirements of the obligor's country or the purchaser's country (or both) be taken into account?

It is likely that the Scottish courts will recognise the sale contract and in particular give effect to the sale to the purchaser in questions against the seller and any creditor of, or insolvency practitioner appointed to, the seller. The effect of the sale contract in questions against the relevant obligor and the purchaser may require local country law to be considered.

3.4 Example 3: If (a) the seller is located in your jurisdiction but the obligor is located in another country, (b) the receivable is governed by the law of the obligor's country, (c) the seller sells the receivable to a purchaser located in a third country, (d) the seller and the purchaser choose the law of the obligor's country to govern the receivables purchase agreement, and (e) the sale complies with the requirements of the obligor's country, will a court in your jurisdiction recognise that sale as being effective against the seller and other third parties (such as creditors or insolvency administrators of the seller) without the need to comply with your jurisdiction's own sale requirements?

It is likely that the Scottish courts will recognise the choice of law in respect of the sale contract and will not require any additional Scots law formalities to be complied with, in order to give effect to the transfer of the receivables pursuant to the sale in questions against the seller, the creditors of, or insolvency administrator appointed to, the seller.

3.5 Example 4: If (a) the obligor is located in your jurisdiction but the seller is located in another country, (b) the receivable is governed by the law of the seller's country, (c) the seller and the purchaser choose the law of the seller's country to govern the receivables purchase agreement, and (d) the sale complies with the requirements of the seller's country, will a court in your jurisdiction recognise that sale as being effective against the obligor and other third parties (such as creditors or insolvency administrators of the obligor) without the need to comply with your jurisdiction's own sale requirements?

See the answer to question 3.4 above.

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3.6 Example 5: If (a) the seller is located in your jurisdiction (irrespective of the obligor's location), (b) the receivable is governed by the law of your jurisdiction, (c) the seller sells the receivable to a purchaser located in a third country, (d) the seller and the purchaser choose the law of the purchaser's country to govern the receivables purchase agreement, and (e) the sale complies with the requirements of the purchaser's country, will a court in your jurisdiction recognise that sale as being effective against the seller and other third parties (such as creditors or insolvency administrators of the seller, any obligor located in your jurisdiction and any third party creditor or insolvency administrator of any such obligor)?

It is likely that the Scottish courts will recognise the choice of law in respect of the sale contract. On the basis that the receivables are governed by Scots law, the transfer of the receivables pursuant to the sale in compliance with the requirements of the purchaser's country will be recognised by the Scottish courts, provided they also comply with the Scots law requirements in respect of the transfer of such receivables.

4 Asset Sales

4.1 Sale Methods Generally. In your jurisdiction what are the customary methods for a seller to sell receivables to a purchaser? What is the customary terminology – is it called a sale, transfer, assignment or something else?

The most common way for a seller to sell receivables to a purchaser is by means of a sale contract, supported by an assignation or assignment of the receivables with notice to the relevant obligors; or, where notice is unattractive (or inconsistent with arrangements to be put in place in other jurisdictions for that particular portfolio), a trust is declared over the relevant interests under the receivables contracts and related receivables and cash receipts. Scots law does not recognise equitable transfers in respect of Scottish assets and, accordingly, an equitable assignment of the receivable would not, as a matter of Scots law, pass a proprietary interest in the receivables to the purchaser. The trust would, however, create a protected interest in the Scottish receivables which would be good against the seller or any insolvency official appointed to the seller.

4.2 Perfection Generally. What formalities are required generally for perfecting a sale of receivables? Are there any additional or other formalities required for the sale of receivables to be perfected against any subsequent good faith purchasers for value of the same receivables from the seller?

The sale of Scottish receivables is perfected by the relevant obligors receiving notice of the assignation. Scots law recognises various forms of notice. While the assignation is effective from the date of receipt of notice by the obligor, an acknowledgment of such notice provides evidence of both receipt and understanding of the new arrangements by the relevant obligor.

If the same receivables are assigned by the seller to several third-party purchasers all acting in good faith, the order of priority between such purchasers is determined by the date of receipt of notice by the obligor of the assignations. Accordingly, a subsequent third-party purchaser who acquires in good faith and notifies the obligor first will take a better title to the receivables than the first purchaser and any intervening purchaser.

4.3 Perfection for Promissory Notes, etc. What additional or different requirements for sale and perfection apply to sales of promissory notes, mortgage loans, consumer loans or marketable debt securities?

Mortgage loans and related security are transferred by formal assignation with notice and, in the case of the transfer of the mortgage security, by registration of such transfer at the Scottish land registers. Many securitisations are structured on the basis of equitable assignments of mortgage loans and related security. Generally, such arrangements are implemented in Scotland by means of an express trust.

Securities which are in bearer form are generally transferable by mere delivery of the relevant security certificate. Instruments which are negotiable in nature may be transferred by a combination of endorsement and delivery with, in certain circumstances, notice to the relevant obligor under the instrument. Bearer form securities issued by UK companies are now restricted in the UK by virtue of the Small Business, Enterprise and Employment Act 2015.

4.4 Obligor Notification or Consent. Must the seller or the purchaser notify obligors of the sale of receivables in order for the sale to be effective against the obligors and/or creditors of the seller? Must the seller or the purchaser obtain the obligors' consent to the sale of receivables in order for the sale to be an effective sale against the obligors? Whether or not notice is required to perfect a sale, are there any benefits to giving notice – such as cutting off obligor set-off rights and other obligor defences?

Notice is a requirement of Scots law for the formal transfer of the seller's interest in the receivable. Prior to notification the obligor can obtain a valid discharge of the debt by paying the seller. The proprietary interest in the receivable remains with the seller until notice of the transfer is given to the obligor. Consequently, unless a trust has been declared over the receivables, such interests are available to the creditors of the seller on insolvency.

The consent of the obligor to the sale is not necessary unless expressly required under the contract or unless the principle of *delictus personae* applies (the contract being of a nature specific to the parties to it). The contract does not need to contain an express permission for a party's interest to be assignable.

Notice has the effect of limiting rights of set-off affecting the receivables arising from other ongoing arrangements between the obligor and the seller. The purchaser acquires the receivable subject to any existing rights of set-off the obligor has against the seller. Notice also prevents the obligor from obtaining a valid discharge of the debt from the seller. See question 8.7 below for a brief summary of proposed domestic legislatory reform in relation to the transfer of Scottish receivables.

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4.5 Notice Mechanics. If notice is to be delivered to obligors, whether at the time of sale or later, are there any requirements regarding the form the notice must take or how it must be delivered? Is there any time limit beyond which notice is ineffective – for example, can a notice of sale be delivered after the sale, and can notice be delivered after insolvency proceedings have commenced against the obligor or the seller? Does the notice apply only to specific receivables or can it apply to any and all (including future) receivables? Are there any other limitations or considerations?

The form of notice is not prescribed under Scots law. Various forms of notice or intimation are recognised including those permitted by the Transmission of Moveable Property (Scotland) Act 1862. The 1862 Act provides for notarial intimation and postal intimation. In the latter case, to obtain the benefit of the terms of the Act, the intimation should contain a certified true copy of the assignation. The notice can be delivered after the sale. The transfer would, however, be subject to the rights of parties who have effected diligence in the meantime, third-party purchasers acquiring in good faith, perfected security holders and insolvency officials appointed to the seller. The intimation can be delivered after the commencement of insolvency proceedings against the obligor. The impact of insolvency of the seller is considered in the answer to question 6.1 below.

While an assignation of receivables arising under future contracts is theoretically possible under Scots law, the position is subject to much academic debate and issues arise around the ability to clearly identify the receivable in question. For the assignation to be effective, it is a fundamental principle of Scots law that the receivable is either identified or identifiable. Accordingly, assignations of receivables arising under future contracts should be treated with care. See question 8.7 below for a brief summary of proposed domestic legislatory reform in relation to the transfer of Scottish receivables.

4.6 Restrictions on Assignment – General Interpretation. Will a restriction in a receivables contract to the effect that "None of the [seller's] rights or obligations under this Agreement may be transferred or assigned without the consent of the [obligor]" be interpreted as prohibiting a transfer of receivables by the seller to the purchaser? Is the result the same if the restriction says "This Agreement may not be transferred or assigned by the [seller] without the consent of the [obligor]" (i.e., the restriction does not refer to rights or obligations)? Is the result the same if the restriction says "The obligations of the [seller] under this Agreement may not be transferred or assigned by the [seller] without the consent of the [obligor]" (i.e., the restriction does not refer to rights)?

Restrictions of this nature (whether expressed in relation to the assignation or transfer of rights or obligations under the Agreement or relating to the assignation or transfer of the Agreement itself) will generally be interpreted as prohibiting a transfer at least in any question between the purchaser and any obligor. Dependent upon the purchaser's awareness of the prohibition and the terms of the assignation itself, the purchaser may have a claim against the seller for failing to transfer title to the receivables.

Generally, obligations cannot be assigned under Scots Law (whether the contract contains a prohibition on assignations of obligations or not). It is more common for the transfer of obligations to be effected by a novation between the seller, the purchaser and the relevant obligor. As such, the cooperation of the obligor is required. An assignation of receivables should not be captured by a prohibition on transfer or assignation of obligations of the seller.

4.7 Restrictions on Assignment; Liability to Obligor. If any of the restrictions in question 4.6 are binding, or if the receivables contract explicitly prohibits an assignment of receivables or "seller's rights" under the receivables contract, are such restrictions generally enforceable in your jurisdiction? Are there exceptions to this rule (e.g., for contracts between commercial entities)? If your jurisdiction recognises restrictions on sale or assignment of receivables and the seller nevertheless sells receivables to the purchaser, will either the seller or the purchaser be liable to the obligor for breach of contract or tort, or on any other basis?

Such restrictions are generally enforceable in Scotland. If a sale or assignation is effected in breach of a prohibition, the sale or assignation will likely be ineffective as between the seller and the obligor. A claim for damages for breach of contract may also be available to the obligor against the seller.

4.8 Identification. Must the sale document specifically identify each of the receivables to be sold? If so, what specific information is required (e.g., obligor name, invoice number, invoice date, payment date, etc.)? Do the receivables being sold have to share objective characteristics? Alternatively, if the seller sells *all* of its receivables to the purchaser, is this sufficient identification of receivables? Finally, if the seller sells *all* of its receivables *other than* receivables owing by one or more specifically identified obligors, is this sufficient identification of receivables?

The receivables must be identified or identifiable for the purposes of the sale and transfer of the receivables. The receivables must be ascertainable for the purpose of any transfer. Relevant information usually includes the obligor's name, invoice number, invoice date and amount. The receivables being sold do not need to share objective characteristics. It is possible for the seller to contract to sell all of their receivables to the purchaser or all receivables other than those specifically excluded (and identifiable). It is unlikely that this would be sufficient to identify the receivables for the purpose of an assignation and notice.

4.9 Recharacterisation Risk. If the parties describe their transaction in the relevant documents as an outright sale and explicitly state their intention that it be treated as an outright sale, will this description and statement of intent automatically be respected or is there a risk that the transaction could be characterised by a court as a loan with (or without) security? If recharacterisation risk exists, what characteristics of the transaction might prevent the transfer from being treated as an outright sale? Among other things, to what extent may the seller retain any of the following without jeopardising treatment as an outright sale: (a) credit risk; (b) interest rate risk; (c) control of collections of receivables; (d) a right of repurchase/redemption; (e) a right to the residual profits within the purchaser; or (f) any other term?

A transaction expressed to be a sale may be recharacterised by the courts in Scotland as potentially a secured financing in certain circumstances. A true sale analysis of the sale is usually undertaken.

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In the Scottish context, this involves reviewing the transaction documentation and deal structure and considering the tests applicable in the English case of *Re Inglefield* and an assessment of the 'ultimate right' in the receivables sold. No single factor will result in the transaction being characterised as a sale or a secured financing. Retention of credit risk by the seller may suggest that the purchaser has not truly acquired the receivables, and accordingly buyback provisions are required to be formulated with care. Again, interest rate risk may be characterised as either an indication of true ownership being retained by the seller or merely a purchase price adjustment mechanism. Control of collections of receivables when such services are provided for a commensurate fee, and where the seller does not retain any economic exposure to the receivables either for failing to collect or entitlement to profit from collection is unlikely, in itself, to result in the sale being recharacterised.

4.10 Continuous Sales of Receivables. Can the seller agree in an enforceable manner to continuous sales of receivables (i.e., sales of receivables as and when they arise)? Would such an agreement survive and continue to transfer receivables to the purchaser following the seller's insolvency?

The seller can agree in an enforceable manner to a continuous sale of receivables as and when they arise (at least so far as the purchaser acquiring a contractual right to the receivables) provided such receivables are identifiable. Such contractual arrangements would be effective until the insolvency of the seller.

4.11 Future Receivables. Can the seller commit in an enforceable manner to sell receivables to the purchaser that come into existence after the date of the receivables purchase agreement (e.g., "future flow" securitisation)? If so, how must the sale of future receivables be structured to be valid and enforceable? Is there a distinction between future receivables that arise prior to *versus* after the seller's insolvency?

See question 4.10 above. The transfer of such receivables to the purchaser would, however, need to be documented separately and an automatic transfer of such receivables (at least in respect of Scottish receivables and pending any domestic legislatory reform as referred to in question 8.7 below) is unlikely to be recognised by the Scottish courts without the Scottish formalities being met. To the extent relating to future receivables, we would generally recommend that express supplemental trusts are declared over receivables as and when they are originated (or regularly in batches) pending formal transfer of the receivables to the purchaser.

4.12 Related Security. Must any additional formalities be fulfilled in order for the related security to be transferred concurrently with the sale of receivables? If not all related security can be enforceably transferred, what methods are customarily adopted to provide the purchaser the benefits of such related security?

Each relevant interest should be transferred in accordance with the formal transfer requirements under Scots law unless the security is held on a security trust basis. Related security is generally assigned to the purchaser under Scots law and notice given to obligors or registrations at the relevant Scottish land register depending upon the security involved. Under Scots law, it is thought that an assignation has the effect of 'ruling off' the liabilities secured by the related security at the time of the transfer even if the security is expressed as being for 'all sums'. Accordingly, further advances would be unsecured unless the security is amended or new security is granted to support the further advance. Pending formal transfer, a trust is commonly declared in favour of the purchaser over the receivables and related security. This can also cover certain ancillary rights which are difficult to formally transfer to the purchaser.

4.13 Set-Off; Liability to Obligor. Assuming that a receivables contract does not contain a provision whereby the obligor waives its right to set-off against amounts it owes to the seller, do the obligor's set-off rights terminate upon its receipt of notice of a sale? At any other time? If a receivables contract does not waive set-off but the obligor's set-off rights are terminated due to notice or some other action, will either the seller or the purchaser be liable to the obligor for damages caused by such termination?

The obligor's rights of set-off continue after notice of a sale and related assignation is given to the obligor, but only in respect of amounts which were subsisting prior to such notice being given. Accordingly, any new liabilities of the seller to the obligor arising after notice of the sale and assignation has been given to the obligor will be excluded from the obligor's rights of set-off.

The purchaser should not be liable to the obligor for damages caused by set-off rights being restricted after the assignation of the receivable. Depending upon the terms of the Agreement and any other arrangement between the obligor and the seller, the obligor may have a claim of damages against the seller for losses suffered as a result of set-off rights being restricted after the transfer of the receivable.

4.14 Profit Extraction. What methods are typically used in your jurisdiction to extract residual profits from the purchaser?

Generally, the sale can be unwound/assets subject to a subsequently agreed buyback, resulting in the balance of the assets being returned to the originator. Care needs to be taken to ensure that any alternative mechanism incorporated in the documentation at the outset and designed to extract residual profits from the purchaser do not affect the true sale analysis in respect of any particular transaction.

5 Security Issues

5.1 Back-up Security. Is it customary in your jurisdiction to take a "back-up" security interest over the seller's ownership interest in the receivables and the related security, in the event that an outright sale is deemed by a court (for whatever reason) not to have occurred and have been perfected (see question 4.9 above)?

It is not customary in Scotland to take back up security over the seller's interest in the receivables in the event that the sale is deemed by the court not to have been perfected or is being recharacterised as a secured financing, save in some cases where a floating charge may be granted.

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5.2 Seller Security. If it is customary to take back-up security, what are the formalities for the seller granting a security interest in receivables and related security under the laws of your jurisdiction, and for such security interest to be perfected?

The formalities for granting fixed security over receivables are similar to those in respect of the transfer of such an interest. Accordingly, the receivable should be assigned to the purchaser and notice given to the obligor. The form of security required in respect of related security interests will depend upon the security involved.

In addition, a corporate seller may grant a floating charge over its assets including the receivables and related security.

The security may also need to be registered at Companies House.

The Financial Collateral Arrangements No.2 Regulations 2003 (as amended) also apply in Scotland.

5.3 Purchaser Security. If the purchaser grants security over all of its assets (including purchased receivables) in favour of the providers of its funding, what formalities must the purchaser comply with in your jurisdiction to grant and perfect a security interest in purchased receivables governed by the laws of your jurisdiction and the related security?

The answer is the same as that to question 5.2 above. The purchaser may also hold an interest as beneficiary under a trust declared by the seller over the relevant receivables. Such an interest is capable of being subject to fixed security by means of an assignation duly intimated to the seller.

5.4 Recognition. If the purchaser grants a security interest in receivables governed by the laws of your jurisdiction, and that security interest is valid and perfected under the laws of the purchaser's jurisdiction, will the security be treated as valid and perfected in your jurisdiction or must additional steps be taken in your jurisdiction?

To the extent that the receivables are governed by Scots law, the Scottish courts may not recognise any security granted over such receivables which falls short of the Scots law formalities in respect of such security. The appropriate form of security is set out under question 5.2 above.

5.5 Additional Formalities. What additional or different requirements apply to security interests in or connected to insurance policies, promissory notes, mortgage loans, consumer loans or marketable debt securities?

See questions 4.3 and 4.12 above.

5.6 Trusts. Does your jurisdiction recognise trusts? If not, is there a mechanism whereby collections received by the seller in respect of sold receivables can be held or be deemed to be held separate and apart from the seller's own assets (so that they are not part of the seller's insolvency estate) until turned over to the purchaser?

Trusts are recognised as a matter of Scots law under the Recognition of Trusts Act 1987.

5.7 Bank Accounts. Does your jurisdiction recognise escrow accounts? Can security be taken over a bank account located in your jurisdiction? If so, what is the typical method? Would courts in your jurisdiction recognise a foreign law grant of security (for example, an English law debenture) taken over a bank account located in your jurisdiction?

Scotland recognises arrangements whereby parties hold funds in a designated account and agree to the release of such amounts following satisfaction of certain conditions or on the consent of all relevant parties. Security can be created over bank accounts in Scotland. Certain issues arise in respect of security granted over accounts in favour of the account bank. In such circumstances the security relies upon the operation of set-off. The typical method of taking security is by means of a bank account pledge and assignation duly intimated to the account bank. The Scottish courts would recognise a foreign law grant of security taken over a bank account to the extent that the form of security complies with the Scots law formalities for such a charge.

5.8 Enforcement over Bank Accounts. If security over a bank account is possible and the secured party enforces that security, does the secured party control all cash flowing into the bank account from enforcement forward until the secured party is repaid in full, or are there limitations? If there are limitations, what are they?

The rights of the account bank (such as rights of set-off) will usually be waived under the security and any acknowledgment to be signed by them. All amounts received into the account are secured. An arrestor of the bank account should rank behind the holder of an existing duly perfected account charge. Insolvency should not affect the validity of any fixed security over sums subsequently received into the bank account; although in practice an insolvency official may seek to divert payments, which the purchaser is only contractually obliged to procure are made to such an account. The terms of the bank account security itself can affect the position.

5.9 Use of Cash Bank Accounts. If security over a bank account is possible, can the owner of the account have access to the funds in the account prior to enforcement without affecting the security?

Control by the account holder over the funds in the account is inconsistent with a duly perfected charge under Scots law. Accordingly any such arrangements, which occur frequently in practice, would affect the security. The relevant account should be blocked in order for effective security to be created in Scotland.

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6 Insolvency Laws

6.1 Stay of Action. If, after a sale of receivables that is otherwise perfected, the seller becomes subject to an insolvency proceeding, will your jurisdiction's insolvency laws automatically prohibit the purchaser from collecting, transferring or otherwise exercising ownership rights over the purchased receivables (a "stay of action")? If so, what generally is the length of that stay of action? Does the insolvency official have the ability to stay collection and enforcement actions until he determines that the sale is perfected? Would the answer be different if the purchaser is deemed to only be a secured party rather than the owner of the receivables?

Most insolvency proceedings for corporate entities provide for some form of automatic stay of action or moratorium preventing court proceedings from being raised or enforcement action being taken against the insolvent entity or its assets for a period of time without either the insolvency practitioner's consent or permission of the court. This would prohibit the purchaser from collecting, transferring or otherwise exercising, ownership rights over the purchased receivables to the extent they continued to be assets of the seller at the time of commencement of insolvency proceedings. If, however, ownership of the receivables has been transferred to the purchaser and that transfer has been perfected, the purchaser could sue the obligor in its own name without reference to the insolvent entity.

There is no formal time period applicable to the stay of action which may subsist throughout the insolvency process, unless the insolvency practitioner has consented or permission of the court is obtained.

6.2 Insolvency Official's Powers. If there is no stay of action, under what circumstances, if any, does the insolvency official have the power to prohibit the purchaser's exercise of its ownership rights over the receivables (by means of injunction, stay order or other action)?

On the basis that the receivables have been transferred to the purchaser and that transfer has been perfected, the insolvency official should have no power to interfere with the purchaser's exercise of rights in respect of the receivables, unless the transfer is capable of challenge under the various creditor protection provisions outlined under question 6.3 below.

6.3 Suspect Period (Clawback). Under what facts or circumstances could the insolvency official rescind or reverse transactions that took place during a "suspect" or "preference" period before the commencement of the seller's insolvency proceedings? What are the lengths of the "suspect" or "preference" periods in your jurisdiction for (a) transactions between unrelated parties, and (b) transactions between related parties? If the purchaser is majority-owned or controlled by the seller or an affiliate of the seller, does that render sales by the seller to the purchaser "related party transactions" for purposes of determining the length of the suspect period? If a parent company of the seller guarantee's the performance by the seller of its obligations under contracts with the purchaser, does that render sales by the seller to the purchaser "related party transactions" for purposes of determining the length of the suspect period?

UK Insolvency legislation contains creditor protections which give rise to suspect periods during which transactions may be rescinded or reversed. Certain protections have UK-wide application and, as such, also apply in Scotland (for example, s.245 (Avoidance of certain floating charges) of the Insolvency Act 1986). Transactions entered into by Scottish companies and certain overseas companies may be subject to the provisions of ss.242 and 243 of the 1986 Act (Gratuitous Alienations and Unfair Preferences) and to Scots common law equivalents.

The relevant period to challenge a gratuitous alienation is five years for a transaction with a connected party and two years for any other person and the period for challenge of an unfair preference is six months. An alienation cannot be challenged as gratuitous if: (i) immediately or at any other time after the alienation the company's assets were greater than its liabilities; or (ii) the alienation was made for adequate consideration. An unfair preference is a transaction which has the effect of creating a preference in favour of a creditor to the prejudice of the general body of creditors. A transaction is not a preference if (i) it is in the ordinary course of trade or business, or (ii) it involves the parties undertaking reciprocal obligations unless the transaction was collusive with the purpose of prejudicing the general body of creditors.

If the purchaser is majority-owned and controlled by the seller directly or indirectly, sales by the seller to the purchaser are related party transactions (connected parties) for the purposes of determining the length of the suspect period.

The existence of a guarantee by the parent company of the seller in favour of the purchaser should not in itself result in sales by the seller to the purchaser being related party transactions, for the purpose of determining the length of the suspect period.

6.4 Substantive Consolidation. Under what facts or circumstances, if any, could the insolvency official consolidate the assets and liabilities of the purchaser with those of the seller or its affiliates in the insolvency proceeding? If the purchaser is owned by the seller or by an affiliate of the seller, does that affect the consolidation analysis?

This doctrine is not recognised under Scots law. In addition, the courts will only pierce the corporate veil in very limited circumstances. The position is unaffected by the seller or an affiliate of the seller owning the purchaser.

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6.5 Effect of Insolvency on Receivables Sales. If insolvency proceedings are commenced against the seller in your jurisdiction, what effect do those proceedings have on (a) sales of receivables that would otherwise occur after the commencement of such proceedings, or (b) on sales of receivables that only come into existence after the commencement of such proceedings?

The contractual obligations continue albeit the purchaser is likely to have only a claim against the seller's estate which will rank with other unsecured creditors. As the future Scottish receivables are not transferred to the purchaser without further action of the seller (i.e., the grant of an assignation duly notified to the relevant obligors), the Scottish receivables will remain the property of the seller unless the insolvency official transfers the receivables to the purchaser pursuant to the sale contract.

6.6 Effect of Limited Recourse Provisions. If a debtor's contract contains a limited recourse provision (see question 7.3 below), can the debtor nevertheless be declared insolvent on the grounds that it cannot pay its debts as they become due?

Much will depend upon the terms of the limited recourse wording. Generally, limited recourse provisions will result in the liability being extinguished by the realisation of the relevant assets and application of proceeds in satisfaction of the equivalent value of debt (any balance being cancelled). As such, they are asset/liability-neutral. Scottish corporate debtors can be declared insolvent if, among other things, their liabilities exceed their assets. They can also be declared insolvent if a creditor has served on the debtor a written demand for payment and the debtor has failed to pay such demand within the prescribed period. The limited recourse wording should be checked to establish whether or not it permits the creditor to serve such a demand. A Scottish corporate debtor may also be declared insolvent if it is proved to the court that the company is unable to pay its debts as they fall due. The debtor's whole assets and liabilities position needs to be taken into account when considering this final test.

7 Special Rules

7.1 Securitisation Law. Is there a special securitisation law (and/or special provisions in other laws) in your jurisdiction establishing a legal framework for securitisation transactions? If so, what are the basics? Is there a regulatory authority responsible for regulating securitisation transactions in your jurisdiction?

There is no special securitisation law in Scotland establishing a legal framework for securitisation transactions, although particular tax laws may apply and various EU legislation may have effect in Scotland in respect of certain securitisation transactions. There is no specific securitisation regulatory authority in Scotland, although certain rules of the Financial Conduct Authority and Prudential Regulation Authority, being the financial regulatory bodies in the UK, are relevant to securitisation transactions.

7.2 Securitisation Entities. Does your jurisdiction have laws specifically providing for establishment of special purpose entities for securitisation? If so, what does the law provide as to: (a) requirements for establishment and management of such an entity; (b) legal attributes and benefits of the entity; and (c) any specific requirements as to the status of directors or shareholders?

There are no mandatory or special requirements in respect of the establishment of special-purpose entities for securitisations in Scotland. The Securitisation Regulation (see question 8.7 below) will impose at EU level certain restrictions on the jurisdiction of establishment of special-purpose entities for securitisations.

7.3 Location and form of Securitisation Entities. Is it typical to establish the special purpose entity in your jurisdiction or offshore? If in your jurisdiction, what are the advantages to locating the special purpose entity in your jurisdiction? If offshore, where are special purpose entities typically located for securitisations in your jurisdiction? What are the forms that the special purpose entity would normally take in your jurisdiction and how would such entity usually be owned?

For UK securitisations involving Scottish assets the special purpose entity is typically established in England as opposed to Scotland. There is no particular reason for not establishing the special purpose entity in Scotland other than that the principal documentation for UK securitisation transactions is typically governed by English law. Other common jurisdictions of establishment include Ireland, Luxembourg, the Netherlands and certain offshore jurisdictions including Jersey and the Cayman Islands.

7.4 Limited-Recourse Clause. Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) limiting the recourse of parties to that agreement to the available assets of the relevant debtor, and providing that to the extent of any shortfall the debt of the relevant debtor is extinguished?

Generally, the courts in Scotland would recognise a limited-recourse clause.

7.5 Non-Petition Clause. Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) prohibiting the parties from: (a) taking legal action against the purchaser or another person; or (b) commencing an insolvency proceeding against the purchaser or another person?

Although there is no direct Scottish authority in this regard, non-petition clauses are likely to be valid in Scotland provided such provisions are not contrary to public policy. A Scottish court might still accept a winding-up petition contrary to the terms of a non-petition clause resulting instead in only a damages claim for breach. A clause in a consumer contract which has the object or effect of excluding or hindering the consumer's right to take legal action or exercise any other legal remedy, which could include restrictive jurisdiction or enforcement clauses, may be regarded as unfair pursuant to the Consumer Rights Act 2015.

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7.6 Priority of Payments "Waterfall". Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) distributing payments to parties in a certain order specified in the contract?

Yes. Pre-insolvency of the purchaser, contractual arrangements fixing the priority of distributions are of a type which would be recognised by the Scottish courts. Priority of payments of unsecured amounts post-insolvency may still be recognised, however, as a general rule an insolvency official would not be bound by the terms of such provisions and is required to pay creditors in accordance with statutory rules. Payments in breach of such arrangements will create only contractual claims against the parties to the contract.

7.7 Independent Director. Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) or a provision in a party's organisational documents prohibiting the directors from taking specified actions (including commencing an insolvency proceeding) without the affirmative vote of an independent director?

As a matter of UK company law, directors are unable to limit the exercise of their powers. Constitutional documents may be drafted so as to require director consent for certain actions. However, to the extent such provisions are contrary to public policy they would be unenforceable. The directors have overriding duties to creditors including, where appropriate, to call for winding-up or administration of a corporate entity in certain circumstances. It is unlikely that such provisions would be overridden by contractual or constitutional document provisions.

7.8 Location of Purchaser. Is it typical to establish the purchaser in your jurisdiction or offshore? If in your jurisdiction, what are the advantages to locating the purchaser in your jurisdiction? If offshore, where are purchasers typically located for securitisations in your jurisdiction?

Common jurisdictions for place of establishment are England, Ireland and Luxembourg. Scottish issuers are broadly in a similar position to issuers established in England. In addition see question 7.3 above.

8 Regulatory Issues

8.1 Required Authorisations, etc. Assuming that the purchaser does no other business in your jurisdiction, will its purchase and ownership or its collection and enforcement of receivables result in its being required to qualify to do business or to obtain any licence or its being subject to regulation as a financial institution in your jurisdiction? Does the answer to the preceding question change if the purchaser does business with more than one seller in your jurisdiction?

The acquisition, collection or ownership of receivables will not in itself result in the purchaser being required to do business or to obtain a licence, or its being subject to regulation as a financial institution in Scotland unless such activities are regulated (for example, origination or administration of regulated mortgage contracts for which FCA authorisation would be required) or constitute consumer credit activities (for which a consumer credit permission would be required).

8.2 Servicing. Does the seller require any licences, etc., in order to continue to enforce and collect receivables following their sale to the purchaser, including to appear before a court? Does a third-party replacement servicer require any licences, etc., in order to enforce and collect sold receivables?

Servicing activities are likely to require a consumer credit and/or FCA authorisation and permissions if they relate to consumer credit activities or regulated activities. Any third-party replacement servicer will require the same licences and authorisations.

8.3 Data Protection. Does your jurisdiction have laws restricting the use or dissemination of data about or provided by obligors? If so, do these laws apply only to consumer obligors or also to enterprises?

The provisions of the UK Data Protection Act 1998 apply in Scotland. With effect from 25 May 2018, the 1998 Act will be replaced by the EU-wide General Data Protection Regulation (Regulation 2016/679) and the Data Protection Act 2018.

The laws apply only to information relating to identified or identifiable living individuals ('personal data') and not to enterprises, however, information relating to a sole trader or partnership is likely to be treated as personal data.

8.4 Consumer Protection. If the obligors are consumers, will the purchaser (including a bank acting as purchaser) be required to comply with any consumer protection law of your jurisdiction? Briefly, what is required?

If the obligors are consumers, the purchaser will probably be required to comply with the UK consumer credit protection laws and to be authorised by the FCA.

If the contract constitutes a regulated mortgage contract (or equivalent regulated contract) for the purposes of the Financial Services and Markets Act 2000, the purchaser would need to be authorised by the FCA and comply with the detailed requirements of the FCA Handbook relating to such contracts.

Certain unfair terms in consumer contracts may not be enforceable against the consumer. Similarly, provisions in a consumer contract, which purport to restrict liability of a party for damage caused, may be restricted or struck at by the Unfair Contract Terms Act 1977 in relation to contracts entered into prior to 1 October 2015, and the Consumer Rights Act 2015 in relation to contracts entered into from 1 October 2015.

8.5 Currency Restrictions. Does your jurisdiction have laws restricting the exchange of your jurisdiction's currency for other currencies or the making of payments in your jurisdiction's currency to persons outside the country?

Subject to currency transfer and dealing restrictions applicable under current United Nations sanctions and US sanctions and to compliance with anti-money laundering/anti-terrorism legislation, there are no restrictions on currency exchange or the making of payments to persons outside Scotland.

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8.6 Risk Retention. Does your jurisdiction have laws or regulations relating to "risk retention"? How are securitisation transactions in your jurisdiction usually structured to satisfy those risk retention requirements?

Yes, risk retention rules apply (such that the originator, sponsor or original lender requires to retain 'skin-in-the-game') at EU level through Articles 404 to 410 of the Capital Requirements Regulation (Regulation (EU) No 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012) (the "CRR"). The CRR provides that EU credit institutions and investment firms must ensure that the originator, sponsor or original lender has retained for the life of the transaction a material net economic interest in the securitisation of not less than 5%, before the investor is exposed to the credit risk of the securitisation. In addition, the CRR imposes certain due diligence and ongoing monitoring requirements on investors to ensure in-depth knowledge of the structure and material characteristics of the particular securitisation. It is currently (see question 8.7 below) for the investor to ensure compliance with the risk retention rules. Retention holders can opt to choose one of five retention mechanisms:

- retention of 5% or more of the nominal value of each class of notes sold/transferred to investors;
- for revolving exposures, retention of 5% or more of the originator's interest in the nominal value of the securitised exposure;
- retention of randomly selected assets equal to 5% or more of the nominal value of the securitised exposure, where such assets would otherwise have been securitised (such selection to be made from a pool comprising not less than 100 assets at origination);
- retention of the first loss tranche and, if necessary, other tranches which have the same or a more severe risk profile than those transferred or sold, and not maturing any earlier than those transferred or sold equal to 5% or more of the nominal value of the securitised exposures; or
- retention of first loss exposure of 5% or more of every securitised exposure in the securitisation.

Relevant investors who fail to comply with the risk retention rules will be subject to regulatory penalties including additional risk weighting and capital requirements in respect of non-compliant securitised positions.

8.7 Regulatory Developments. Have there been any regulatory developments in your jurisdiction which are likely to have a material impact on securitisation transactions in your jurisdiction?

Significant proposed and pending regulatory reform impacting securitisations in this jurisdiction include, at EU level, the Securitisation Regulation (Regulation (EU) 2017/2402 of the European Parliament and of the Council of 12 December 2017, amending Directives 2009/65/EC, 2009/138/EC and 2011/61/EU and Regulations (EC) No 1060/2009 and (EU) No 648/2012) forming part of the broader Capital Markets Union (CMU) initiative. At domestic level, the publication of a draft Bill to reform and modernise the moveables transaction law in Scotland will also impact on asset risk and security structures supporting securitisations.

The stated objective of the Securitisation Regulation, which will apply to securitisations where the securities are issued on or after 1 January 2019, is to lay down a general framework for securitisations and create a specific framework for simple, transparent and standardised (STS) securitisations. The principal reforms introduced by the Securitisation Regulation are: to place a direct risk retention obligation on originators, sponsors and original lenders; to widen the category of entity defined as a 'sponsor' to include non-EU credit institutions and investment firms; to provide that an entity shall not be considered to be an 'originator' if the entity was established or operates for the sole purpose of securitising exposures; to impose restrictions on the jurisdiction of establishment of securitisation issuers; and to create the concept of STS securitisations — a class of securitisations which, if certain criteria are met, will benefit from more favourable capital requirements for an institution's exposure to such securitisation through regulatory reform, to be introduced by the CRR Amendment Regulation (Regulation (EU) 2017/2401, amending Regulation (EU) No 575/2013 on prudential requirements for credit institutions and investment firms).

The European Union (Withdrawal) Bill, once enacted into UK law, adopts EU legislation (including the Securitisation Regulation) into UK law at 29 March 2019 (the anticipated withdrawal date). This is intended to preserve the continuing effect of the Securitisation Regulation, and all other EU legislation affecting securitisations, as such EU law applies in the UK as at the date of the UK's withdrawal from the EU. The exact implications of this will require more detailed regulations to be prepared and will be influenced by the market access deal agreed between the UK and the rest of the EU.

The Moveable Transactions (Scotland) Bill, once enacted into legislation in Scotland (it is not currently known when the legislation will be enacted), will simplify the law relating to the assignation of claims (including receivables) governed by Scots law by providing that: a claim is transferred on either intimation of the assignation or registration of the assignation in a newly established public register to be known as the Register of Assignations; intimation of the assignation may be by hand, postal or electronic delivery; and the assignation of future claims is competent. The Transmission of Moveable Property (Scotland) Act 1862 will be expressly repealed. The proposed legislation also provides for an alternative form of non-possessory security or charge over certain moveable assets.

9 Taxation

9.1 Withholding Taxes. Will any part of payments on receivables by the obligors to the seller or the purchaser be subject to withholding taxes in your jurisdiction? Does the answer depend on the nature of the receivables, whether they bear interest, their term to maturity, or where the seller or the purchaser is located? In the case of a sale of trade receivables at a discount, is there a risk that the discount will be recharacterised in whole or in part as interest? In the case of a sale of trade receivables where a portion of the purchase price is payable upon collection of the receivable, is there a risk that the deferred purchase price will be recharacterised in whole or in part as interest? If withholding taxes might apply, what are the typical methods for eliminating or reducing withholding taxes?

Withholding tax is subject to UK-wide legislation. Accordingly, the Scottish rules follow those applicable elsewhere in the UK (including in respect of the potential recharacterisation of any deferred purchase price). In summary, withholding tax applies in respect of payments of interest unless the purchaser is resident in the UK, or carries on business in the UK through a permanent establishment. Withholding tax can be eliminated or mitigated

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by ensuring the transaction is structured so that residence and/or carrying out business criteria (and other conditions) are met. Withholding tax may also be subject to treaty relief under a Double Taxation Convention, though there are practical difficulties in particular cases.

9.2 Seller Tax Accounting. Does your jurisdiction require that a specific accounting policy is adopted for tax purposes by the seller or purchaser in the context of a securitisation?

The seller tax treatment follows UK tax requirements, which are based on the accounting treatment subject to specific regulations.

9.3 Stamp Duty, etc. Does your jurisdiction impose stamp duty or other transfer or documentary taxes on sales of receivables?

Certain documents are subject to stamp duty in Scotland and certain transactions to the extent not documented are subject to stamp duty reserve tax (SDRT). Those relating to land or interests in land may be subject to the Land and Buildings Transaction Tax (LBTT) or in some cases to Stamp Duty Land Tax (SDLT), which applied to transactions in Scotland prior to 1 April 2015. The transfer of mortgages, lease and trade receivables and finance payments are normally exempt from stamp duty, SDRT, LBTT and SDLT.

9.4 Value Added Taxes. Does your jurisdiction impose value added tax, sales tax or other similar taxes on sales of goods or services, on sales of receivables or on fees for collection agent services?

VAT is generally payable in Scotland in respect of the supply of goods and services within the UK by taxable persons in the course or furtherance of a business. The current standard rate of VAT is 20%, although different rates apply depending upon the goods or services supplied. Certain supplies are exempt and some transfers are outside the scope of VAT.

9.5 Purchaser Liability. If the seller is required to pay value-added tax, stamp duty or other taxes upon the sale of receivables (or on the sale of goods or services that give rise to the receivables) and the seller does not pay, then will the taxing authority be able to make claims for the unpaid tax against the purchaser or against the sold receivables or collections?

To the extent payable, VAT has to be accounted for by the provider of services only (i.e., the seller). Stamp duty liability falls to the party seeking to enforce the transfer (i.e., the purchaser). Generally, HM Revenue & Customs would not have a claim against the purchaser for VAT for which the seller had to account.

9.6 Doing Business. Assuming that the purchaser conducts no other business in your jurisdiction, would the purchaser's purchase of the receivables, its appointment of the seller as its servicer and collection agent, or its enforcement of the receivables against the obligors, make it liable to tax in your jurisdiction?

The purchase of receivables by the purchaser or its appointment of the seller as its servicer and collection agent should not, in itself, result in the purchaser being liable to pay tax in Scotland; however, as with the rest of the UK, enforcement of receivables may require more detailed consideration. In each case all circumstances need to be considered and advice obtained.

9.7 Taxable Income. If a purchaser located in your jurisdiction receives debt relief as the result of a limited recourse clause (see question 7.3 above), is that debt relief liable to tax in your jurisdiction?

Where a debt is forgiven, this is likely to lead to a corporation tax charge for a borrower which is a company to the extent that the amount forgiven is recognised as a credit in the borrower's accounts. The accounting treatment would depend on the nature of the financing arrangements. The position would be different if the borrower and the finance provider are connected, in which case no tax charge would arise.

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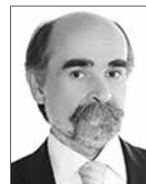
Chapter 27

Serbia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1 Receivables Contracts

1.1 Formalities. In order to create an enforceable debt obligation of the obligor to the seller: (a) is it necessary that the sales of goods or services are evidenced by a formal receivables contract; (b) are invoices alone sufficient; and (c) can a binding contract arise as a result of the behaviour of the parties?

a) As a general rule of law, sales of goods/services do not require a formal receivables contract. However, certain goods/services are under specific legal regimes requiring either a written or notarised form, such as sales of immovable assets or vehicles, construction contracts, licence contracts, sales representation' contracts, financial leasing, factoring, bank credits/loans, financial consumer contracts, etc. Please note that when the required written form has been missed, Serbian obligations' law allows for a contract to be recognised and in force if the parties have executed the obligations arising out of that contract in full or in its prevailing part, if such option has not been excluded by a specific law (validation through performance of the contract). This does not, as a general rule of law, apply to contracts requiring a notarised form.

b) This depends on the type of goods and services, but as a general rule, yes. Please refer to answers under a).

c) As a general rule of law, the Serbian law on obligations sets that a will to enter into a contract may be expressed in words, usual signs or by other behaviour out of which a clear conclusion on the existence of the will to enter into a contract may be ascertained. As to exemptions, please refer to answers under a).

1.2 Consumer Protections. Do your jurisdiction's laws: (a) limit rates of interest on consumer credit, loans or other kinds of receivables; (b) provide a statutory right to interest on late payments; (c) permit consumers to cancel receivables for a specified period of time; or (d) provide other noteworthy rights to consumers with respect to receivables owing by them?

a) No, they do not.

b) Yes. A principle rule under the law is that a contractual penalty cannot be set under an agreement for pecuniary obligations and that an obligor is committed to pay statutory interest set under the law. The statutory interest is payable even if not set under the agreement between the parties. Further, if contractual interest is higher than the rate of the statutory interest, the contractual interest may accrue following obligor's delay. The statutory penalty does not accrue in such a case. The creditor has the right to statutory interest irrespective of damage caused to it, but if the damage is higher, the creditor may request the difference up to the total damage in a court process. A bank operating in Serbia has special rules, i.e. there is a possibility for the bank to set that the penalty interest will be payable on the accrued contractual interest, and there is a possibility for the bank to make an agreement with the obligor that the contractual interest shall be increased in the case of the obligor delaying.

c) As a general rule, a consumer may cancel their credit/loan contract, overdraft, credit card contract, financial leasing and financial agreements within 14 days as of signing without stating the reasons for cancellation. Specific rules apply depending on the type of a financial services contract (for example, a mortgage may be cancelled provided that the consumer has not started using the credit or the financing).

d) A consumer has the right to object, in writing, to the provider of the financial services if it thinks that the provider does not act in line with the Law on Protection of Consumers of Financial Services or other regulations on financial services, to the general terms of use or to the good business customs *in re* of financial services, or to the provisions of the contract with right to execute such objection within three years as of breaching such regulations/customs/contract. There is also a right of complaint to the National Bank of Serbia (hereinafter the **NBS**). The NBS may issue a decision ordering the financial services' provider to remedy the irregularities which have been ascertained and to deliver evidence on completing the terms from such decision of the NBS.

1.3 Government Receivables. Where the receivables contract has been entered into with the government or a government agency, are there different requirements and laws that apply to the sale or collection of those receivables?

When seeking enforcement via court lawsuit, a purchaser is no longer required to seek mediation with the government (Public Attorney General) before filing a lawsuit against the government/local government. Also, facilities, weapons and equipment destined for defence and security of the Republic of Serbia cannot be subject to a forced sale.

Sale of receivables from a foreign credit/loan taken by a public company, by a state-owned legal entity or by a legal entity in the process of restructuring or privatisation may be sold only upon a contract between, consents or statements given by all participants involved, with a previous consent of the government, save for receivables and payables of a resident-legal entity founded by the Republic of Serbia upon a special law for the purposes of export

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financing. A resident public company, a state-owned legal entity or a legal entity in the process of restructuring or privatisation may give a guarantee to a non-resident for transactions involving goods or services' import and investment works in Serbia, under the terms and in manner set by the government.

2 Choice of Law – Receivables Contracts

2.1 No Law Specified. If the seller and the obligor do not specify a choice of law in their receivables contract, what are the main principles in your jurisdiction that will determine the governing law of the contract?

The Law on Conflict of Laws of the Republic of Serbia sets that if the parties have not chosen the applicable law, the rules of that law shall apply, if the case does not concern an international treaty.

Therefore, if there is no applicable law chosen and special circumstances do not lead to application of another governing law, the governing law would be the law of the place of the party receiving the payment obligation, i.e. the money at the time of the receipt of the contract offer. This would apply to sale of movable goods (i.e. the seller's place of residence/seat), services or construction contracts (the place of the service provider/contractor), commission sale, shipping, lease of movable goods, warehousing, transport, insurance, and copyright. For the licence contract, the governing law would be the place of residence/seat of the licensee at the time of entering into the contract. For other contracts not explicitly listed in the law, the governing law would be the place of residence/seat of the party making the offer at the time of receipt of the offer.

For contracts involving immovable property, there is exclusive governing law of the state in which the property is located.

2.2 Base Case. If the seller and the obligor are both resident in your jurisdiction, and the transactions giving rise to the receivables and the payment of the receivables take place in your jurisdiction, and the seller and the obligor choose the law of your jurisdiction to govern the receivables contract, is there any reason why a court in your jurisdiction would not give effect to their choice of law?

With the facts given, there is no foreign element in such transaction and therefore any application of foreign law, i.e. choice of law would not receive court protection, and, respectively, the choice of the governing law would not make legal sense. Therefore, in such situation a court in Serbia would always apply Serbian regulations.

2.3 Freedom to Choose Foreign Law of Non-Resident Seller or Obligor. If the seller is resident in your jurisdiction but the obligor is not, or if the obligor is resident in your jurisdiction but the seller is not, and the seller and the obligor choose the foreign law of the obligor/seller to govern their receivables contract, will a court in your jurisdiction give effect to the choice of foreign law? Are there any limitations to the recognition of foreign law (such as public policy or mandatory principles of law) that would typically apply in commercial relationships such as that between the seller and the obligor under the receivables contract?

As explained under question 2.1, the governing law for a contract would be the one chosen by the parties (if there is a foreign element in any aspect of the contract), if not set otherwise by the law or by an international treaty. If the contract relates to immovable property, there is exclusive governing law of the country in which territory the property is located.

Per the Law on Conflict of Laws, the law of a foreign country would not be applied if its effect would be contrary to the principles of social order set under the constitution of the Republic of Serbia. Also, a foreign law which would be applicable under the provisions of the Law or another Act would not be applied if its application is aimed at avoiding the application of the law of the Republic of Serbia.

3 Choice of Law – Receivables Purchase Agreement

3.1 Base Case. Does your jurisdiction's law generally require the sale of receivables to be governed by the same law as the law governing the receivables themselves? If so, does that general rule apply irrespective of which law governs the receivables (i.e., your jurisdiction's laws or foreign laws)?

In general, there is no such requirement and it is possible for the agreement on the sale of receivables to be governed by a law other than the law governing the receivables. However, there are mandatory rules on foreign exchange set under the Law on Foreign Exchange which apply irrespective of the choice of law (if there is a Serbian resident involved in the sale/purchase of receivables). A further issue in such a case would be treatment of rights and obligations of a party in the original receivables document that did not participate in the assignment of claim or a debt takeover, if any. The effect of such transfer to such a person and the conditions for such a transfer to be enforced towards/against such a person would have to be regulated under the law governing original receivable documents.

3.2 Example 1: If (a) the seller and the obligor are located in your jurisdiction, (b) the receivable is governed by the law of your jurisdiction, (c) the seller sells the receivable to a purchaser located in a third country, (d) the seller and the purchaser choose the law of your jurisdiction to govern the receivables purchase agreement, and (e) the sale complies with the requirements of your jurisdiction, will a court in your jurisdiction recognise that sale as being effective against the seller, the obligor and other third parties (such as creditors or insolvency administrators of the seller and the obligor)?

If the sale complies with the requirements of the laws of Serbia (presupposing compliance with the foreign exchange regulations of Serbia), such sale would be effective against the seller and the obligor. However, creditors/insolvency administrators of the seller would have the right to challenge such sale if it has been taken to the detriment of the creditors. There is a legal presumption in the Serbian regulations of obligations that such a sale would be considered as detrimental to creditors if, due to performance from such sale, the seller would not have sufficient assets to settle the creditor's claim. Deadlines for filing a suit against such a sale are longer if insolvency of the seller is involved.

Insolvency administrator of a seller/obligor has the right to accept or deny the claim filed in the bankruptcy procedure and in the latter case, the purchaser would have to sue the seller/obligor in the insolvency procedure. There is also right of a creditor/insolvency administrator of the obligor to challenge the sale; however, their

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interests would be much harder to prove (potentially in the case where the creditor was a creditor for both the seller and the obligor).

3.3 Example 2: Assuming that the facts are the same as Example 1, but either the obligor or the purchaser or both are located outside your jurisdiction, will a court in your jurisdiction recognise that sale as being effective against the seller and other third parties (such as creditors or insolvency administrators of the seller), or must the foreign law requirements of the obligor's country or the purchaser's country (or both) be taken into account?

If the sale complies with the Serbian regulations (including compliance with conflict of laws and the foreign exchange regulations, where applicable), the sale would be recognised as effective against the seller. Creditors/insolvency administrators of the seller would retain their rights under the Serbian laws as explained under question 3.2.

As to the issues of status of a person, the foreign law would be taken into account when determining the origin of a legal entity (which would be the law of the country of foundation or, as a second rule, of its actual seat). Also, the country of citizenship would be taken as applicable when determining legal and operational capacity of a natural person.

3.4 Example 3: If (a) the seller is located in your jurisdiction but the obligor is located in another country, (b) the receivable is governed by the law of the obligor's country, (c) the seller sells the receivable to a purchaser located in a third country, (d) the seller and the purchaser choose the law of the obligor's country to govern the receivables purchase agreement, and (e) the sale complies with the requirements of the obligor's country, will a court in your jurisdiction recognise that sale as being effective against the seller and other third parties (such as creditors or insolvency administrators of the seller) without the need to comply with your jurisdiction's own sale requirements?

The rules as to the mandatory application of the Serbian law on conflicts of laws explained under question 2.3 would apply, but also the Serbian foreign exchange regulations, which are mandatory public provisions surpassing private law, stipulated in the agreements with foreign exchange elements in aspects concerning foreign exchange. Therefore, since the receivables agreement concerns foreign exchange matters (if the obligor is a non-resident), both the receivables agreement and the receivables purchase agreement would have to meet criteria from the Law on Foreign Exchange of Serbia in order to be enforced in Serbia. Therefore, there would be a need for compliance with the Serbian regulations. Also, if the case concerns international factoring (please see question 8.1), the sale of receivables would have to comply with the Law on Factoring of Serbia. Outside these aspects, foreign governing law would apply without the need to comply with the requirements of the Serbian jurisdiction.

However, a foreign governing law would not have effect to the rights of the creditors/insolvency administrators of the seller, i.e. creditors/insolvency administrators would retain their rights under the respective Serbian laws (the governing law of the receivables/receivables purchase agreements have *inter partes* effect, only between the parties thereto).

3.5 Example 4: If (a) the obligor is located in your jurisdiction but the seller is located in another country, (b) the receivable is governed by the law of the seller's country, (c) the seller and the purchaser choose the law of the seller's country to govern the receivables purchase agreement, and (d) the sale complies with the requirements of the seller's country, will a court in your jurisdiction recognise that sale as being effective against the obligor and other third parties (such as creditors or insolvency administrators of the obligor) without the need to comply with your jurisdiction's own sale requirements?

In view of the above-mentioned and subject to general applicability of a foreign law (not contrary to the public policy/Constitution), and the rule that as to the effects of the assignment of a claim or of debt takeover towards an obligor, or the creditor which did not participate in the assignment/debt takeover, the Law on Conflict of Laws sets application of the law applicable to the claim/debt, and if not set otherwise, the law of the sellers' country would apply. However, the Law on Foreign Exchange of Serbia sets that in the case of assignment of a receivable the obligor has to be informed/to give its consent or even in some specific cases to provide the consent of the Government of Serbia (for details see question 3.6 below) for such assignment. Therefore, in such a case the obligor needs to be informed and special sale requirements set under the mentioned Law would be applicable. The issue of international factoring from point 3.4 would also apply here.

Creditors/insolvency administrators would retain their rights as explained under question 3.4.

3.6 Example 5: If (a) the seller is located in your jurisdiction (irrespective of the obligor's location), (b) the receivable is governed by the law of your jurisdiction, (c) the seller sells the receivable to a purchaser located in a third country, (d) the seller and the purchaser choose the law of the purchaser's country to govern the receivables purchase agreement, and (e) the sale complies with the requirements of the purchaser's country, will a court in your jurisdiction recognise that sale as being effective against the seller and other third parties (such as creditors or insolvency administrators of the seller, any obligor located in your jurisdiction and any third party creditor or insolvency administrator of any such obligor)?

If the obligor is located in Serbia:

- The receivables agreement is a domestic transaction.
- The receivables purchase agreement is under foreign law. If the application of the foreign law passes through the "filter" explained under question 2.3 above, the seller would be responsible as set under the respective applicable foreign law.
- As to the obligor, the issue is not clear in full. Namely, the Serbian transaction would be transformed into the foreign exchange transaction. The Law on Foreign Exchange of Serbia would not be applicable to the original transaction, but a foreign element would be added by sale of receivables to a foreign purchaser. This issue is not regulated under the mentioned Law, but to be cautious it would be advisable for the mandatory rules to be applied, especially if the obligor is a company under state ownership or undergoing privatisation, in which case prior approval from the Government is needed. If the seller and the purchaser would, irrespective to this ambiguity under the mentioned Law, decide not to implement the provisions of the Law on Foreign exchange, the obligor

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would be subject to the law applicable to the receivables contract (in this case Serbian law). Per the Law on Conflict of Laws of Serbia – as to the effects of assignment of a claim or of debt takeover towards an obligor, the law applicable to the claim/debt (i.e. the law governing the receivables contract) shall apply to the creditor which did not participate in the assignment/debt takeover.

- If any obligor would mean any kind of guarantor for the obligation of the obligor from the receivables contract, according to the Law on Conflict of Laws, accessory legal matter (such as a guarantee, warranty, etc.) would be subject to the law applicable to the main legal matter if not set otherwise. In this case, if the receivables contract (main legal matter) does not set otherwise, such obligor would be subject to the law applicable to the receivables contract, in this case Serbian law.
- The issue of international factoring from question 3.4 would also apply here.
- Creditors/insolvency administrators would retain their respective rights under Serbian regulations, since the governing law of a contract has only *inter partes* effect (i.e. only between the parties to the receivables purchase agreement). This would also apply towards other obligors of the seller (save for the ones from the previous paragraph) since the purchaser has become a creditor of a specific obligor of the seller and such other obligors would retain their respective rights under Serbian regulations. The same goes for third-party creditor/insolvency administrators of such obligors.

If the obligor is located outside Serbia:

- The receivables agreement has a foreign element but is subject to Serbian law. The receivables purchase contract is governed by foreign law. Therefore, in order to be valid in front of a Serbian Court, the receivables purchase agreement would have to pass through the "filters" of the Law on Conflict of Laws (see answers under question 2.3) and meet the criteria of the Law on Foreign Exchange of Serbia.
- According to Article 7 (international sale of goods/services and similar), respectively, Article 20 (foreign credits/loans and similar financial arrangements) of the Law on Foreign Exchange, there must be a contract between the seller and the purchaser of the receivable (in writing) with a duty of the seller to inform the obligor of the transaction. Also, the receivables purchase agreement would have to contain data set under the law. If a receivable agreement concerns a public company or a state-owned legal entity or an entity under restructuring or under privatisation (whether as a seller or an obligor), there must a trilateral agreement (seller, purchaser and obligor) or statements of all parties involved with a previous consent of the government of Serbia. If the seller is a natural person, he would not be allowed to sell the receivables. If the receivables purchase agreement meets the said criteria, it would be applied as under foreign governing law.
- As to applicable law, since the Law on Foreign Exchange requires informing/consent of the obligor, the rule of Law on Conflict of Law as to the effects of the transfer where the obligor was not a party to the receivables purchase agreement (as explained above) would not apply and the obligor would be subject to the governing law of the receivables purchase agreement.
- The creditors/insolvency administrators of the seller would be subject to Serbian laws (the same situation as when the obligor is in Serbia).
- If any obligor would mean any kind of guarantor for the obligation of the obligor from the receivables contract, according to the Law on Conflict of Laws, accessory legal matter (such as a guarantee, warranty, etc.) would be subject to the law applicable to the main legal matter if not set otherwise. In this case, if the receivables contract (main legal matter) does not set otherwise, such obligor would be subject to the law applicable to the receivables contract, in this case Serbian law. Other obligors would not be subject to the governing law of the receivables purchase contract, since they are not parties to the receivables and receivables purchase contract in any way and would have the rights under Serbian regulations.

4 Asset Sales

4.1 Sale Methods Generally. In your jurisdiction what are the customary methods for a seller to sell receivables to a purchaser? What is the customary terminology – is it called a sale, transfer, assignment or something else?

The sale of receivables usually involves a written agreement between the seller and the purchaser, and the parties usually tend to obtain the signing by the obligor in order for him to be informed of the sale. This is usually called an assignment of rights. In the case of a transaction involving no foreign element, the signing by the obligor is not a must and the seller is obliged to inform the obligor of the sale done, and as of such information the obligor has the obligation to make any payments to the purchaser only.

4.2 Perfection Generally. What formalities are required generally for perfecting a sale of receivables? Are there any additional or other formalities required for the sale of receivables to be perfected against any subsequent good faith purchasers for value of the same receivables from the seller?

In general, Serbian regulations on obligations do not require any form of sale of receivables; however, parties tend to have a written agreement or even a notarised agreement in order to have evidence of the sale (especially when it comes to sale of receivables between commercial entities, since Serbian litigation regulations provide that proving a point in a commercial case is to be made primarily by providing written exhibits, i.e. evidence). Exceptions include sale of receivables when the obligor is in insolvency, when the receivable purchase agreement has to be notarised and the notification to the insolvency administrator has to be delivered in writing.

According to the Serbian regulations on obligations, if the seller has sold the same receivable to different persons, the receivable shall belong to the purchaser which the seller has firstly informed the obligor, i.e. to the purchaser who was the first to contact the obligor. In the case of the sale for value, the seller shall be responsible to the purchaser for the existence of the receivable at the moment of sale thereof. It is possible, and only if provided so under the agreement, for the seller to be responsible for enforceability and collection of the amount staying *de facto* a kind of warrantor for the obligor towards the purchaser. When it comes to the sale of receivables from credits/loans or international sale of goods/services, the Law on Foreign Exchange rules (as explained under section 3) would apply, as well as rules of the Law on Factoring, if the case concerns international factoring. Sale of banking credits/loans taken by commercial entities, require informing the National Bank of Serbia.

In general, there are no additional or other formalities save for proving the right of the purchaser to the receivable.

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4.3 Perfection for Promissory Notes, etc. What additional or different requirements for sale and perfection apply to sales of promissory notes, mortgage loans, consumer loans or marketable debt securities?

The sale of a claim under a promissory note is to be effected by an endorsement (i.e. the promissory note is transferred by an endorsement). Before that, the promissory note has to be registered at the National Bank of Serbia. The collection of a promissory note also includes a payment order given to a bank (managing the banking account of the obligor/obligor from the receivables agreement). Also, the person making the collection has to be in possession of the promissory note.

The sale of mortgage loans requires a contract in a notarised form. The sale of a mortgage without the sale of the receivable collateralised by the mortgage shall have no legal effect. The transfer also requires the registration of the transfer of the mortgage at the cadastre register.

Consumer loans could be transferred only to a bank, payment services' provider or to an issuer of electronic money.

The sale of marketable debt securities has very limited application and volume in Serbia. It mostly concerns short-term debt securities issued by the Republic of Serbia which are only to be bought by banks in Serbia.

4.4 Obligor Notification or Consent. Must the seller or the purchaser notify obligors of the sale of receivables in order for the sale to be effective against the obligors and/or creditors of the seller? Must the seller or the purchaser obtain the obligors' consent to the sale of receivables in order for the sale to be an effective sale against the obligors? Whether or not notice is required to perfect a sale, are there any benefits to giving notice – such as cutting off obligor set-off rights and other obligor defences?

In general, the seller is to inform the obligor of the sale of the receivables. However, there are exceptions where the consent of the obligor is mandatory (cases involving public companies in foreign exchange operations, for example, as explained under section 3). In the case where the receivables agreement between the seller and the obligor provides for obligor's consent, the seller has to obtain the obligor's consent to the sale of receivables.

The obligor may file all objections he personally has towards the purchaser (irrespective of the sale of receivables) and may file objections which he could file against the seller up to the moment he learned of the transfer, i.e. sale of the receivables.

4.5 Notice Mechanics. If notice is to be delivered to obligors, whether at the time of sale or later, are there any requirements regarding the form the notice must take or how it must be delivered? Is there any time limit beyond which notice is ineffective – for example, can a notice of sale be delivered after the sale, and can notice be delivered after insolvency proceedings have commenced against the obligor or the seller? Does the notice apply only to specific receivables or can it apply to any and all (including future) receivables? Are there any other limitations or considerations?

In general, there are no conditions as to the form of notice. However, in the case of factoring, the notice has to be given either in writing or electronically.

In general, there is no time limit as to the effectiveness of the notice. However, in the case of factoring, sale presupposes the notice to have been already given to the obligor. In the case of insolvency proceedings, a written notification to the obligor in insolvency has to be delivered to the insolvency administrator until the issuing of the decision on main distribution of liquidated assets.

In general, there are no limitations as to whether the sale concerns specific receivables, all or future receivables. In the case of factoring, the sale only covers any existing non-mature or future short-term monetary claim, in whole or in part, arising from a sale of goods/services, entered between legal entities and entrepreneurs.

4.6 Restrictions on Assignment – General Interpretation. Will a restriction in a receivables contract to the effect that "None of the [seller's] rights or obligations under this Agreement may be transferred or assigned without the consent of the [obligor]" be interpreted as prohibiting a transfer of receivables by the seller to the purchaser? Is the result the same if the restriction says "This Agreement may not be transferred or assigned by the [seller] without the consent of the [obligor]" (i.e., the restriction does not refer to rights or obligations)? Is the result the same if the restriction says "The obligations of the [seller] under this Agreement may not be transferred or assigned by the [seller] without the consent of the [obligor]" (i.e., the restriction does not refer to rights)?

The Serbian regulations on obligations allow for the seller and the obligor to contract such a term, therefore it could be interpreted as allowing the prohibition of a transfer of receivables by the seller to the purchaser.

The second case concerns the assignment of an agreement, where all rights and obligations of one party to the contract are being assigned; therefore, the law sets that there must be consent of the party in the agreement. Legally, this is a different situation but the outcome would be the same.

In the case of restriction on the sale of the seller's liabilities, this would not be interpreted as a restriction on assignment of rights of the seller, since it is clear that the restriction does not refer to the rights of the seller.

4.7 Restrictions on Assignment; Liability to Obligor. If any of the restrictions in question 4.6 are binding, or if the receivables contract explicitly prohibits an assignment of receivables or "seller's rights" under the receivables contract, are such restrictions generally enforceable in your jurisdiction? Are there exceptions to this rule (e.g., for contracts between commercial entities)? If your jurisdiction recognises restrictions on sale or assignment of receivables and the seller nevertheless sells receivables to the purchaser, will either the seller or the purchaser be liable to the obligor for breach of contract or tort, or on any other basis?

Yes, the restrictions in question 4.6 if stipulated under the agreement are binding and they are generally enforceable in Serbia.

No, there are no specific exceptions for contracts between commercial entities.

Primarily, the seller would be liable to the obligor in the case of breaching the restriction. According to the Serbian regulations on obligations, the sale or assignment of receivable shall have no effect towards the obligor in the case of restriction to sale/assignment. However, procedurally speaking and depending on the facts of the case, the obligor could sue both the seller and the purchaser.

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4.8 Identification. Must the sale document specifically identify each of the receivables to be sold? If so, what specific information is required (e.g., obligor name, invoice number, invoice date, payment date, etc.)? Do the receivables being sold have to share objective characteristics? Alternatively, if the seller sells *all* of its receivables to the purchaser, is this sufficient identification of receivables? Finally, if the seller sells *all* of its receivables *other than* receivables owing by one or more specifically identified obligors, is this sufficient identification of receivables?

Per the Serbian regulations on obligations, the seller is to deliver to the purchaser an invoice, agreement or any other document evidencing the receivable, as well as other evidences on the transferred receivable and accessory rights. If requested by the purchaser, the seller is to issue a notarised certificate on the sale of the receivable. Therefore, in general, there is no specific information or a specific document directly regulated under the law, but for the full identification of the obligor's name and the evidence as to the receivable that has to be as such so as for the court (in a potential case) to ascertain the existence of the receivable and the transfer thereof with sufficient credibility. In general, there is no obligation as to specific identification of each of the receivables, but the evidence as to the existence and transfer of the receivable has to be sufficient for the court to ascertain them. This also applies to the sale of all of the receivables or sale of all of receivables other than receivables owing by one or more specifically identified obligors.

In the case of factoring, the agreement has to contain the data set under the Law on Factoring of Serbia (data on the contracting parties, type of factoring, legal basis and data on the receivable from the receivables agreement, amount, manner of calculation and payment for the purchased receivable to the seller, amount, manner of calculation and payment of the factoring fee, right of the factor to interest and other costs which may come from performance of the agreement and the date of the agreement).

In case of sale of receivables against an obligor in insolvency proceedings, only the receivable, i.e. the claim filed to the insolvency administrator could be the subject of the sale/assignment.

4.9 Recharacterisation Risk. If the parties describe their transaction in the relevant documents as an outright sale and explicitly state their intention that it be treated as an outright sale, will this description and statement of intent automatically be respected or is there a risk that the transaction could be characterised by a court as a loan with (or without) security? If recharacterisation risk exists, what characteristics of the transaction might prevent the transfer from being treated as an outright sale? Among other things, to what extent may the seller retain any of the following without jeopardising treatment as an outright sale: (a) credit risk; (b) interest rate risk; (c) control of collections of receivables; (d) a right of repurchase/redemption; (e) a right to the residual profits within the purchaser; or (f) any other term?

The general rule is that the Court would analyse the entirety of the agreement, i.e. of the stipulated rights and obligations of the parties and only then would it conclude on the character of the agreement. Therefore, the recharacterisation risk could potentially exist, depending on the facts of the case. The fact of a security existing in the transaction could boost the possibility of the transfer being characterised as a loan.

As to the second and third question, as stated in the previous paragraph hereinabove, the conclusion would depend on the overall facts of the case by a court; therefore retaining some of the items by the seller does not mean that the court would automatically conclude that there is an outright sale or a loan.

4.10 Continuous Sales of Receivables. Can the seller agree in an enforceable manner to continuous sales of receivables (i.e., sales of receivables as and when they arise)? Would such an agreement survive and continue to transfer receivables to the purchaser following the seller's insolvency?

In general, yes it is possible for the seller to agree in an enforceable manner to continue sale of receivables as and when they arise.

As to insolvency, only until reaching the decision on the final distribution of liquidated assets of the insolvent obligor.

4.11 Future Receivables. Can the seller commit in an enforceable manner to sell receivables to the purchaser that come into existence after the date of the receivables purchase agreement (e.g., "future flow" securitisation)? If so, how must the sale of future receivables be structured to be valid and enforceable? Is there a distinction between future receivables that arise prior to *versus* after the seller's insolvency?

As to the first question, the answer is affirmative. The exception would be the insolvency procedure, where only filed claims could be subject to sale/assignment and only until reaching the decision on the final distribution of liquidated assets of the insolvent obligor.

As explained earlier, in general, there are no specific requests as to the content of the receivables purchase agreement, save in specific cases like factoring (as explained under question 4.8).

There is a distinction between the future receivables that arise prior to the seller's insolvency, to the ones that arise after it. Those that arise before the opening of the insolvency procedure, if not matured, shall become mature and must be filed to the insolvency administrator. As to future receivables arising after the opening of the insolvency procedure, such receivables are considered as conditional (either as a deferred or breakdown condition), and the insolvency administrator shall provide for adequate funds from the insolvency mass for settling such claims. In case of a deferred conditional receivable, if the condition does not occur until the decision on main distribution of liquidated assets becomes final, the receivable shall cease to exist and if the breakdown condition does not occur until the said decision becoming final, such condition shall be deemed as if it never existed.

4.12 Related Security. Must any additional formalities be fulfilled in order for the related security to be transferred concurrently with the sale of receivables? If not all related security can be enforceably transferred, what methods are customarily adopted to provide the purchaser the benefits of such related security?

In case of collateral over movable assets and mortgage, there are formalities to be fulfilled. Both cases also require registration at competent registers (business register/cadastre).

In line with the Serbian regulations on obligations, accessory rights such as right to preferential collection, mortgage, collateral over movable assets, rights from guarantee agreements, right to

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interest, contractual penalty etc. shall be transferred along with the receivable; therefore it is unlikely to expect that any of the security would not be enforceably transferred.

4.13 Set-Off; Liability to Obligor. Assuming that a receivables contract does not contain a provision whereby the obligor waives its right to set-off against amounts it owes to the seller, do the obligor's set-off rights terminate upon its receipt of notice of a sale? At any other time? If a receivables contract does not waive set-off but the obligor's set-off rights are terminated due to notice or some other action, will either the seller or the purchaser be liable to the obligor for damages caused by such termination?

The obligor may file objections against the purchaser which it has directly towards him as well as those objections which he could file against the seller up to the moment he learned of the sale of the receivable. The seller and the purchaser cannot by themselves strip the obligor of the rights set under the Law and potential rights to set-off. However, since the Serbian law prohibits any set-off during the period of blockade of accounts of a party, if e.g. the purchaser's account is blocked and due to this situation there is no possibility for set-off, the obligor would be obliged to pay to the account of the purchaser the debt which has been transferred to the purchaser, and would have the right to block the account of the purchaser for the amount due to the obligor or later on try to enforce its receivables towards the purchaser. Please note also, that the seller cannot transfer the debt in the cases where his accounts are blocked. If, however, in any circumstances any right of the obligor is breached by the actions of the sellers and/or the purchaser, the obligor could have the right to request compensation of damage.

4.14 Profit Extraction. What methods are typically used in your jurisdiction to extract residual profits from the purchaser?

Dividends, salaries (to the management), and retaining profits.

5 Security Issues

5.1 Back-up Security. Is it customary in your jurisdiction to take a "back-up" security interest over the seller's ownership interest in the receivables and the related security, in the event that an outright sale is deemed by a court (for whatever reason) not to have occurred and have been perfected (see question 4.9 above)?

Back-up security is not customary in the Serbian legal practice, save for loans/credits (usually syndicated) with a foreign element which are usually governed by the English law with foreign arbitration clauses. However, it is questionable what the court practice would be as to interpretation of the back-up security. It should be taken into account that capital markets in Serbia are fragmented and undeveloped and the industry heavily relies on commercial or financial credits and loans taken from the banks on regular basis.

5.2 Seller Security. If it is customary to take back-up security, what are the formalities for the seller granting a security interest in receivables and related security under the laws of your jurisdiction, and for such security interest to be perfected?

Though back-up security is rarely practised in Serbia as explained above, this would depend on the form of the security granted. For the forms of collaterals (promissory notes, mortgages, collateral over movables) please refer to answers in section 4 above.

5.3 Purchaser Security. If the purchaser grants security over all of its assets (including purchased receivables) in favour of the providers of its funding, what formalities must the purchaser comply with in your jurisdiction to grant and perfect a security interest in purchased receivables governed by the laws of your jurisdiction and the related security?

If the purchaser has assets in Serbia, it is free to provide security to the providers of funding in line with formalities set under the Serbian law as described above for each specific collateral.

As regards the security interest in purchased receivables the purchaser may enter with the providers of its funding in a pledge agreement whereunder the receivable is pledged in favour of the providers of funding. The relevant pledge is subject to registration with the Register of Pledges kept with the Agency for Commercial Registers. Further, if so agreed, the purchaser may transfer by endorsement promissory notes to the fund providers and also may enter into an agreement on a super-mortgage, allowing the fund provider to be registered as the super-mortgage creditor in the relevant Cadastre of immovable, where the immovable of the original obligor is recorded. The super-mortgage has effects on the obligor of the receivable as of the receipt of the written information on the pledge of receivables, and has effect towards third parties from the day of registration in the Cadastre Register.

5.4 Recognition. If the purchaser grants a security interest in receivables governed by the laws of your jurisdiction, and that security interest is valid and perfected under the laws of the purchaser's jurisdiction, will the security be treated as valid and perfected in your jurisdiction or must additional steps be taken in your jurisdiction?

The answer would depend on the residential status of the parties to the receivables contract and the receivables purchase contract rather than the choice of law. It is very likely that the enforcement of a security in Serbia would require meeting criteria from the Law on Foreign Exchange. For example, in accordance with Article 33, a resident may collect payment from or make payment to a non-resident other than the one (non-resident) towards which the resident has the debt, from whom he has the claim, on the basis of a contract signed by all the parties to such legal affair or on the basis of a statement of the resident that he has been informed of such transfer. Therefore, in such case, the security would require additional steps to be taken in the Serbian jurisdiction. Further, to be on the safe side for the purposes of enforcement it would be advisable for the obligor to be informed and for the pledge to be recorded in the Register of Pledges and other required registers (e.g. super-mortgage as mentioned above), for the fund provider to be able to enforce security interest against the obligor in the Serbian jurisdiction with no formal obstacles *in re* identification of the creditor in the process.

5.5 Additional Formalities. What additional or different requirements apply to security interests in or connected to insurance policies, promissory notes, mortgage loans, consumer loans or marketable debt securities?

As regards the insurance policies, it is usual that an insurance policy

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is issued for the benefit of the bank as a security for a mortgage loan (life insurance), and it is the obligation of the insured person and the insurance company to contract assignment of insurance right to the bank if the insured situation occurs (no other formalities required).

There are no additional formalities unless set under the specific regulation for the specific obligor. Namely, a physical person obligor is protected under the laws with special rights e.g.: it is not possible to contract under the agreement on pledge with a physical person that the object of pledge will be transferred into ownership of the holder of pledge if the claim is not settled in full, and also it is not possible to set in advance the price for the object of pledge; there is the Law on Protection of Users of Financial Services that further regulates the relevant issues concerning the protection of consumers of banking and financial leasing services.

5.6 Trusts. Does your jurisdiction recognise trusts? If not, is there a mechanism whereby collections received by the seller in respect of sold receivables can be held or be deemed to be held separate and apart from the seller's own assets (so that they are not part of the seller's insolvency estate) until turned over to the purchaser?

Trusts do not exist in Serbia as a legal form. However, if the law to be applied by a Serbian Court is a legal system with trust law, there is a possibility for a trust to be recognised but only in a specific case brought in front of the Court.

No, there is no effective mechanism for such receivables to be held as the seller's assets separate from his other assets until turned to the purchaser.

5.7 Bank Accounts. Does your jurisdiction recognise escrow accounts? Can security be taken over a bank account located in your jurisdiction? If so, what is the typical method? Would courts in your jurisdiction recognise a foreign law grant of security (for example, an English law debenture) taken over a bank account located in your jurisdiction?

There is no specific regulation of the escrow accounts under the Law, but they are possible and are used in practice in Serbia. Please note, however, that the owner of the account needs to be one person (not all interested), but the conditions for release may be freely agreed between the parties and the bank. In Serbia, as the issue is not so regulated, the bank would require a clear instruction issued and signed by the persons authorised to dispose of the funds.

It is possible to establish the security over the bank account located in Serbia. One should note that the relevant bank account, however, is not exempted from blockade (under the specific laws and regulations regulating the issue of enforcement) in the case of compulsory enforcement against the obligor by other creditors.

The security over a bank account requires a written agreement on collateral over the bank account and registration of the collateral at the business register of the Agency for Commercial Registers of Republic of Serbia.

As to foreign law granting of security, please refer to the answers given under question 5.4.

5.8 Enforcement over Bank Accounts. If security over a bank account is possible and the secured party enforces that security, does the secured party control all cash flowing into the bank account from enforcement forward until the secured party is repaid in full, or are there limitations? If there are limitations, what are they?

According to the Law on Pledge over Movable Assets Registered in the Register of Republic of Serbia, as of the moment of enforcement of the pledge, the pledgor must deliver the subject of the security or a document required for possession over a security to the pledgee (i.e. secured party) and until doing so he must refrain from actions which may lead to the decrease of the value of the security and shall be liable to the secured party for possible damages. Legally, as of coming into default, the pledgor is no longer in possession of the bank account. Therefore, from the moment when the secured party is in possession of the bank account, it would control all cash flow but up to the secured amount.

5.9 Use of Cash Bank Accounts. If security over a bank account is possible, can the owner of the account have access to the funds in the account prior to enforcement without affecting the security?

The owner, as a pledgor, has the right to use the funds in the account prior to the enforcement; however, it must not take actions which would decrease the value of the security. The issues of the use of the bank account and eventual yields from the account can be set differently by the secured party and the owner as the pledgor of the bank account (e.g. the use of the funds may be conditioned by co-signature of the creditor etc.).

6 Insolvency Laws

6.1 Stay of Action. If, after a sale of receivables that is otherwise perfected, the seller becomes subject to an insolvency proceeding, will your jurisdiction's insolvency laws automatically prohibit the purchaser from collecting, transferring or otherwise exercising ownership rights over the purchased receivables (a "stay of action")? If so, what generally is the length of that stay of action? Does the insolvency official have the ability to stay collection and enforcement actions until he determines that the sale is perfected? Would the answer be different if the purchaser is deemed to only be a secured party rather than the owner of the receivables?

Under the Serbian law there is no possibility for assignment, takeover of claim/debt, assignment of collection and similar if a party in the legal operation (and especially seller) has blocked accounts in the process of compulsory enforcement in line with the law. Therefore, if prior to official initiation of insolvency the accounts of the seller were for a period of time blocked (which, in practice, is usually the case), any transfer of receivables would be highly problematic.

In the case where the receivable has been transferred to the purchaser, the receivable is no longer in the ownership of the seller, therefore it could not be subject to insolvency proceedings. In the case where the seller is still in possession of the receivable but the purchaser has the ownership over the receivable (if that is hypothetically possible, depending on the type of the receivable), the purchaser may seek possession over the receivable from the seller/insolvency administrator. However, the insolvency administrator or

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other creditors of the seller in insolvency may challenge the sale of receivables at the court of law in case such sale was to the detriment of the seller or its creditors. Such challenge may go for sales made as far as five years as of the opening of the insolvency proceedings, depending on the case.

As to "stay of action", the answer would depend on whether the insolvency ended up in bankruptcy or in the restructuring of an insolvent seller.

In the case where the sale of receivables was actually an assignment of the right to collect payment from the obligor by the purchaser, the ownership rights over the receivable are still in the hands of the seller making the receivable its asset and therefore part of the insolvency proceedings. And in general, where the seller had ownership title over a receivable before the opening of the insolvency procedure, the receivable would be part of the assets of the insolvent seller. In the case where the insolvency proceedings ended up in bankruptcy of the insolvent seller, there would be no "stay of action" but the claims of the creditors would be settled from the liquidated assets of the insolvent seller in the priority given by the law. In such cases, the purchaser would become an insolvency creditor with a 3rd degree priority in collection from the liquidated assets of the insolvent seller. In the case where the purchaser has already sued the seller in front of the court before the opening of the insolvency proceedings, the litigation would be halted and the purchaser would have to file their claim in the insolvency proceedings in order for the claim to be accepted/denied by the insolvency administrator. If the filed claim has been denied by the administrator, the purchaser is entitled to continue the litigation until the final decision is reached (or could file a new lawsuit against the insolvent seller), and the enforcement would be executed in the legal order of priority (as an insolvency creditor, that would be 3rd degree priority), if there are liquidated assets for consummation of the claim.

If the insolvency proceedings ended up in the restructuring of the insolvent seller, there would potentially be a "stay of action". A restructuring plan would be drawn, which would usually lead to a debt restructuring (including payment deadlines). The deadline for performing the restructuring plan cannot exceed five years.

In the case of a contract with rights and obligations on both sides and which has not been performed by the parties in whole or in part up till the moment of the opening of the insolvency proceedings, the contracting party of the insolvent party may ask the insolvency administrator to declare whether it would continue to perform the contract or not. In the case where the insolvency administrator accepts to perform the obligations from such contract, the obligations of the insolvent party would be considered as the costs of the insolvency proceeding and the claim of the contracting party would have 1st degree priority in collection from the liquidated assets of the insolvent party.

All collections and enforcements from the moment of opening of the insolvency proceedings would be null and void by law.

In the case where the seller's receivable has been given as a security to the purchaser, the purchaser would become a secured obligor in the insolvency proceeding with a power to seek priority collection from the value of the secured receivable.

6.2 Insolvency Official's Powers. If there is no stay of action, under what circumstances, if any, does the insolvency official have the power to prohibit the purchaser's exercise of its ownership rights over the receivables (by means of injunction, stay order or other action)?

If the purchaser is the owner of the receivable, as explained above, he would not be an insolvency creditor and may exercise his rights outside the insolvency proceedings. However, in such case the purchaser would have to file a request to the insolvency administrator to accept and recognise the purchaser's ownership rights over the receivable. Where the administrator accepts and recognises the ownership rights of the purchaser, the purchaser would be free to take actions as to the receivable, though this would not exclude the right of the insolvency administrator to potentially seek an injunction, though it is questionable whether such injunction would be successful if the administrator has recognised and accepted the rights of the purchaser over the receivables. As mentioned above there is also possibility to challenge the sale. If the administrator refuses to accept and recognise the ownership rights, the purchaser would have to start the litigation process.

Otherwise, if the seller remained the owner, the purchaser may only exercise his rights within the insolvency proceedings and his claim would be settled from the liquidated assets (if any) of the insolvent seller, once it was accepted by the insolvency administrator. Therefore, in such a case the purchaser cannot take actions over the receivables and such actions would be null and void.

6.3 Suspect Period (Clawback). Under what facts or circumstances could the insolvency official rescind or reverse transactions that took place during a "suspect" or "preference" period before the commencement of the seller's insolvency proceedings? What are the lengths of the "suspect" or "preference" periods in your jurisdiction for (a) transactions between unrelated parties, and (b) transactions between related parties? If the purchaser is majority-owned or controlled by the seller or an affiliate of the seller, does that render sales by the seller to the purchaser "related party transactions" for purposes of determining the length of the suspect period? If a parent company of the seller guarantee's the performance by the seller of its obligations under contracts with the purchaser, does that render sales by the seller to the purchaser "related party transactions" for purposes of determining the length of the suspect period?

Depending on the facts of the case, it could go up to five years as of the filing of the motion for insolvency proceedings.

The issue of related/unrelated parties does not influence the length of the suspect/preference period, but it does create legal presumptions for related parties as to whether a contracting party of the insolvent party knew of the circumstances which represent reasons for initiation of the insolvency proceedings. Again, the longest period (irrespective of related/unrelated parties) is five years as of the filing of the motion for insolvency proceedings.

A majority-owned or controlled purchaser of the seller or an affiliate thereof would render sales as a related party transaction. However, as explained above, the suspect period is not related to the issue of the relations of the parties.

As to the last question, as explained above, the issue of related/unrelated parties does not influence the length of the suspect period but creates legal presumptions on the grounds for challenging the sale.

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6.4 Substantive Consolidation. Under what facts or circumstances, if any, could the insolvency official consolidate the assets and liabilities of the purchaser with those of the seller or its affiliates in the insolvency proceeding? If the purchaser is owned by the seller or by an affiliate of the seller, does that affect the consolidation analysis?

Legally speaking, there is no legal institute of substantive consolidation in the Serbian bankruptcy law. The insolvency administrator could potentially sue in front of the court seeking determination that assets and liabilities of another entity (usually a related person) actually belong to the insolvent obligor or potentially seek veil piercing of the related party if there are grounds for it.

Where the purchaser is owned by the seller, there would be no substantive consolidation, but the insolvency administrator may sell capital of the seller in the purchaser.

6.5 Effect of Insolvency on Receivables Sales. If insolvency proceedings are commenced against the seller in your jurisdiction, what effect do those proceedings have on (a) sales of receivables that would otherwise occur after the commencement of such proceedings, or (b) on sales of receivables that only come into existence after the commencement of such proceedings?

a) Once the proceedings have commenced, in the sense of opening of the insolvency proceedings, the insolvent seller would not be entitled to create a commitment to sell its receivables. In case of a receivables purchase contract signed but not performed until opening of the insolvency proceedings, please see the answers to question 6.1.

b) As explained under a), there is no legal possibility for the seller to commit to sales of receivables once the proceedings have been opened.

6.6 Effect of Limited Recourse Provisions. If a a debtor's contract contains a limited recourse provision (see question 7.3 below), can the debtor nevertheless be declared insolvent on the grounds that it cannot pay its debts as they become due?

Limited Recourse would not have effect on the obligor's insolvency, since the grounds for initiation of insolvency proceedings are set under the law and the court would focus only on existence of such grounds. Such grounds include inability to meet payment obligations for a longer continued period of time, a threat of such inability, indebtedness and failure to act per the adopted reorganisation plan and if the reorganisation plan has been worked out in a fraudulent or illegal manner.

7 Special Rules

7.1 Securitisation Law. Is there a special securitisation law (and/or special provisions in other laws) in your jurisdiction establishing a legal framework for securitisation transactions? If so, what are the basics? Is there a regulatory authority responsible for regulating securitisation transactions in your jurisdiction?

There is no special law on securitisation in Serbia. There were earlier talks that Serbia would introduce securitisation, but it never happened. There is no explicit legal framework for securitisation transactions, though the Law on Capital Markets of Serbia does mention secured securities in the definition section but has no other provisions on securitisation (as to process, terms etc.). Technically, the Law on Capital Markets regulates the process of the issuing of securities which also covers the issue of secured debt securities, but it is likely that the actual issue of secured debt securities would require a specific material law regulating securitisation.

It is hard to say whether securitisation could be effected on the basis of the existing Serbian regulations, since there were no cases of securitisation in Serbia.

There is no specific authority to regulate securitisation due to the lack of explicit legal framework, though if the securitisation would be hypothetically feasible under the existing regulation and if it would involve banking loans/credits, the National Bank of Serbia and the Securities Commission of Serbia would be involved in the process.

7.2 Securitisation Entities. Does your jurisdiction have laws specifically providing for establishment of special purpose entities for securitisation? If so, what does the law provide as to: (a) requirements for establishment and management of such an entity; (b) legal attributes and benefits of the entity; and (c) any specific requirements as to the status of directors or shareholders?

Having in mind the answers given to question 7.1, there are no laws providing such matters. However, the Law on Capital Markets speaks, when listing certain investment services of an investment company, of investment services linked to, *inter alia*, secured debt securities. Due to the lack of legal framework for securitisation, it is not likely for investment companies to be perceived as special purpose entities.

7.3 Location and form of Securitisation Entities. Is it typical to establish the special purpose entity in your jurisdiction or offshore? If in your jurisdiction, what are the advantages to locating the special purpose entity in your jurisdiction? If offshore, where are special purpose entities typically located for securitisations in your jurisdiction? What are the forms that the special purpose entity would normally take in your jurisdiction and how would such entity usually be owned?

Please refer to answers given under questions 7.1 and 7.2.

7.4 Limited-Recourse Clause. Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) limiting the recourse of parties to that agreement to the available assets of the relevant obligor, and providing that to the extent of any shortfall the debt of the relevant obligor is extinguished?

The Serbian regulations on obligations do not explicitly recognise the concept of a limited-recourse clause in the sense given in this question.

The existing Serbian provisions which regulate the issues of contract obligation performance do not give rise to questioning the possibility of establishing such clause. However, the provisions of the law regarding limitations to contractual damages establish a concept of limited liability connected to the amount of damages to be owed,

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not to what the object/source of damage compensation could only be. Also, some of those provisions are mandatory thereby excluding the ability of the parties to regulate contractual damages per their own will. Therefore, to the extent where the limited recourse clause does not go against such provisions of the law, such clause could be potentially permitted. Please bear in mind that the use of limited recourse clauses under the Serbian law as the governing law has not been practised to a visible extent of court of law practices and clear standpoints, and it is questionable what the court practice would be.

If a governing law of another country is to be applied by the Serbian Court and the governing law recognises limited recourse clauses, the court would have to enforce them. Please bear in mind that complete facts of the case may lead to mandatory application of some Serbian regulations which would apply irrespective of the governing law, which may articulate differently to the application of limited recourse clauses.

7.5 Non-Petition Clause. Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) prohibiting the parties from: (a) taking legal action against the purchaser or another person; or (b) commencing an insolvency proceeding against the purchaser or another person?

As regards both issues, the relevant provision could be contested by a party as unjust as there are certain rights of a party that cannot be waived at all (e.g. in the case of fraud, misleading, full non-performance, etc.). Therefore, the risk that such clauses would not be given effect by a Serbian Court is high.

7.6 Priority of Payments "Waterfall". Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) distributing payments to parties in a certain order specified in the contract?

The Court in Serbia would, in principle, give effect to a contractual provision in an agreement distributing payments to parties in a certain order specified in the contract, unless there is a specific provision prohibiting the kind of payment. Namely, if a party has blocked accounts in an enforcement process, and the payment to any other party is made by assignment, transfer of claim or similar, the payment and performance under such clause would not be allowed during such compulsory enforcement, i.e. blockade of accounts.

7.7 Independent Director. Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) or a provision in a party's organisational documents prohibiting the directors from taking specified actions (including commencing an insolvency proceeding) without the affirmative vote of an independent director?

In case of agreements, if such actions do not relate to taking legal actions in front of competent governmental bodies, then yes. Therefore, the commencing of insolvency proceedings could not be effectively prohibited by an agreement.

Organisational documents could establish such prohibitions, in the sense of breach of corporative procedures which could trigger voidance of actions taken without such consent. Please note that the risk of cases where organisational documents could not override provisions of the law and therefore making such provision null and void could not be excluded.

7.8 Location of Purchaser. Is it typical to establish the purchaser in your jurisdiction or offshore? If in your jurisdiction, what are the advantages to locating the purchaser in your jurisdiction? If offshore, where are purchasers typically located for securitisations in your jurisdiction?

There is no clear usual practice with which to answer this question.

8 Regulatory Issues

8.1 Required Authorisations, etc. Assuming that the purchaser does no other business in your jurisdiction, will its purchase and ownership or its collection and enforcement of receivables result in its being required to qualify to do business or to obtain any licence or its being subject to regulation as a financial institution in your jurisdiction? Does the answer to the preceding question change if the purchaser does business with more than one seller in your jurisdiction?

If the transaction is factoring in the sense of the Serbian law, i.e. financial service of sale and purchase of an existing undue or future short-term pecuniary claim, existing on the basis of agreement on sale of goods or granting of services made with a foreign element in the sense of the law regulating the foreign trade operations (one of the parties is a foreign person), the purchaser factor does not need to have licence or presence in Serbia.

If the transaction is factoring in the sense of the Serbian law, as described above, but without the foreign element, the purchaser has to have a licence to operate in Serbia.

A receivable towards a physical person cannot be subject to factoring.

If the transaction is the sale of a claim of a bank from a financial credit/banking operation:

a) The purchaser does not need to have operations in Serbia, but the credit has to be reported to the National Bank of Serbia with full observing of the Law on Foreign Exchange.

b) The purchaser of a claim towards a physical person may only be another bank with the licence to operate in Serbia.

Regarding the issue under point (a) please note that a bank may transfer only due receivables or receivables that are considered as problematic in line with the regulations made by the National Bank of Serbia. The sale has to be reported to the National Bank of Serbia at least 30 days in advance.

If the obligor is a physical person and receivables arise from the payment operations towards the issuer of cards and e-money, it may be sold to a bank or other renderer of payment operations with the licence for operations in Serbia.

8.2 Servicing. Does the seller require any licences, etc., in order to continue to enforce and collect receivables following their sale to the purchaser, including to appear before a court? Does a third-party replacement servicer require any licences, etc., in order to enforce and collect sold receivables?

Please see the responses under question 8.1. If there is a requirement for a licence for acquiring of a receivable, such a licence requirement remains for the collection of receivables following the sale to the purchaser. A third-party replacement service does not require any licence in order to enforce and collect receivables.

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As to court enforcement or collection following the sale, the seller would have to provide evidence as to the authorisation for enforcement/collection given by the purchaser. This would also apply to the third-party replacement servicer. However, please note that in the case of compulsory settlement only a licence enforcement officer may carry out the same in a controlled process.

8.3 Data Protection. Does your jurisdiction have laws restricting the use or dissemination of data about or provided by obligors? If so, do these laws apply only to consumer obligors or also to enterprises?

There is the Law on Personal Data Protection. This law applies both to consumer obligors and enterprises as record keepers of personal data. Only data on physical persons are subject to such protection.

The banks are subject to banking secrecy rules. The National Bank of Serbia allows for the data to be provided in the process of due diligence completed by potential purchasers of loans, but such should be also subject to confidentiality clauses. Admittedly, the issue is yet to be regulated additionally.

8.4 Consumer Protection. If the obligors are consumers, will the purchaser (including a bank acting as purchaser) be required to comply with any consumer protection law of your jurisdiction? Briefly, what is required?

If the case concerns consumer loans/credits, as explained earlier, the sale of receivables is possible only between domestic banks. There is an obligation to comply with the Law on Protection of Consumers of Financial Services. Outside financial services, it is highly likely that the purchaser would have to comply with the consumer protection laws of Serbia. Receivables against consumers cannot be subject to factoring.

8.5 Currency Restrictions. Does your jurisdiction have laws restricting the exchange of your jurisdiction's currency for other currencies or the making of payments in your jurisdiction's currency to persons outside the country?

The National Bank of Serbia provides a list of currencies which could be exchanged for the Serbian Dinar. There is a list of 21 currencies for which the Serbian Dinar could be exchanged. Therefore, there are restrictions, though the list of permitted currencies is long.

Payments to persons outside Serbia and in Serbian Dinars are feasible only if the payment is made to a non-resident bank account located in Serbia.

8.6 Risk Retention. Does your jurisdiction have laws or regulations relating to "risk retention"? How are securitisation transactions in your jurisdiction usually structured to satisfy those risk retention requirements?

There are no laws regulating risk retention in Serbia.

There is no experience as to structuring of securitisation transactions (or at least it is very scarce and there is practically no legal practice to that matter).

8.7 Regulatory Developments. Have there been any regulatory developments in your jurisdiction which are likely to have a material impact on securitisation transactions in your jurisdiction?

As explained earlier, the Serbian financial system almost exclusively relies on bank financing and capital markets, in the sense of private IPOs, and especially as to the issue of backed debt securities, are scarce. There were talks that Serbia would introduce laws regulating securitisation, but this has not happened insofar.

9 Taxation

9.1 Withholding Taxes. Will any part of payments on receivables by the obligors to the seller or the purchaser be subject to withholding taxes in your jurisdiction? Does the answer depend on the nature of the receivables, whether they bear interest, their term to maturity, or where the seller or the purchaser is located? In the case of a sale of trade receivables at a discount, is there a risk that the discount will be recharacterised in whole or in part as interest? In the case of a sale of trade receivables where a portion of the purchase price is payable upon collection of the receivable, is there a risk that the deferred purchase price will be recharacterised in whole or in part as interest? If withholding taxes might apply, what are the typical methods for eliminating or reducing withholding taxes?

In principle, and subject to deviation in any specific case, payments of principle of receivables by the obligors to the seller or the purchase should not be subject to any withholding taxes.

If there is nothing else set under an international treaty, withholding tax is payable to the income of a non-resident legal entity on the basis of, *inter alia*, interest. A tax to be established by the decision of the tax authority is also payable for the income made by a non-resident legal entity on the basis of capital gains that may exist in the case of, e.g. the sale of mortgaged property or similar.

Per the Law on Income Tax of Serbia, incomes from dividends and profit shares, from copyright and intellectual property rights, interests, lease and sub-lease fees for immovable and movable property on the territory of Serbia, fees from market research services, accounting and auditing services and other services from legal and business counselling irrespective of the place of service or consummation, respectively of the place where such services would be provided or consummated, such incomes would be subject to withholding taxation.

There is a possible risk of sale of trade receivables at a discount to be recharacterised as interest (in part or in whole), depending on the interpretation given by the Serbian tax authority.

There is a risk of recharacterisation *in re* of deferred purchase price payment, depending on the interpretation given by the Serbian tax authority.

9.2 Seller Tax Accounting. Does your jurisdiction require that a specific accounting policy is adopted for tax purposes by the seller or purchaser in the context of a securitisation?

As explained earlier, there are no laws on securitisation. However, Serbia applies IAS and other accounting standards, so if such standards require such specific policy, it is likely that the seller must have such policy.

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9.3 Stamp Duty, etc. Does your jurisdiction impose stamp duty or other transfer or documentary taxes on sales of receivables?

Stamp duty as defined under common law does not exist in Serbia. However, there are taxes burdening the transfer of ownership over immovable property or a lease etc., but comparison with a stamp duty should be taken with caution, due to the potentially different operation of stamp duty and such taxes levied in Serbia.

The sale of receivables which would include shares or other securities is exempted from VAT or taxes on transfer of ownership rights.

9.4 Value Added Taxes. Does your jurisdiction impose value added tax, sales tax or other similar taxes on sales of goods or services, on sales of receivables or on fees for collection agent services?

Sales of goods/services are, in general, subject to VAT. As to sales of receivables, if this concerns sales of monetary claims, cheques, promissory notes and similar securities, such sales are exempted from VAT, save if collection is made for the account of third parties.

9.5 Purchaser Liability. If the seller is required to pay value-added tax, stamp duty or other taxes upon the sale of receivables (or on the sale of goods or services that give rise to the receivables) and the seller does not pay, then will the taxing authority be able to make claims for the unpaid tax against the purchaser or against the sold receivables or collections?

In case of sale of goods/services, the tax duty in the sense of VAT would lie on the seller and not on the obligor or purchaser of receivables. As explained under question 9.4, sale of receivables is generally exempted from VAT. If, however, the VAT is payable, i.e. not exempted and the seller is a foreign legal person, the risk of claim against purchaser cannot be eliminated.

If the case would concern other taxes (such as transfer of ownership over immovable property), there is a possibility for the purchaser to be subject to paying such taxes. As to the collection of taxes, the whole assets of the tax obligor could be subject to tax collection, therefore the sold receivables could also be subject to tax collection.

9.6 Doing Business. Assuming that the purchaser conducts no other business in your jurisdiction, would the purchaser's purchase of the receivables, its appointment of the seller as its servicer and collection agent, or its enforcement of the receivables against the obligors, make it liable to tax in your jurisdiction?

As explained earlier, the sale of receivables in the sense of monetary receivables is not subject to VAT or other taxes. However, if the seller acts as a collection agent, the seller would be liable to pay VAT, since it is making a collection for the account of the purchaser. As a foreign entity, the purchaser could not be held liable for taxes in Serbia, but the Serbian tax authorities would charge the Serbian resident involved in the transaction, if there is a tax obligation to be honoured. If a foreign purchaser applied and obtained a Serbian VAT number, it could be held liable for VAT, if applicable.

9.7 Taxable Income. If a purchaser located in your jurisdiction receives debt relief as the result of a limited recourse clause (see question 7.3 above), is that debt relief liable to tax in your jurisdiction?

The debt relief would be part of the calculation of incomes and expenses when filing a tax return for income tax, and whether there would be taxation would depend on accounting standards applied and the interpretation and acceptance of such calculation by the tax authority.

Acknowledgment

Special acknowledgment and tribute goes to Miodrag Jevtić, Senior Associate, who greatly contributed to the detailed research of various aspects of Securitisation law for this chapter.

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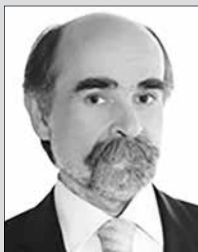

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Singapore

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1 Receivables Contracts

1.1 Formalities. In order to create an enforceable debt obligation of the obligor to the seller: (a) is it necessary that the sales of goods or services are evidenced by a formal receivables contract; (b) are invoices alone sufficient; and (c) can a binding contract arise as a result of the behaviour of the parties?

Under Singapore law, it is generally not necessary for a sale of goods or services to be evidenced by a formal receivables contract in order to create an enforceable debt obligation of the obligor to the seller. The debt obligation of the obligor to the seller may also be enforced if parties can demonstrate that there was an oral or implied agreement supported by consideration. This is reiterated in Section 4 of the *Sale of Goods Act* (Cap. 393, 1999 Revised Edition). It would nonetheless still be advisable from an evidentiary viewpoint to have a receivables contract reduced to writing.

It should be noted, however, that certain debt obligations must be evidenced by a written contract in order for the same to be enforceable against the obligor. For example, under Section 6 of the *Civil Law Act* (Cap. 43, 1999 Revised Edition), a contract for the sale or other disposition of immovable property or any interest in such property must be evidenced in writing. Similarly, an agreement that is not to be performed within the space of one year from the making thereof (i.e. the sale of goods and services at a future date) must also be made in writing, failing which no action may be brought on the agreement.

A binding receivables contract may be implied by the conduct of the parties notwithstanding the absence of a written agreement. The issuance of an invoice by the Seller may be construed as giving rise to a debt obligation especially where it can be established from the surrounding circumstances that parties had, by their conduct, implicitly agreed to the sale of goods and services. A typical example is where parties have a pre-existing or ongoing business relationship where the seller has issued similar invoices as part of the transaction for the sale of goods and services which have been previously accepted by the obligor as giving rise to an enforceable debt obligation.

1.2 Consumer Protections. Do your jurisdiction's laws: (a) limit rates of interest on consumer credit, loans or other kinds of receivables; (b) provide a statutory right to interest on late payments; (c) permit consumers to cancel receivables for a specified period of time; or (d) provide other noteworthy rights to consumers with respect to receivables owing by them?

There is no express limit on the rate of interest on consumer credit, loans or other kinds of receivables except where the credit, loan or other kinds of receivable has been extended by a "moneylender" as defined under Section 2 of the *Moneylenders Act* (Cap. 188, 2010 Revised Edition). However, the following guiding principles are generally considered when determining whether the interest rate imposed should be enforced:

(i) the interest rate imposed represents a genuine pre-estimate of loss and not an *in terrorem* penalty;

(ii) the terms of the contract involving a person dealing as a consumer are reasonable within the meaning of the *Unfair Contract Terms Act* (Cap. 396, 1994 Revised Edition);

(iii) the interest rate is imposed as part of a *bona fide* contract and not a sham transaction in order to circumvent any statutory or other licensing requirements applicable for moneylending; and

(iv) the interest rate imposed does not lead to the transaction being an extortionate credit transaction within the meaning of Section 103 of the *Bankruptcy Act* (Cap. 20, 2009 Revised Edition) which may be voided by the court if it was entered into within three years before the commencement of the bankruptcy of the consumer.

The *Moneylenders Act* does not apply to an "excluded moneylender" (for example, banks, credit societies, pawnbrokers or persons who lend solely to corporations or business/real estate investment trusts or who do not carry on the business of moneylending) or an "exempt moneylender".

Insofar as licensed moneylending is concerned, the prescribed maximum fees/rates chargeable on a loan by a licensed moneylender under the *Moneylenders Rules 2009* are as follows:

(a) nominal interest rate of 4% per month; and

(b) late interest at the nominal interest rate of 4% per month.

Late fees, administrative fees, variation fees, unsuccessful deductions etc. in relation to a loan (other than business loans) are also provided for and subject to certain restrictions as to how much may be charged.

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Under Section 23(1) of the *Moneylenders Act* (Cap. 188, 2010 Revised Edition), a court may (in the course of proceedings brought by a licensed moneylender for the recovery of a loan or enforcement of a contract for a loan or any guarantee or security given for a loan) re-open moneylending transactions where the rate of interest or late interest charged is deemed to be excessive and the transaction is unconscionable and substantially unfair. Section 23(4) of the Act extends the above-mentioned powers of the court to any proceedings for relief brought by a borrower, a surety or other person liable to repay a loan to a licensed moneylender, and Section 23(5) of the Act extends the same powers to the Official Assignee when determining whether the debt or liability claimed by a licensed moneylender against a borrower in his bankruptcy is proved, and its value.

The Rules of Court further provide that (unless otherwise agreed between parties) a default rate of interest applies on judgment debts and costs at the (presently) civil interest rate of 5.33% *per annum* (as directed by the Chief Justice with effect from 1 April 2007).

Insofar as consumer protection is concerned, the Consumer Protection (Fair Trading) Act (Cap. 52A) provides for the right of consumers to cancel certain regulated contracts (which generally refer to direct sales contracts, long-term holiday product contracts, time share or time share-related contracts) within prescribed cancellation periods of five days to up to six months in certain cases. The Act also provides certain remedies to consumers in relation to unfair practices of suppliers in relation to a consumer transaction, and "lemon law" rights for the repair, replacement, refund or reduction in price of defective products sold to a consumer.

1.3 Government Receivables. Where the receivables contract has been entered into with the government or a government agency, are there different requirements and laws that apply to the sale or collection of those receivables?

Under Section 2 of the *Government Contracts Act* (Cap. 118, 2013 Revised Edition), all contracts including contracts for the sale of goods and services entered into with the Singapore government or a government agency and reduced in writing, must be made in the name of the government and signed by a Minister or by any public officer duly authorised in writing by the Minister for Finance, either specially in any particular case, or generally for all contracts below a certain value in his Ministry or department.

Claims against the Singapore government or a government agency would be subject to the provisions of the *Government Contracts Act* (Cap. 118, 2013 Revised Edition). Insofar as civil claims against the Government or a government agency are concerned (including claims for receivables under a contract for the sale and purchase of goods and services), such claims will generally be treated the same as any similar claim made against a non-governmental entity.

2 Choice of Law – Receivables Contracts

2.1 No Law Specified. If the seller and the obligor do not specify a choice of law in their receivables contract, what are the main principles in your jurisdiction that will determine the governing law of the contract?

Where no choice of law has been specified in a receivables contract, the Singapore courts will firstly consider whether the intention of the parties with regard to the governing law can be inferred from the contract or the surrounding circumstances at the time when the contract was made.

Where a common intention of the parties to adopt a particular governing law cannot be inferred from the contract or the surrounding circumstances, the Singapore courts will have to determine the objective proper law applicable to the contract, being the law with the closest and most real connection with the transaction. In doing so, the Singapore courts will examine the connecting factors (including but not limited to where the parties are situated and where the obligations under the contract are to be performed) and arrive at what a reasonable man ought to have intended the governing law to be, had he thought about the matter at the time when the contract was made.

2.2 Base Case. If the seller and the obligor are both resident in your jurisdiction, and the transactions giving rise to the receivables and the payment of the receivables take place in your jurisdiction, and the seller and the obligor choose the law of your jurisdiction to govern the receivables contract, is there any reason why a court in your jurisdiction would not give effect to their choice of law?

Where the parties have expressly stipulated the contractual governing law to be Singapore law, the Singapore courts will generally uphold the same unless the choice of law was made in bad faith or is otherwise illegal or contrary to public policy in Singapore.

2.3 Freedom to Choose Foreign Law of Non-Resident Seller or Obligor. If the seller is resident in your jurisdiction but the obligor is not, or if the obligor is resident in your jurisdiction but the seller is not, and the seller and the obligor choose the foreign law of the obligor/seller to govern their receivables contract, will a court in your jurisdiction give effect to the choice of foreign law? Are there any limitations to the recognition of foreign law (such as public policy or mandatory principles of law) that would typically apply in commercial relationships such as that between the seller and the obligor under the receivables contract?

Where the parties have expressly stipulated the contractual governing law to be a foreign law other than Singapore law, the Singapore courts will generally uphold the same notwithstanding that one or more of the parties to the contract are resident in Singapore, unless the choice of foreign law was made in bad faith or is otherwise illegal or contrary to public policy in Singapore.

For example, the parties may be deemed to have acted in bad faith where the choice of foreign law was made deliberately for the purpose of evading the operation of Singapore law, which is intended to be mandatorily applicable in Singapore to the parties and/or the transaction. Section 27(2) of the *Unfair Contract Terms Act* (Cap. 396, 1994 Revised Edition) provides that the Act is to apply notwithstanding any contract term purporting to apply the law of some country outside Singapore where either (a) the term appears to the court, or the arbitrator or arbiter, to have been imposed wholly or mainly for the purpose of enabling the party imposing it to evade the operation of the Act, or (b) in the making of the contract, one of the parties dealt as consumer, and he was then habitually resident in Singapore, and the essential steps necessary for the making of the contract were taken there, whether by him or by others on his behalf.

Singapore has enacted the *Choice of Court Agreements Act 2016* (which came into effect on 1 October 2016) giving effect to the Hague Convention on Choice of Court Agreements, providing for the recognition and enforcement of choice of court agreements in relation to courts of contracting states.

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3 Choice of Law – Receivables Purchase Agreement

3.1 Base Case. Does your jurisdiction's law generally require the sale of receivables to be governed by the same law as the law governing the receivables themselves? If so, does that general rule apply irrespective of which law governs the receivables (i.e., your jurisdiction's laws or foreign laws)?

There is no requirement under Singapore law for a contract for the sale of receivables to be governed by the same law governing the receivables themselves. Parties are free to choose a contractual governing law which is different from the law governing the receivables, and the Singapore courts will generally uphold the choice of law of the parties unless the choice of law was made in bad faith or is otherwise illegal or contrary to public policy in Singapore. Notwithstanding the choice of contractual governing law, where the receivables are payable in Singapore, Singapore law may still apply mandatorily to certain issues including the assignability, perfection, enforceability and recovery of the receivables in Singapore.

3.2 Example 1: If (a) the seller and the obligor are located in your jurisdiction, (b) the receivable is governed by the law of your jurisdiction, (c) the seller sells the receivable to a purchaser located in a third country, (d) the seller and the purchaser choose the law of your jurisdiction to govern the receivables purchase agreement, and (e) the sale complies with the requirements of your jurisdiction, will a court in your jurisdiction recognise that sale as being effective against the seller, the obligor and other third parties (such as creditors or insolvency administrators of the seller and the obligor)?

In the absence of any qualifying information, the Singapore courts will generally recognise such a sale as being effective in Singapore as against the seller, the obligor and other third parties (such as creditors or insolvency administrators of the seller and the obligor) unless the choice of Singapore law to govern the receivables purchase agreement was made in bad faith or is otherwise illegal or contrary to public policy in Singapore.

The relevant laws in Singapore will also apply in the determination of the following issues: (a) the capacity of the parties located in Singapore to enter into or perform their respective obligations under the contract; (b) the validity and perfection of the sale of the receivables by the seller to the purchaser; and (c) the enforceability of the obligations of the parties in Singapore especially in the event of their insolvency.

3.3 Example 2: Assuming that the facts are the same as Example 1, but either the obligor or the purchaser or both are located outside your jurisdiction, will a court in your jurisdiction recognise that sale as being effective against the seller and other third parties (such as creditors or insolvency administrators of the seller), or must the foreign law requirements of the obligor's country or the purchaser's country (or both) be taken into account?

Similar to Example 1, the Singapore courts will generally recognise the sale as being effective in Singapore as against the seller and other third parties (such as creditors or insolvency administrators of the seller) located in Singapore unless the choice of Singapore law to govern the receivables purchase agreement was made in bad faith or is otherwise illegal or contrary to public policy in Singapore.

The relevant laws in Singapore will also apply in the determination of the following issues: (a) capacity of the parties located in Singapore to enter into or perform their respective obligations under the contract; (b) the validity and perfection of the sale of the receivables by the seller to the purchaser; and (c) the enforceability of the obligations of the parties in Singapore especially in the event of their insolvency.

The law governing the receivables will apply in determining questions relating to the assignability, perfection, enforceability and recovery of the receivables.

The foreign law requirements of the obligor's country or the purchaser's country may be relevant when determining the capacity of the obligor or purchaser to enter into or perform their respective obligations under the contract, and the enforceability of the obligations of the obligor or purchaser in their respective jurisdictions, especially where there are mandatory laws applicable in the event of their insolvency.

3.4 Example 3: If (a) the seller is located in your jurisdiction but the obligor is located in another country, (b) the receivable is governed by the law of the obligor's country, (c) the seller sells the receivable to a purchaser located in a third country, (d) the seller and the purchaser choose the law of the obligor's country to govern the receivables purchase agreement, and (e) the sale complies with the requirements of the obligor's country, will a court in your jurisdiction recognise that sale as being effective against the seller and other third parties (such as creditors or insolvency administrators of the seller) without the need to comply with your jurisdiction's own sale requirements?

Provided that it has been established that the sale is valid and enforceable under the foreign governing law of the contract and the Singapore courts have jurisdiction, the Singapore courts will generally recognise the sale as being effective as against the seller and other third parties (such as creditors or insolvency administrators of the seller) located in Singapore without the need to comply with the sale requirements under Singapore law, unless the choice of foreign governing law was made in bad faith or is otherwise illegal or contrary to public policy in Singapore.

The foreign law governing the receivables will apply in determining questions relating to the assignability, perfection, enforceability and recovery of the receivables.

The relevant laws in Singapore will, however, apply in the determination of the following issues: (a) capacity of the seller to enter into or perform its obligations under the contract; (b) the validity and perfection of the sale of the receivables by the seller to the purchaser located in a third country; and (c) the enforceability of the obligations of the parties in Singapore especially in the event of their insolvency.

3.5 Example 4: If (a) the obligor is located in your jurisdiction but the seller is located in another country, (b) the receivable is governed by the law of the seller's country, (c) the seller and the purchaser choose the law of the seller's country to govern the receivables purchase agreement, and (d) the sale complies with the requirements of the seller's country, will a court in your jurisdiction recognise that sale as being effective against the obligor and other third parties (such as creditors or insolvency administrators of the obligor) without the need to comply with your jurisdiction's own sale requirements?

Provided that it has been established that the sale is valid and enforceable under the foreign governing law of the contract and

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the Singapore courts have jurisdiction, the Singapore courts will generally recognise the sale as being effective as against the obligor and other third parties (such as creditors or insolvency administrators of the obligor) located in Singapore without the need to comply with the sale requirements under Singapore law, unless the choice of foreign governing law was made in bad faith or is otherwise illegal or contrary to public policy in Singapore.

The foreign law governing the receivables will apply in determining questions relating to the assignability, perfection, enforceability and recovery of the receivables.

The relevant laws in Singapore will, however, still apply in the determination of the following issues: (a) capacity of the obligor to enter into or perform its obligations under the contract; and (b) the enforceability of the obligations of the obligor in Singapore especially in the event of their insolvency.

3.6 Example 5: If (a) the seller is located in your jurisdiction (irrespective of the obligor's location), (b) the receivable is governed by the law of your jurisdiction, (c) the seller sells the receivable to a purchaser located in a third country, (d) the seller and the purchaser choose the law of the purchaser's country to govern the receivables purchase agreement, and (e) the sale complies with the requirements of the purchaser's country, will a court in your jurisdiction recognise that sale as being effective against the seller and other third parties (such as creditors or insolvency administrators of the seller, any obligor located in your jurisdiction and any third party creditor or insolvency administrator of any such obligor)?

Provided that it has been established that the sale is valid and enforceable under the foreign governing law of the contract and the Singapore courts have jurisdiction, the Singapore courts will generally recognise the sale as being effective as against the seller and other third parties (such as creditors or insolvency administrators of the seller, any obligor in Singapore and any third party creditor or insolvency administrator of any such obligor) in Singapore without the need to comply with the sale requirements under Singapore law, unless the choice of foreign governing law was made in bad faith or is otherwise illegal or contrary to public policy in Singapore.

However, as the governing law of the receivables, Singapore law will apply in determining questions relating to the assignability, perfection, enforceability and recovery of the receivables.

The relevant laws in Singapore will also apply in the determination of the following issues: (a) capacity of all parties located in Singapore to enter into or perform their respective obligations under the contract; (b) the validity and perfection of the sale of the receivables by the seller to the purchaser located in a third country; and (c) the enforceability of the obligations of all parties located in Singapore especially in the event of their insolvency.

4 Asset Sales

4.1 Sale Methods Generally. In your jurisdiction what are the customary methods for a seller to sell receivables to a purchaser? What is the customary terminology – is it called a sale, transfer, assignment or something else?

Under Singapore law, there is no specific terminology which must be used in order for a seller to sell receivables to a purchaser. However, a sale of receivables (whether current or future) usually takes the form of an absolute assignment from the seller to the purchaser in exchange for which the purchaser provides a consideration (which may be pecuniary or otherwise) to the seller. It is also not uncommon for a seller to assign to the purchaser receivables together with the contract rights conferred onto the seller under the underlying sale agreement to enforce the terms of the same against the obligor.

A legal assignment of receivables from a seller to a purchaser under Singapore law requires that:

(a) the underlying contract between the seller and the obligor under which the receivables are payable permits assignment of such receivables;

(b) the assignment must be absolute;

(c) the assignment must be in writing and signed by the assignor; and

(d) notice in writing of the assignment must be given to the obligor.

If any of the above requirements are not met, the assignment of receivables may still be recognised under Singapore law as an equitable assignment.

4.2 Perfection Generally. What formalities are required generally for perfecting a sale of receivables? Are there any additional or other formalities required for the sale of receivables to be perfected against any subsequent good faith purchasers for value of the same receivables from the seller?

The formalities required under Singapore law for perfecting a sale of receivables are as set out in question 4.1 above. A party who has received a legal assignment of the receivables will have priority over any subsequent good faith purchaser for value of the same receivables from the seller without the need to take any further steps.

A subsequent legal assignment of receivables in good faith, for value and without notice of a preceding equitable assignment over the same receivables will take priority over such a preceding equitable assignment, unless the subsequent purchaser was not *bona fide* or was aware at the time of the assignment to that subsequent purchaser of the earlier equitable interest in those receivables.

4.3 Perfection for Promissory Notes, etc. What additional or different requirements for sale and perfection apply to sales of promissory notes, mortgage loans, consumer loans or marketable debt securities?

Promissory notes can be sold and transferred by delivery (if it is a bearer instrument) or by delivery and endorsement (if it is a negotiable instrument). A promissory note is categorised as a "bill of exchange" under Section 3(1) of the *Bills of Exchange Act* (Cap. 23, 2004 Revised Edition) and is subject to the provisions thereunder. Under Section 21 of the Act, the holder of a bill is presumed to have received valid delivery of the same from the drawer, acceptor or indorser until the contrary is proven.

Loans including mortgage and consumer loans can be sold and transferred by way of assignment. The requirements for the legal assignment of loans are similar to that for a legal assignment of receivables as set out under question 4.1 above. Where the mortgage loan is secured by a mortgage over an asset (i) which requires that, or (ii) in respect of which, legal title is derived from registration with any authority or registry (for example, for immovable property and ships etc.), and which is also to be transferred together with the loan, registration of the transfer of the mortgage will need to be lodged with the appropriate authority or registry (e.g. Singapore Land Authority, Singapore Ship Registry etc.). In addition, where

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the mortgagor is a company, particulars of the mortgage will need to be lodged with the Accounting and Corporate Regulatory Authority of Singapore.

Marketable debt securities can be sold and transferred by giving instructions for this transfer from the account of the seller to the account of the purchaser in the clearing system.

4.4 Obligor Notification or Consent. Must the seller or the purchaser notify obligors of the sale of receivables in order for the sale to be effective against the obligors and/or creditors of the seller? Must the seller or the purchaser obtain the obligors' consent to the sale of receivables in order for the sale to be an effective sale against the obligors? Whether or not notice is required to perfect a sale, are there any benefits to giving notice – such as cutting off obligor set-off rights and other obligor defences?

A sale of receivables by the seller must be notified in writing to the obligor in order for the same to be effective as against the obligor. The sale of receivables is effective as against the creditors of the seller notwithstanding the absence of a written notification to the obligor.

While it is customary for the seller as the contracting party to give notice to the obligor, a purchaser may also notify the obligor if the seller fails to do so. The consent or acknowledgment of the obligor to the sale of the receivables is not required unless the transfer of the receivables is expressly prohibited in the contract between the seller and the obligor under which the receivables arise.

The giving of the written notice to the obligor of the sale of the receivables entitles the purchaser to certain benefits including:

1. ensuring that payment of the receivables is made to the purchaser instead of the seller, and that a failure of the obligor to do so subsequent to notification does not constitute a satisfactory discharge of the obligations of the obligor under the underlying contract;
2. "cutting off" the set-off rights of the obligor (other than those which have already accrued prior to the notice of assignment being given);
3. the purchaser will have the right to seek recourse directly against the obligor and its creditors for payment of the receivables without joining the seller; and
4. the purchaser will be able to claim priority to the receivables as against any subsequent good faith purchaser of the same receivables for value without notice of the prior sale.

4.5 Notice Mechanics. If notice is to be delivered to obligors, whether at the time of sale or later, are there any requirements regarding the form the notice must take or how it must be delivered? Is there any time limit beyond which notice is ineffective – for example, can a notice of sale be delivered after the sale, and can notice be delivered after insolvency proceedings have commenced against the obligor or the seller? Does the notice apply only to specific receivables or can it apply to any and all (including future) receivables? Are there any other limitations or considerations?

There is no prescribed form for the notice of sale and no specific method required for the delivery of the same. The only requirement is for the notice to be made in writing.

There is no limit beyond which the notice will be ineffective. The notice of sale can be delivered at any time subsequent to the sale including after insolvency proceedings have commenced against the obligor or the seller. However, the sale will be inchoate until the notice is given and the purchaser will lose his priority as against subsequent good faith purchasers of the same receivables for value without notice of the prior sale.

A notice of the sale of receivables can apply for specific receivables as well as any and all future receivables.

There may be limitations in the enforcement of the purchaser's rights to the receivables in a situation where the notice is given after insolvency proceedings have commenced against the obligor or the seller, since the assets of the seller and obligor will be subject to the insolvency regime.

4.6 Restrictions on Assignment – General Interpretation. Will a restriction in a receivables contract to the effect that "None of the [seller's] rights or obligations under this Agreement may be transferred or assigned without the consent of the [obligor]" be interpreted as prohibiting a transfer of receivables by the seller to the purchaser? Is the result the same if the restriction says "This Agreement may not be transferred or assigned by the [seller] without the consent of the [obligor]" (i.e., the restriction does not refer to rights or obligations)? Is the result the same if the restriction says "The obligations of the [seller] under this Agreement may not be transferred or assigned by the [seller] without the consent of the [obligor]" (i.e., the restriction does not refer to rights)?

A restriction in either of the first two examples is likely to be construed as prohibiting a transfer of receivables by the seller to the purchaser unless consent of the obligor has been obtained.

However, a restriction in a receivables contract to the effect that "The obligations of the [seller] under this Agreement may not be transferred or assigned by the [seller] without the consent of the [obligor]" is not likely to be construed as prohibiting the sale and transfer of receivables as the same would be treated as a right conferred on the seller and not an obligation. It is not uncommon for only the rights and benefits of the seller to be transferred to the purchaser but with the obligations to remain with the seller under the receivables contract.

4.7 Restrictions on Assignment; Liability to Obligor. If any of the restrictions in question 4.6 are binding, or if the receivables contract explicitly prohibits an assignment of receivables or "seller's rights" under the receivables contract, are such restrictions generally enforceable in your jurisdiction? Are there exceptions to this rule (e.g., for contracts between commercial entities)? If your jurisdiction recognises restrictions on sale or assignment of receivables and the seller nevertheless sells receivables to the purchaser, will either the seller or the purchaser be liable to the obligor for breach of contract or tort, or on any other basis?

If the receivables contract explicitly prohibits an assignment of receivables or the "seller's rights" under the receivables contract, whether in the wording set out in question 4.6 above or otherwise, the Singapore courts will generally enforce such restriction. As far as we are aware, there are no exceptions to this rule.

Where such restrictions are present but the seller nevertheless sells receivables to the purchaser, the seller (as party to the receivables contract) will be liable to the obligor for breach of contract. If the purchaser is also aware of the restriction but nonetheless procures or induces the seller to breach the receivables contract by the sale of the receivables, the purchaser may be made liable for inducing the breach of contract.

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4.8 Identification. Must the sale document specifically identify each of the receivables to be sold? If so, what specific information is required (e.g., obligor name, invoice number, invoice date, payment date, etc.)? Do the receivables being sold have to share objective characteristics? Alternatively, if the seller sells *all* of its receivables to the purchaser, is this sufficient identification of receivables? Finally, if the seller sells *all* of its receivables *other than* receivables owing by one or more specifically identified obligors, is this sufficient identification of receivables?

There is no requirement for any specific information to be provided so long as the sale document provides sufficient details to enable the receivables to be clearly identified at the time of the sale or as and when any future receivables sold under the receivables contract come into existence. This is a question of fact.

The sale of "all receivables", whether or not qualified by the exclusion of certain specifically identified receivables or not, may not always be sufficient identification of the receivables intended to be sold by the seller. In the absence of clarity on what constitutes "receivables" for the purposes of the sale, the use of the terms such as "all receivables" without an accompanying definition may give rise to disputes between the parties as to the scope of receivables to which the purchaser is entitled under the sale.

4.9 Recharacterisation Risk. If the parties describe their transaction in the relevant documents as an outright sale and explicitly state their intention that it be treated as an outright sale, will this description and statement of intent automatically be respected or is there a risk that the transaction could be characterised by a court as a loan with (or without) security? If recharacterisation risk exists, what characteristics of the transaction might prevent the transfer from being treated as an outright sale? Among other things, to what extent may the seller retain any of the following without jeopardising treatment as an outright sale: (a) credit risk; (b) interest rate risk; (c) control of collections of receivables; (d) a right of repurchase/redemption; (e) a right to the residual profits within the purchaser; or (f) any other term?

The Singapore courts would generally treat a transaction as being a genuine and outright sale where the relevant documents explicitly state the parties' intention as such. That being said, a court is entitled to and would examine the facts, circumstances and effect of the transaction notwithstanding its express provisions.

There is a risk of recharacterisation of the sale as a loan with (or without) security, where it appears to the Singapore courts from the express wording of the sale contract or the surrounding circumstances that the parties had an inappropriate or dishonest intention of entering into a sham transaction, whether for the purpose of circumventing any applicable laws or to disguise what is substantially a loan with (or without) security or otherwise.

A purported sale where the credit risks and interest rate risks remain with the seller may be construed as being inconsistent with the sale of the receivables to the purchaser. Granting the seller the right to repurchase or redeem the receivables are also indicative of the sale being intended more as a security rather than an outright sale. The retention by the seller of control over collection of the receivables or the right to residual profits within the purchaser may or may not, depending on the circumstances, contribute towards the sale being treated as a loan with (or without) security. The Singapore courts typically consider these factors along with any other facts which in their opinion may be relevant in inferring the true intention of the parties.

4.10 Continuous Sales of Receivables. Can the seller agree in an enforceable manner to continuous sales of receivables (i.e., sales of receivables as and when they arise)? Would such an agreement survive and continue to transfer receivables to the purchaser following the seller's insolvency?

A seller can agree in an enforceable manner to a continuous sale of receivables so long as the formalities required to perfect the sale are complied with. In order to ensure the purchaser's priority to the receivables, notice of the sale should be given to each and every obligor from whom the receivables sold are payable as and when the obligation arises.

Such an agreement can survive and continue to transfer receivables to the purchaser following the seller's insolvency, provided the obligor continues to be obliged to pay such receivables under its contract with the seller.

4.11 Future Receivables. Can the seller commit in an enforceable manner to sell receivables to the purchaser that come into existence after the date of the receivables purchase agreement (e.g., "future flow" securitisation)? If so, how must the sale of future receivables be structured to be valid and enforceable? Is there a distinction between future receivables that arise prior to *versus* after the seller's insolvency?

A seller can commit in an enforceable manner to sell receivables to the purchaser that come into existence after the date of the receivables purchase agreement, so long as the formalities required to perfect the sale have been complied with.

As with question 4.10 above, notice of the sale must be given to the obligor at the future date when the seller enters into the contract with the obligor under which the obligor's obligation to pay the receivable arises to ensure the purchaser's priority to the same.

Receivables that arise after the seller's insolvency is only legally assigned to the purchaser if notice has been given to the obligor of the sale and the receivables remain payable under the contract between the seller and the obligor notwithstanding the seller's insolvency. Until notice is given, the purchaser only has an equitable assignment of the receivables and is vulnerable to claims from intervening good faith purchasers or assignees of the same receivables for value without notice of the prior sale.

4.12 Related Security. Must any additional formalities be fulfilled in order for the related security to be transferred concurrently with the sale of receivables? If not all related security can be enforceably transferred, what methods are customarily adopted to provide the purchaser the benefits of such related security?

The formalities required in order to transfer related security concurrently with the sale of receivables depends on the nature of the security. Most types of security can be transferred by way of assignment or novation of the rights of the seller to the purchaser. Additional requirements may be in place for assignment of certain types of security. For example, if the security is a mortgage over Singapore registered land or a ship, the transfer of the same requires

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registration with the Singapore Land Authority (in the case of land) and the Singapore Ship Registry (in the case of a ship). If the obligor is a company registered in Singapore, particulars of the security and the secured party will need to be lodged with the Accounting and Corporate Regulatory Authority of Singapore if they fall within the categories set out under Section 131(3) of the *Companies Act* (Cap. 50, 2006 Revised Edition).

If there is any security which cannot be enforceably transferred, it is customary for the purchaser to require the seller to either hold the security on trust for the purchaser or to concurrently discharge the security in favour of the seller and create an identical security in favour of the purchaser. The former retains the priority of the purchaser to the security as from the time it was granted to the seller. The latter, while potentially leading the purchaser to lose priority in respect of the security, will give the purchaser a direct recourse against the obligor without joining the seller.

4.13 Set-Off; Liability to Obligor. Assuming that a receivables contract does not contain a provision whereby the obligor waives its right to set-off against amounts it owes to the seller, do the obligor's set-off rights terminate upon its receipt of notice of a sale? At any other time? If a receivables contract does not waive set-off but the obligor's set-off rights are terminated due to notice or some other action, will either the seller or the purchaser be liable to the obligor for damages caused by such termination?

Assuming that a receivables contract does not contain a provision whereby the obligor waives its right to set off against amounts it owes to the seller, the obligor's set-off rights terminate at the time the obligor receives notice of the sale and assignment of the receivables without prejudice to any pre-existing rights of set-off accrued prior to that time.

Notwithstanding the above, the seller may remain liable to the obligor for the damages resulting from the termination of the obligor's set-off rights after notice of the sale and assignment has been given.

4.14 Profit Extraction. What methods are typically used in your jurisdiction to extract residual profits from the purchaser?

In Singapore, where the sale is outright, the benefit of any residual profits resulting from the sale of the receivables to the purchaser is retained by the purchaser. Where the seller wishes to extract the residual profits from the purchaser, an agreement between the seller and the purchaser as to how and in what circumstances residual profit is paid back to the seller will need to be in place. However, such an arrangement may lead to the Singapore courts questioning whether in substance the transaction is a genuine sale or recharacterising the sale as a loan.

5 Security Issues

5.1 Back-up Security. Is it customary in your jurisdiction to take a "back-up" security interest over the seller's ownership interest in the receivables and the related security, in the event that an outright sale is deemed by a court (for whatever reason) not to have occurred and have been perfected (see question 4.9 above)?

While it is not uncommon for the sale of the receivables to be accompanied by the sale of all ancillary security granted by the obligor to secure its obligations under the receivables contract, it is not customary for "back up" security interests over the seller's ownership interest in the receivables to be taken in a transaction for sale of receivables. Consistent with a genuine sale, both the benefit and risk of non-payment of the receivables by the obligor is passed on to the purchaser. To secure such risks by taking "back up" security interests over the seller's ownership interest in the receivables may be construed as being more akin to a loan with security.

5.2 Seller Security. If it is customary to take back-up security, what are the formalities for the seller granting a security interest in receivables and related security under the laws of your jurisdiction, and for such security interest to be perfected?

We refer to our response under question 5.1 in respect of any security interest granted by the seller over the receivables.

In respect of any other security to be transferred to the purchaser together with the sale, please refer to our response under question 4.12.

5.3 Purchaser Security. If the purchaser grants security over all of its assets (including purchased receivables) in favour of the providers of its funding, what formalities must the purchaser comply with in your jurisdiction to grant and perfect a security interest in purchased receivables governed by the laws of your jurisdiction and the related security?

If the purchaser grants security over all of its assets (including purchased receivables) in favour of the providers of its funding, the purchaser will need to take such appropriate steps to create and perfect the security created over each asset secured depending on the nature of the asset.

Insofar as receivables are concerned, any assignment of the receivables by way of security (as opposed to a sale) will need to be perfected by giving notice of the assignment to the obligor from whom the receivables are or will be due.

Other securities such as a mortgage over registered land must be registered with the Singapore Land Authority. If the obligor is a company registered in Singapore, particulars of the security and the secured party will need to be lodged with the Accounting and Corporate Regulatory Authority of Singapore if they fall within the categories set out under Section 131(3) of the *Companies Act* (Cap. 50, 2006 Revised Edition) failing which the security will not be enforceable against the liquidators or other creditors of the obligor.

5.4 Recognition. If the purchaser grants a security interest in receivables governed by the laws of your jurisdiction, and that security interest is valid and perfected under the laws of the purchaser's jurisdiction, will the security be treated as valid and perfected in your jurisdiction or must additional steps be taken in your jurisdiction?

Where the receivables are governed by Singapore law, the questions as to the substantive validity of the security interest created or the enforceability of the security in Singapore will be determined under Singapore law.

However, questions of the purchaser's capacity to grant such security over the receivables or the procedural and formal requirements for the perfection of the security will be determined under the law of the purchaser's jurisdiction as the grantor of the security.

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5.5 Additional Formalities. What additional or different requirements apply to security interests in or connected to insurance policies, promissory notes, mortgage loans, consumer loans or marketable debt securities?

Security interest in insurance policies, mortgage loans and consumer loans are usually granted by way of an assignment. As with all other assignments, notification to the counterparty identifying the secured party and its interest is necessary in order to ensure that the secured party may seek recourse directly against the counterparty. We refer to our response in question 5.3 in relation to the requirements for creation of a mortgage over registered land connected to a mortgage loan.

It is customary for an assignment of an insurance policy to require the insurer to provide an endorsement to the policy recognising the secured party's interest and to name the secured party as a loss payee of the insurance policy. Depending on the nature of the insurance, a secured party may also require certain undertakings to be provided in respect of non-cancellation/information to be provided by insurers, underwriters or brokers.

A security interest in promissory notes is usually created by way of a pledge and requires the delivery of the promissory notes to the secured party so that the right to receive payment under the promissory note from its issuer is preserved.

A security interest over marketable debt securities held with the Central Depository (Pte) Limited is created by way of a statutory security by filing the requisite security forms.

If the grantor of the security is a company registered in Singapore, particulars of the security and the secured party will need to be lodged with the Accounting and Corporate Regulatory Authority of Singapore if they fall within the categories set out under Section 131(3) of the *Companies Act* (Cap. 50, 2006 Revised Edition) failing which the security will not be enforceable against the liquidators or other creditors of the grantor.

5.6 Trusts. Does your jurisdiction recognise trusts? If not, is there a mechanism whereby collections received by the seller in respect of sold receivables can be held or be deemed to be held separate and apart from the seller's own assets (so that they are not part of the seller's insolvency estate) until turned over to the purchaser?

Trusts are recognised under Singapore law.

5.7 Bank Accounts. Does your jurisdiction recognise escrow accounts? Can security be taken over a bank account located in your jurisdiction? If so, what is the typical method? Would courts in your jurisdiction recognise a foreign law grant of security (for example, an English law debenture) taken over a bank account located in your jurisdiction?

Singapore law recognises escrow accounts.

Security can be taken over a bank account located in Singapore by way of a charge over the account. This charge may require the consent of the bank with which the bank account is held in order for the same to have priority over the general bankers' lien which the bank may have over the account and the funds standing therein. In addition, a charge over a bank account and the funds standing therein would need to be registered under 131(3) of the *Companies Act* (Cap. 50, 2006 Revised Edition) failing which the charge will not be enforceable against the liquidator or other creditors of the account holder.

5.8 Enforcement over Bank Accounts. If security over a bank account is possible and the secured party enforces that security, does the secured party control all cash flowing into the bank account from enforcement forward until the secured party is repaid in full, or are there limitations? If there are limitations, what are they?

This depends on the provisions of the security instrument. Most such instruments typically provide that (upon enforcement) the secured party will be able to control all cash flowing into the bank account until the secured party is paid in full.

5.9 Use of Cash Bank Accounts. If security over a bank account is possible, can the owner of the account have access to the funds in the account prior to enforcement without affecting the security?

This depends on the provisions of the security instrument. If permitted under the terms of the charge, the account holder can be given the right to deal with the funds in the bank account prior to the enforcement of the charge without affecting the security. The same will be treated as a floating charge until such time when the security is enforced and the charge is crystallised.

6 Insolvency Laws

6.1 Stay of Action. If, after a sale of receivables that is otherwise perfected, the seller becomes subject to an insolvency proceeding, will your jurisdiction's insolvency laws automatically prohibit the purchaser from collecting, transferring or otherwise exercising ownership rights over the purchased receivables (a "stay of action")? If so, what generally is the length of that stay of action? Does the insolvency official have the ability to stay collection and enforcement actions until he determines that the sale is perfected? Would the answer be different if the purchaser is deemed to only be a secured party rather than the owner of the receivables?

If a sale of receivables is not perfected before the seller becomes subject to an insolvency proceeding, the purchaser would be able to continue to collect, transfer or otherwise exercise ownership rights over the purchased receivables as against the seller or its liquidator or creditors.

A sale which is not a genuine sale and which has been recharacterised as a loan with security by way of the sale of receivables will not be enforceable against the liquidator and other creditors of the seller unless lodgement of the security is made in accordance with Section 131 of the *Companies Act* (Cap. 50, 2006 Revised Edition).

In the case of a judicial management application made in respect of a Singapore company, upon the making of such an application no steps may be taken to enforce any charge or security or to repossess any goods or to commence any proceedings, execution or other legal process against the company or its property except with leave of court. When a judicial management order is made, any receiver shall vacate office and: (i) no execution or other legal process shall be commenced against them; and (ii) no steps taken to enforce security over or to repossess the company or its property except with the consent of the judicial manager or with leave of the court.

In the case of a winding-up application having been commenced, the company or any creditor or contributory may apply to court at any

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time before a winding-up order is made for a stay of proceedings pending against the company. Any disposition of the property of the company (including things in action) made after the commencement of the winding-up shall (unless the court otherwise orders) be void, and any attachment, sequestration, distress or execution shall be void. Upon the winding-up application being granted, no proceedings may be commenced or continued against the company without leave of court.

6.2 Insolvency Official's Powers. If there is no stay of action, under what circumstances, if any, does the insolvency official have the power to prohibit the purchaser's exercise of its ownership rights over the receivables (by means of injunction, stay order or other action)?

The insolvency official may be able to apply to the Singapore court for an injunction prohibiting the purchaser to exercise its ownership rights over the receivables, where it can be shown that the sale was not a genuine sale and is liable to be set aside as a transaction which is at an undervalue or which gives rise to an unfair preference in accordance with Sections 98 or 99 of the *Bankruptcy Act* (Cap. 20, 2009 Revised Edition) (as applied to a company pursuant to Sections 227T or 329 of the *Companies Act*).

The sale may be considered to be a transaction at an undervalue where:

1. the seller makes a gift to that purchaser or otherwise enters into a transaction with the purchaser on terms that provide for the seller to receive no consideration;
2. the seller enters into a transaction with the purchaser in consideration of marriage; or
3. the seller enters into a transaction with the purchaser for a consideration the value of which, in money or money's worth, is significantly less than the value, in money or money's worth, of the consideration provided by the purchaser.

On the other hand, the sale may be deemed to give rise to an undue preference where:

1. the purchaser is one of the seller's creditors or a surety or guarantor for any of the seller's debts or other liabilities; or
2. the seller does anything or suffers anything to be done which (in either case) has the effect of putting the purchaser in a position which, in the event of the seller's insolvency, will be better than the position he would have been in if that thing had not been done;

and the seller has given an unfair preference with a desire to produce in relation to the purchaser the effect referred to above. Such intention is presumed, unless the contrary is shown, where the purchaser is an associate of the seller.

6.3 Suspect Period (Clawback). Under what facts or circumstances could the insolvency official rescind or reverse transactions that took place during a "suspect" or "preference" period before the commencement of the seller's insolvency proceedings? What are the lengths of the "suspect" or "preference" periods in your jurisdiction for (a) transactions between unrelated parties, and (b) transactions between related parties? If the purchaser is majority-owned or controlled by the seller or an affiliate of the seller, does that render sales by the seller to the purchaser "related party transactions" for purposes of determining the length of the suspect period? If a parent company of the seller guarantee's the performance by the seller of its obligations under contracts with the purchaser, does that render sales by the seller to the purchaser "related party transactions" for purposes of determining the length of the suspect period?

With reference to our response under question 6.2 above, the clawback period is as set out in Section 100 of the *Bankruptcy Act* (Cap. 20, 2009 Revised Edition). In summary, the lengths of the suspect periods are as follows:

1. five years from the date of commencement of the insolvency proceedings in respect of any transactions at an undervalue;
2. six months from the date of commencement of the insolvency proceedings in respect of any undue preference granted to a creditor who is not an associate to the insolvent party; and
3. two years from the date of commencement of the insolvency proceedings in respect of any undue preference granted to a creditor who is an associate to the insolvent party.

The definition of what constitutes an "associate" of the insolvent party can be found under Section 101 of the *Bankruptcy Act* (Cap. 20, 2009 Revised Edition) which, for companies, generally include its directors and controllers, whether they are legal shareholders or otherwise.

6.4 Substantive Consolidation. Under what facts or circumstances, if any, could the insolvency official consolidate the assets and liabilities of the purchaser with those of the seller or its affiliates in the insolvency proceeding? If the purchaser is owned by the seller or by an affiliate of the seller, does that affect the consolidation analysis?

Under Singapore law, it is not common for assets and liabilities of separate legal entities to be consolidated even if there exists a parent-subsidiary relationship between the entities. As such, if the seller, as the shareholder of the purchaser, becomes subject to insolvency proceedings, the purchaser subsidiary can continue to exist without being affected.

The Singapore courts will only be willing to pierce the corporate veil and look to the assets of other affiliated companies of an insolvent company in limited circumstances such as fraud.

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6.5 Effect of Insolvency on Receivables Sales. If insolvency proceedings are commenced against the seller in your jurisdiction, what effect do those proceedings have on (a) sales of receivables that would otherwise occur after the commencement of such proceedings, or (b) on sales of receivables that only come into existence after the commencement of such proceedings?

With reference to our response under questions 4.10 and 4.11, the purchaser will still be entitled to receivables which would otherwise occur after the commencement of insolvency proceedings against the seller or that only come into existence after the commencement of such proceedings provided the obligor remains bound under the receivables contract to pay those receivables.

6.6 Effect of Limited Recourse Provisions. If a debtor's contract contains a limited recourse provision (see question 7.3 below), can the debtor nevertheless be declared insolvent on the grounds that it cannot pay its debts as they become due?

Where the debtor's contract contains a limited recourse provision, it is still possible for the debtor to be declared insolvent on the grounds that it cannot pay its debts as they become due given that this is essentially a question of fact.

7 Special Rules

7.1 Securitisation Law. Is there a special securitisation law (and/or special provisions in other laws) in your jurisdiction establishing a legal framework for securitisation transactions? If so, what are the basics? Is there a regulatory authority responsible for regulating securitisation transactions in your jurisdiction?

There is no statute in Singapore dealing with securitisation law. However, the Monetary Authority of Singapore (MAS), as the financial regulator, occasionally issues notices, circulars and guidelines which provides the framework for securitisation transactions.

MAS Notice No. 628 deals with securitisation and sets out under sections 3, 4 and the Annexes the mandatory requirements applicable to banks and under section 5 the non-mandatory guidelines on the responsibilities of banks in respect of a securitisation. MAS has also issued Notice No. 832 (with effect from 1 January 2018) which sets out similar requirements applicable to finance companies.

Income derived by an approved securitisation company resident in Singapore from asset securitisation transactions are exempt from income tax provided they meet the conditions under Section 13P of the *Income Tax Act* (Cap. 134, 2014 Revised Edition). The regulations dealing with this exemption are set out under the *Income Tax (Exemption of Income of Approved Securitisation Company) Regulations 2008*.

7.2 Securitisation Entities. Does your jurisdiction have laws specifically providing for establishment of special purpose entities for securitisation? If so, what does the law provide as to: (a) requirements for establishment and management of such an entity; (b) legal attributes and benefits of the entity; and (c) any specific requirements as to the status of directors or shareholders?

MAS Notice No. 628 referred to in question 7.1 deals with the establishment by banks of special purpose entities (SPE) to undertake asset securitisation transactions and the requirements imposed on the same.

Section 3.1 of the Notice requires that any bank acting as the programme sponsor, manager or an originator of a securitisation transaction comply with the separation requirements set out in Annex A and the disclosure requirements set out in Annex B.

Annex A provides that any bank acting as the programme sponsor, manager or an originator of a securitisation transaction shall not, in respect of the SPE used in securitisation:

1. in the case where the SPE is a corporation, own any share capital in the SPE, including ordinary or preference shares, or in the case where the SPE is a trust, own any share capital in the trustee or be a beneficiary of the SPE;
2. name the SPE in a manner as to imply any connection with the bank;
3. have any director, officer or employee on the board of the SPE unless:
   a. the board is made up of at least three members the majority of whom are independent directors; and
   b. the officer representing the bank does not have veto powers;
4. directly or indirectly control the SPE; or
5. provide implicit support or bear any of the recurring expenses of the securitisation.

Notwithstanding the above, a bank may hold preference shares issued pursuant to a securitisation provided:

1. the bank does not directly or indirectly control the SPE or the underlying exposures; and
2. MAS is satisfied that the preference shares have debt-like characteristics.

All transactions between the bank and the SPE are to be conducted at arm's length and on market terms and conditions.

7.3 Location and form of Securitisation Entities. Is it typical to establish the special purpose entity in your jurisdiction or offshore? If in your jurisdiction, what are the advantages to locating the special purpose entity in your jurisdiction? If offshore, where are special purpose entities typically located for securitisations in your jurisdiction? What are the forms that the special purpose entity would normally take in your jurisdiction and how would such entity usually be owned?

There is no customary practice of establishing SPEs in a particular jurisdiction – this will depend on the individual facts of the transaction.

A key advantage of locating the SPE in Singapore would be the ease of incorporation and doing business here:

1. Singapore's corporate tax rate is presently 17%, which is significantly lower than jurisdictions like Philippines (30%), Indonesia (25%) and Australia (27.5–30%), and on par with

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jurisdictions like Taiwan (17%) and Hong Kong (16.5%). The single tier taxation system and the absence of a tax on dividends and capital gains are also pull-factors;

2. a company can be incorporated in as little as one to three days due to Singapore's lack of red tape and efficiency, and a minimum paid-up capital requirement of just S$1.00; and
3. other considerations like our high connectivity and relative political and social stability also facilitate the conduct of business locally.

That said, the Monetary Authority of Singapore (MAS) has imposed several requirements for banks in Singapore that wish to establish special purpose entities (SPEs) to undertake asset securitisation transactions. The separation and disclosure requirements set out in MAS Notice No. 628 have been discussed in question 7.1 above, and MAS Notice No. 648 (dealing with covered bonds – debt securities issued by a bank or through an SPE that are collaterised against a cover pool of the bank's assets) provides for an encumbrance limit of 4%, which means that the percentage of the bank's assets that can be used in the cover pool is capped at 4%. If the bank should use an SPE to issue covered bonds or to hold the cover pool, the bank and the SPE shall be treated as a single entity for the purposes of the encumbrance limit. The encumbrance limit reduces the potential for covered bond issuance and stands in contrast to other jurisdictions with a higher encumbrance limit: Australia and South Korea both set theirs at 8%, while New Zealand has a limit of 10%.

SPEs that are incorporated in Singapore typically take the form of a limited liability company. The bank is not permitted to own any share capital in the SPE or to name it in such manner as to imply any connection with the bank – please refer to the full set of separation requirements set out in question 7.1 above for further limitations on the ownership of the SPE.

7.4 Limited-Recourse Clause. Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) limiting the recourse of parties to that agreement to the available assets of the relevant debtor, and providing that to the extent of any shortfall the debt of the relevant debtor is extinguished?

The Singapore courts generally recognise and give great weight to the freedom of parties to a contract. A Singapore court is likely to give effect to a contractual provision in an agreement (whether or not governed by Singapore law) limiting the recourse of parties to that agreement to the available assets of the relevant debtor, and providing that to the extent of any shortfall the debt of the relevant debtor is extinguished (so long as such clauses are valid, binding and enforceable under the governing law of the agreement).

7.5 Non-Petition Clause. Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) prohibiting the parties from: (a) taking legal action against the purchaser or another person; or (b) commencing an insolvency proceeding against the purchaser or another person?

The Singapore courts generally recognise and give great weight to the freedom of parties to a contract. That being said, the position under Singapore law is not entirely clear as to whether a contractual provision in an agreement (whether or not governed by Singapore law) prohibits the parties from: (a) taking legal action against the purchaser or another person; or (b) commencing an insolvency proceeding against the purchaser or another person.

Provided a court does not find such a provision objectionable on the grounds that it is contrary to public policy or is intended to evade the application of any law which would have otherwise been mandatorily applicable to the transaction, the Singapore courts will likely give effect to the clause (so long as such clauses are valid, binding and enforceable under the governing law of the agreement).

7.6 Priority of Payments "Waterfall". Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) distributing payments to parties in a certain order specified in the contract?

A Singapore court is likely to give effect to a contractual provision in an agreement (whether or not governed by Singapore law) distributing payments to parties in a certain order specified in the contract so long as such clauses are valid, binding and enforceable under the governing law of the agreement but subject to any statutory priorities which may arise in the event of the insolvency of the debtor under the provisions of the *Companies Act* (Cap. 50, 2006 Revised Edition).

7.7 Independent Director. Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) or a provision in a party's organisational documents prohibiting the directors from taking specified actions (including commencing an insolvency proceeding) without the affirmative vote of an independent director?

A Singapore court is generally likely to give effect to a contractual provision in an agreement (whether or not governed by Singapore law) or a provision in a party's organisational documents prohibiting the directors from taking specified actions (including commencing an insolvency proceeding) without the affirmative vote of an independent director so long as such restriction is valid, binding and enforceable under the governing law of the agreement and the law of the place of incorporation of the organisation.

That being said, the *Companies Act* (Cap. 50, 2006 Revised Edition) confers on directors of a Singapore company certain statutory rights, powers and duties which cannot be excluded by way of contract and notwithstanding the constitution of the company, and a director has fiduciary duties to the company under common law. This is to ensure the proper regulation of the company. A restriction or limitation which is construed as an impermissible fetter on a director's discretion wholesale may also not be recognised.

7.8 Location of Purchaser. Is it typical to establish the purchaser in your jurisdiction or offshore? If in your jurisdiction, what are the advantages to locating the purchaser in your jurisdiction? If offshore, where are purchasers typically located for securitisations in your jurisdiction?

There is no customary practice to establish a purchaser in Singapore or elsewhere. Whether this should be done will ultimately depend on the individual facts of the transaction including where the seller and obligor are located, where the receivables are payable and whether there are any income or other tax implications.

As set out in question 7.1, Singapore law provides income tax exemptions for income derived by an approved securitisation company resident in Singapore from asset securitisation transactions. Depending on the location of the obligor and where the receivables

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are to be paid, the purchaser may also wish to consider whether the receivables may be subject to withholding tax or other value added or similar tax in the jurisdiction from which the receivables are to be paid.

8 Regulatory Issues

8.1 Required Authorisations, etc. Assuming that the purchaser does no other business in your jurisdiction, will its purchase and ownership or its collection and enforcement of receivables result in its being required to qualify to do business or to obtain any licence or its being subject to regulation as a financial institution in your jurisdiction? Does the answer to the preceding question change if the purchaser does business with more than one seller in your jurisdiction?

If the purchaser is a foreign company, it will not be regarded as carrying on business in Singapore simply because it:

1. secures or collects any of its debts or enforces its rights in regard to any securities relating to such debts; or
2. conducts an isolated transaction that is completed within a period of 31 days, but not being one of a number of similar transactions repeated from time to time.

The above is set out in Section 366 of the *Companies Act* (Cap. 50, 2006 Revised Edition). As such, if the purchaser does no other business in Singapore, it is unlikely to be regarded as carrying on business in Singapore simply by reason of its purchase and ownership or its collection and enforcement of receivables.

If the purchaser does business with more than one seller in Singapore, there is a higher likelihood of the purchaser being found to be "carrying on business" in Singapore. The factors which will be considered include:

1. whether the purchaser has established a place of business in Singapore;
2. whether the purchaser has employed any employee or agent in connection with the business;
3. whether the purchaser has raised any loans or finance;
4. whether the purchaser has undertaken any collection of information or soliciting of business; and
5. trading within Singapore.

8.2 Servicing. Does the seller require any licences, etc., in order to continue to enforce and collect receivables following their sale to the purchaser, including to appear before a court? Does a third-party replacement servicer require any licences, etc., in order to enforce and collect sold receivables?

The seller does not require any licence or permit to enforce and collect receivables. However, under Section 33 of the *Legal Profession Act* (Cap. 161, 2009 Revised Edition), should the seller wish to sue out any writ, summons or process, or commence, continue or defend legal proceedings in the Singapore courts, he will need to engage an advocate and solicitor of the Supreme Court of Singapore. In addition, a seller cannot, for any fee, gain or reward, directly or indirectly draw or prepare any document or instrument relating to any movable property (including receivables) or immovable property or to any legal proceeding. A seller also cannot, on behalf of a claimant, write, publish or send a letter or notice threatening legal proceedings other than a letter or notice that the matter will be handed to a solicitor for legal proceedings.

8.3 Data Protection. Does your jurisdiction have laws restricting the use or dissemination of data about or provided by obligors? If so, do these laws apply only to consumer obligors or also to enterprises?

The *Personal Data Protection Act 2012* (No. 26 of 2012) (PDPA) governs the collection, use and disclosure of personal data by organisations. "Personal data" refers to data, whether true or not, about an individual who can be identified from that data or from that data and other information to which the organisation has or is likely to have access. The PDPA applies to all companies and entities, but generally does not apply to individuals acting in a personal or domestic basis, or any public agency. In addition, sensitive or confidential information and trade secrets may be contractually protected or secured by way of non-disclosure agreements and confidentiality agreements.

Certain other Acts provide for confidentiality of information, for example, banking secrecy in relation to the customer information of a bank under the *Banking Act*.

Certain information is publicly available for a fee and these include information about companies such as the particulars of its officers and shareholders, the company's registered address and share capital.

8.4 Consumer Protection. If the obligors are consumers, will the purchaser (including a bank acting as purchaser) be required to comply with any consumer protection law of your jurisdiction? Briefly, what is required?

There are two main statutes relating to consumer protection in Singapore which the purchaser will be required to comply with. The *Unfair Contract Terms Act* (Cap. 396, 1994 Revised Edition) imposes limits on the extent to which civil liability for breach of contract, or for negligence or other breach of duty, can be avoided by means of contract terms and otherwise. The *Consumer Protection (Fair Trading) Act* (Cap. 52A, 2009 Revised Edition) protects consumers against unfair practices and gives consumers additional rights in respect of goods that do not conform to contract. Under these statutes, the purchaser shall not, among other things:

1. by reference to its standard terms of business exclude its own liability for breaches of terms;
2. take advantage of a consumer by including in an agreement terms or conditions that are harsh, oppressive or excessively one-sided so as to be unconscionable; and
3. do or say anything, or omit to do or say anything, if as a result a consumer might reasonably be deceived or misled.

If the bank acts as purchaser, there may be additional requirements pertaining to transactions with customers which the bank has to comply with under the *Banking Act* (Cap. 19, 2008 Revised Edition) and the Monetary Authority of Singapore's notices, guidelines and codes of conduct.

8.5 Currency Restrictions. Does your jurisdiction have laws restricting the exchange of your jurisdiction's currency for other currencies or the making of payments in your jurisdiction's currency to persons outside the country?

Singapore does not currently impose any currency restrictions and has not imposed any currency restrictions since 1 June 1978 when the Monetary Authority of Singapore suspended the *Exchange Control Act* (Cap. 99).

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8.6 Risk Retention. Does your jurisdiction have laws or regulations relating to "risk retention"? How are securitisation transactions in your jurisdiction usually structured to satisfy those risk retention requirements?

Regulations relating to risk retention and management in securitisation transactions are set out in Part VII Division 6 of Notice 637 issued by the Monetary Authority of Singapore.

There is no fixed way in which securitisation transactions are to be structured. Instead, Reporting Banks (as defined in Notice 637) are to determine the capital treatment of a securitisation on the basis of its economic substance rather than its legal form in order to determine their regulatory obligations on exposures.

8.7 Regulatory Developments. Have there been any regulatory developments in your jurisdiction which are likely to have a material impact on securitisation transactions in your jurisdiction?

The Monetary Authority of Singapore proposed amendments to MAS Notice 637 in January 2017 to implement requirements for Singapore-incorporated banks in respect of securitisation transactions that are consistent with the standards issued by the Basel Committee on Banking Supervision. These amendments were taken in and implemented by way of MAS Notice 637 (Amendment No. 2) 2017 issued on 29 November 2017 and MAS Notice 637 (Amendment No. 3) 2017 issued on 28 December 2017 in respect of revised Part VII Division 6 of MAS Notice 637, and which took effect from 1 January 2018.

9 Taxation

9.1 Withholding Taxes. Will any part of payments on receivables by the obligors to the seller or the purchaser be subject to withholding taxes in your jurisdiction? Does the answer depend on the nature of the receivables, whether they bear interest, their term to maturity, or where the seller or the purchaser is located? In the case of a sale of trade receivables at a discount, is there a risk that the discount will be recharacterised in whole or in part as interest? In the case of a sale of trade receivables where a portion of the purchase price is payable upon collection of the receivable, is there a risk that the deferred purchase price will be recharacterised in whole or in part as interest? If withholding taxes might apply, what are the typical methods for eliminating or reducing withholding taxes?

Withholding tax is applicable in Singapore in respect of certain types of payments (including interest on overdue trade accounts or credit terms) paid from a resident to a non-resident. The prevailing rate of withholding tax on interest payments is 15%.

Accordingly, while the payment of receivables arising from the sale of goods and services in itself is not subject to withholding tax, interest charged on the same will be.

In the event that the sale of trade receivables is at an artificial discount, or part of the purchase price is artificially payable upon collection of the receivable, there is a risk that such discount or deferred purchase price will be recharacterised in whole or in part as interest which will be wholly subject to withholding tax.

9.2 Seller Tax Accounting. Does your jurisdiction require that a specific accounting policy is adopted for tax purposes by the seller or purchaser in the context of a securitisation?

There is no requirement under Singapore law for any specific accounting policy to be adopted for tax purposes by the seller or the purchaser in the context of a securitisation.

9.3 Stamp Duty, etc. Does your jurisdiction impose stamp duty or other transfer or documentary taxes on sales of receivables?

Singapore law does not impose any stamp duty or other documentary taxes on the sale of receivables.

9.4 Value Added Taxes. Does your jurisdiction impose value added tax, sales tax or other similar taxes on sales of goods or services, on sales of receivables or on fees for collection agent services?

In respect of the sale of goods and services, a Goods and Services Tax (GST) which is akin to a value added tax or sales tax in other jurisdictions is imposed subject to the provisions and exemptions under the *Goods and Services Tax Act* (Cap. 117A, 2005 Revised Edition). The rate of GST applicable depends on the nature of the goods and services supplied. Certain supplies (including the supply of goods and services in relation to ships and aircrafts) are zero-rated. For most other supplies (including the provision of services as a collection agent in Singapore), the standard GST rate of 7% is applicable.

A sale of receivables is exempt from the GST under the Fourth Schedule of the GST Act.

9.5 Purchaser Liability. If the seller is required to pay value-added tax, stamp duty or other taxes upon the sale of receivables (or on the sale of goods or services that give rise to the receivables) and the seller does not pay, then will the taxing authority be able to make claims for the unpaid tax against the purchaser or against the sold receivables or collections?

We refer to our response under question 9.4 above in relation to the sale of receivables – no GST, stamp duty or other transfer taxes are payable on the sale of receivables.

If GST is payable on the sale of goods and services under which the receivable is paid and the seller fails to file its GST returns or pay the GST due on the same within one month after the end of the accounting period of the GST return, the Inland Revenue Authority of Singapore (IRAS) may, among other things, impose a late submission and a late payment penalty on the seller. IRAS may also appoint a party (in respect of whom any monies or debt is payable to a seller) as a tax agent of IRAS and direct that such party pay over to IRAS such sums as may be directed amounting to tax due and unpaid to IRAS from the seller.

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9.6 Doing Business. Assuming that the purchaser conducts no other business in your jurisdiction, would the purchaser's purchase of the receivables, its appointment of the seller as its servicer and collection agent, or its enforcement of the receivables against the obligors, make it liable to tax in your jurisdiction?

The purchaser may be liable to tax in Singapore if it purchases receivables from obligors in Singapore, or if it appoints the seller as its servicer and collection agent for obligors in Singapore, or if it enforces the receivables against obligors in Singapore.

9.7 Taxable Income. If a purchaser located in your jurisdiction receives debt relief as the result of a limited recourse clause (see question 7.3 above), is that debt relief liable to tax in your jurisdiction?

Bad debt relief is available if the supplier has paid GST on the supply of goods, in respect of which the consideration thereof is later written off in whole or in part. In order to claim for relief, a period of 12 months starting from the date of supply must have elapsed or the debtor has become insolvent during the 12-month period.

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Spain

Héctor Bros

Cuatrecasas

Elisenda Baldrís

1 Receivables Contracts

1.1 Formalities. In order to create an enforceable debt obligation of the obligor to the seller: (a) is it necessary that the sales of goods or services are evidenced by a formal receivables contract; (b) are invoices alone sufficient; and (c) can a binding contract arise as a result of the behaviour of the parties?

Although there are certain exceptions, in general, contracts in Spain do not need to be evidenced by a formal contract. This means that verbal contracts are valid and enforceable in Spain. Having said that, there are certain exceptions; for example, contracts entered into with consumers need to be in written form. In addition, under certain circumstances and pursuant to the relevant legislation, contracts need to be executed before a Public Notary.

That said, the sale of goods or services does not necessarily need to be evidenced by a formal receivables contract. In this regard, invoices may be sufficient to evidence the existence of the contractual relationship. On the other hand, a receivable contract may be deemed to exist as a result of the behaviour of the parties, since tacit contracts are generally accepted in Spain.

However, written form is advisable in order to evidence the conditions under such verbal and tacit contracts.

1.2 Consumer Protections. Do your jurisdiction's laws: (a) limit rates of interest on consumer credit, loans or other kinds of receivables; (b) provide a statutory right to interest on late payments; (c) permit consumers to cancel receivables for a specified period of time; or (d) provide other noteworthy rights to consumers with respect to receivables owing by them?

Limits on interest rates. Spanish laws do not set out specific limits on interest rates other than a general criterion on which interest has to be deemed usurious.

The Act of 23 July, 1908, on invalidity of usurious loan agreements, establishes that any loan setting out an interest rate significantly higher than what is considered to be the normal money-rate of interest and manifestly disproportionate according to the circumstances of the case, will be invalid. The interpretation and application of this general parameter has recently been analysed in a Supreme Court decision in relation to consumer-related transactions. The court considered that in order to determine whether the interest rate was disproportionate, the annual percentage rate should be compared against the "normal money-rate". The latter refers to the statistics published by the Bank of Spain on interest rates applied by credit institutions in Spain. This decision provides objective criteria in determining whether an interest rate shall be deemed usurious.

Limits on late interest. The Spanish Civil Code states that the interest on late payments accrues when the non-defaulting creditor requires the other party to fulfil its payment obligation. The interest on late payments is: (i) compensation for damages and prejudices, and consists of an amount agreed by the parties; or (ii) (in the absence of an agreement) equal to the legal interest rate set out by the government for that year. Notwithstanding the foregoing, there are several limitations to the principle of party autonomy. For example, the Decree of February 8, 1946, approving the new mortgage act ("**Mortgage Act**"), sets out that the late interest on loans for the acquisition of the main residence cannot exceed three times the legal interest. On the other hand, Act 16/2011, of June 24, on Consumer Credit Agreements ("**Act 16/2011**") sets out that the maximum applicable rate for all current account overdrafts is two-and-a-half times the legal interest.

Furthermore, in light of a decision of the Supreme Court (April 22, 2015), the interest on late payments of consumers' personal loans shall be deemed usurious if it increases by more than two percentage points with respect to the interest rate agreed in the loan.

Pursuant to the most recent case law of the Court of Justice of the European Union, in case a national court considers that a particular provision under a contract shall be deemed null and void, the judge may not construe that provision by applying the default rule under the relevant national law. As an exception, in case such clause is required for the existence of the contract, which would not be the case with respect to late interest, the national court may apply the national default rule.

Mortgage loans. Additionally, regarding mortgage loans, the Spanish legislator has introduced urgent measures to protect low-income debtors by means of the Royal Decree-Law 6/2012, of March 9, as amended by Act 25/2015, July 28 ("**RDL 6/2012**"). The most relevant provisions are as follows:

(1) A voluntary accession to a good practice code by credit institutions and professional lenders. The accession to such code involves the mandatory application of a number of provisions for the adhered institutions. At present, almost all Spanish credit institutions have adhered to such good practice code.

(2) A limitation to the maximum default interest applicable to any residential mortgage loans granted before the entry into force of RDL 6/2012 regarding low-income debtors. The cap

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interest is equal to the ordinary interest agreed in the loan plus 2%. This measure applies irrespective of whether the relevant institution has acceded to the above-mentioned good practice code.

(3) An indefinite derogation of any provision in loans and credit agreements limiting the effect of a reduction in the floating interest rate (i.e., the so-called "*cláusulas suelo*").

On the other hand, there has been much controversy on clauses affecting consumers. In this respect, Spanish courts are declaring some clauses within mortgage loan agreements, for abusive, null and void (e.g., certain clauses setting forth a floor instrument, the so-called "*cláusulas suelo*", and clauses regarding assumption of costs).

In particular, in May 2013, the Spanish Supreme Court ruled that in certain cases banks should refund the amounts perceived under those clauses from that date on. However, by the end of 2016, the European Court of Justice established that banks should refund the total amount received by way of application of those clauses over the whole life of the mortgage loan (i.e., not only for the time elapsed since May 2013).

Lastly, Act 1/2013, 14 May, on measures to protect mortgage debtors, debt restructuring and social rent ("**Act 1/2013**") establishes limitations on mortgage loans that finance the acquisition of a primary residence ("*vivienda habitual*"). This act prohibits the compounding of late interest (except under certain circumstances) and limits the cap on default interest up to three times the legal interest rate. These limitations apply to any Spanish residential mortgage loan (unlike the regime set forth in RDL 6/2012), regardless of whether the loan was granted before or after Act 1/2013 entered into force.

Aside from the general Spanish legislation on debtors' protection, some Spanish regions (e.g., Catalonia, the Basque Country and Andalusia), acting in their legislative capacity in the area of consumer affairs, have enacted their own regional law in consumer protection. For example, by virtue of Act 24/2015, of July 29 on urgent measures to face emergency in relation to housing and energy poverty, in Catalonia, a debtor under a mortgage loan may be released satisfying the assignee the assignment price. On the other hand, in October 1, 2013, the Andalusian Parliament enacted Law 4/2013 on measures to secure the proper fulfilment of the social function of housing. Under the Andalusian act, should the debtors be under special social emergency circumstances, houses may be expropriated right after the mortgage foreclosure has taken place.

Withdrawal right. Generally, Royal-Legislative Decree 1/2007, of 16 November, approving the consolidated text of the Act for the Protection of Consumers and Users, sets out that when provided under the applicable sectoral legislation, or when agreed between the parties, consumers shall be entitled to cancel an agreement (and the receivables thereunder). This right of withdrawal is in force for 14 calendar days after the delivery of the goods or the execution of the agreement, as the case may be, unless a different cancellation period is set out in the applicable sectoral legislation. This term period will apply as long as the seller or provider of the services has duly informed the obligor-consumer of the existence and characteristics of the withdrawal right. Otherwise, the term shall be 14 working days since the seller has duly fulfilled this information obligation, up to a maximum of 12 months from the delivery of the goods or execution of the service agreement.

Borrowers under consumer financing agreements and customers of financial services following distance marketing activities by the financial institution, are entitled to very similar withdrawal rights. Under Act 16/2011, borrowers may trigger the agreement without giving any reason within a period of 14 calendar days as from the later of the following dates: (i) the execution date of the credit agreement; and (ii) the date of delivery of certain financial information and terms by the lender to the consumer. The creditor shall not be entitled to any compensation other than payment of the principal and interest accrued from drawdown of the credit until full repayment.

1.3 Government Receivables. Where the receivables contract has been entered into with the government or a government agency, are there different requirements and laws that apply to the sale or collection of those receivables?

Sale. Except otherwise provided in the contract conditions ("*pliegos de condiciones*"), the transfer of the receivables will be enforceable against the Spanish governmental entity or company within the Spanish public sector once notice of transfer of such receivables has been duly served (with proof of delivery) upon the relevant debtor, in accordance with the Spanish Civil Code, the Spanish Commercial Code, the Royal Legislative Decree 3/2011 on Contracts of the Public Sector and the Act 9/2017, of November 8, 2017, regulating Contracts of Public Sector by means of which the European Directives 2014/23/EU and Directive 2014/24/EU, in force since March 9, 2018. This includes the need of servicing a notice to the debtor (i.e., to the government entity or public company) in order to ensure that the assignment is enforceable *vis-à-vis* the same. Additionally, in case of assignment of future receivables, the consent of the government or government agency is required.

Collection. The collection of receivables arising from a contract signed with a governmental authority may be subject to the specific regulation applicable to such governmental entity. This regulation may provide for mandatory provisions of law, the application of which cannot be waived by agreement. This regulation may include:

(1) the legal right of the governmental entity to claim for itself or for some of its assets (i.e., the assets allocated to, or used in, a public service) immunity from suit, execution, attachment or other legal processes in Spain;

(2) the obligation of the governmental entity not to exceed certain limitations; and

(3) the need for the payment of the receivable to be included in the relevant budget law of that entity for the relevant year.

2 Choice of Law – Receivables Contracts

2.1 No Law Specified. If the seller and the obligor do not specify a choice of law in their receivables contract, what are the main principles in your jurisdiction that will determine the governing law of the contract?

Regulation (EC) No.593/2008 ("**Rome I Regulation**"), which directly applies in Spain, sets out the law applicable to contractual obligations on civil and business matters.

Pursuant to article 3 of the Rome I Regulation, parties may choose the applicable law according to the principle of party autonomy. In the case that there is no explicit choice, the applicable law will be determined in light of the circumstances.

In the case of a sale of goods or the provision of services, when there is no explicit choice, the applicable law is the one of the country where the seller or the provider of services has its habitual residence. However, in case there is another country that is manifestly more closely connected, the law of the most closely connected country shall be deemed applicable instead.

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Notwithstanding the above, there are certain exceptions under the Rome I Regulation to those general rules, in particular when there is a contractual asymmetry. For example, the applicable law will be the one of the country of habitual residence of the obligor in the case: (i) the obligor qualifies as a consumer; and (ii) the seller or provider of services performs the contract's business activities in the country of the consumer, or directs its business activities to that country.

2.2 Base Case. If the seller and the obligor are both resident in your jurisdiction, and the transactions giving rise to the receivables and the payment of the receivables take place in your jurisdiction, and the seller and the obligor choose the law of your jurisdiction to govern the receivables contract, is there any reason why a court in your jurisdiction would not give effect to their choice of law?

No, there is no reason why a court in Spain would not give effect to that choice of law.

2.3 Freedom to Choose Foreign Law of Non-Resident Seller or Obligor. If the seller is resident in your jurisdiction but the obligor is not, or if the obligor is resident in your jurisdiction but the seller is not, and the seller and the obligor choose the foreign law of the obligor/seller to govern their receivables contract, will a court in your jurisdiction give effect to the choice of foreign law? Are there any limitations to the recognition of foreign law (such as public policy or mandatory principles of law) that would typically apply in commercial relationships such as that between the seller and the obligor under the receivables contract?

Yes; since, pursuant to article 3 of the Rome I Regulation, the parties may choose a law not linked to the factual circumstances of the contract. In addition, the Rome I Regulation gives the possibility to choose different laws for different parts of the contract, and the possibility to change the applicable law during the contract's validity, if this does not affect third parties' rights.

However, according to article 9 of the Rome I Regulation, the principle of party autonomy has certain restrictions, such as restrictions due to the overriding mandatory provisions. In this regard, the Court of Justice of the European Union (C-369/96 and C-135/15) has deemed 'overriding mandatory provisions' as the rules that a country considers essential for safeguarding its public interest.

In this regard, the Spanish courts may refuse the application of the chosen law if the relevant provisions are clearly contrary to Spanish public policy. In this situation, the relevant Spanish court would apply the relevant provisions under Spanish law instead of those applicable under the chosen foreign law.

On the other hand, the principle of party autonomy may be limited when the chosen law is the law of a non-EU Member State and all the relevant elements in the contract are located in one or more Member States. In this regard, the choice of the parties regarding the applicable law may not prejudice the application of mandatory provisions under EU law.

That said, this restriction would not normally apply in case of commercial relationships such as those between two professionals (the seller and the obligor under a receivables contract), taking into account the regular content of those agreements.

3 Choice of Law – Receivables Purchase Agreement

3.1 Base Case. Does your jurisdiction's law generally require the sale of receivables to be governed by the same law as the law governing the receivables themselves? If so, does that general rule apply irrespective of which law governs the receivables (i.e., your jurisdiction's laws or foreign laws)?

The sale of receivables does not need to be governed by the law applying to the receivable itself. The principle of party autonomy would apply herein pursuant to articles 3 and 14 of the Rome I Regulation, which allow the seller and the purchaser to apply to the sale contract a different law than that applying to the receivable itself.

In these cases, pursuant to article 14.2 of the Rome I Regulation, the law governing the receivable would rule: (i) its assignability; (ii) the relationship between the assignee and the obligor; (iii) the conditions under which the assignment or subrogation may be invoked against the obligor; and (iv) whether the obligations of the obligor have been discharged.

However, the freedom of choice is subject to certain limits:

(1) *All the relevant elements are located in another country*. In case all the relevant elements of the situation are located in a country different from the one of the chosen law, the choice of the parties may not prejudice the application of mandatory provisions of that other country. Accordingly, the mandatory provisions of that other country will prevail over the parties' choice.

(2) *Payment instruments*. In case of transfer of negotiable instruments executed and delivered in Spain, such as bills of exchange and promissory notes, the law applying to the rights and obligations of the parties shall be Spanish law.

(3) *Security interests*. In case the obligations under the transferred receivables are secured by a security interest granted over an asset located in Spain (such as a real estate mortgage or a pledge over the shares of a Spanish company), mandatory Spanish law provisions shall apply on the perfection and enforceability of that security interest. Those provisions will govern, additionally, the assignment of that security interest for the benefit of third parties.

3.2 Example 1: If (a) the seller and the obligor are located in your jurisdiction, (b) the receivable is governed by the law of your jurisdiction, (c) the seller sells the receivable to a purchaser located in a third country, (d) the seller and the purchaser choose the law of your jurisdiction to govern the receivables purchase agreement, and (e) the sale complies with the requirements of your jurisdiction, will a court in your jurisdiction recognise that sale as being effective against the seller, the obligor and other third parties (such as creditors or insolvency administrators of the seller and the obligor)?

According to article 3 of the Rome I Regulation, in principle the chosen law (i.e., Spanish law) would apply to both the sale agreement and to the relationship with the obligor. Accordingly, provided that the transfer agreement complies with the requirements under Spanish law, as mentioned below in questions 4.1 and 4.4, a Spanish court would recognise that sale as being effective against the seller and the obligor.

Regarding the effects against other third parties (such as creditors or insolvency administrators of the seller and the obligor), the Rome I Regulation does not solve this question. In this regard, article 27 of the mentioned regulation sets out that the Commission shall

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submit a report on the question of the effectiveness of an assignment or subrogation of a claim against third parties and the priority of the assigned or subrogated claim over a right of another person, together, if appropriate, by a proposal to amend the Rome I Regulation. To this day, the envisaged report has not been submitted and, accordingly, the effectiveness of the assignment of the receivable against third parties and the priority of the assigned claim, is still a controversial issue.

However, in Spain there is a reference to this issue on the local law governing financial guarantees, i.e., Royal-Legislative Decree 5/2005 ("**RDL 5/2005**"), dated 11 March, which transposes, amongst others, the Directive 2002/47/EC of the European Parliament and of the Council of 6 June, 2002 on financial collateral arrangements. This law expressly sets out that where credit rights constitute financial collateral, the effectiveness of such assignment against the obligor and against third parties shall be determined in light of the law governing the assigned receivable.

The majority of scholars consider that the solution adopted with respect to financial collateral in RDL 5/2005 should apply in other cases where a receivable is assigned by way of security or pledge, and by extension, to any kind of ordinary assignment.

In conclusion, it is likely that under the circumstances described in this question, a Spanish court would recognise the sale as being effective *vis-à-vis* third parties if the sale complies with the relevant requirements under Spanish law.

3.3 Example 2: Assuming that the facts are the same as Example 1, but either the obligor or the purchaser or both are located outside your jurisdiction, will a court in your jurisdiction recognise that sale as being effective against the seller and other third parties (such as creditors or insolvency administrators of the seller), or must the foreign law requirements of the obligor's country or the purchaser's country (or both) be taken into account?

Please refer to questions 3.1 and 3.2 above on the law applicable to the assignment agreement, the conditions under which the assignment may be invoked against the obligor and the effectiveness of such assignment against third parties. Accordingly, a Spanish court would recognise that sale as being effective against the seller and the obligor in the case the legal requirements under Spanish law, as described in questions 4.1 and 4.4 below, are met.

Notwithstanding the above, in the case where the obligor was not located in Spain, since Rome I Regulation has not been further developed, in order to ensure recognition in the country where the obligor is located it would be advisable to comply, additionally, with the requirements that the law of that country imposes for the enforceability of the transfer *vis-à-vis* third parties.

3.4 Example 3: If (a) the seller is located in your jurisdiction but the obligor is located in another country, (b) the receivable is governed by the law of the obligor's country, (c) the seller sells the receivable to a purchaser located in a third country, (d) the seller and the purchaser choose the law of the obligor's country to govern the receivables purchase agreement, and (e) the sale complies with the requirements of the obligor's country, will a court in your jurisdiction recognise that sale as being effective against the seller and other third parties (such as creditors or insolvency administrators of the seller) without the need to comply with your jurisdiction's own sale requirements?

Please refer to questions 3.1 and 3.2 above on the law applicable to the assignment agreement, to the conditions under which the assignment may be invoked against the obligor and the effectiveness of such assignment against third parties.

Provided that the transfer agreement complies with the chosen applicable law (the law of the country where the obligor is located), a Spanish court would recognise that sale as being effective against the seller. However, that foreign law should be evidenced to the Spanish court.

In addition, since the seller is located in Spain, it would be advisable, in order to ensure recognition by Spanish courts, to comply not only with the requirements under the law of the obligor's country but also with the requirements that Spanish law imposes regarding the enforceability of the transfer *vis-à-vis* third parties.

3.5 Example 4: If (a) the obligor is located in your jurisdiction but the seller is located in another country, (b) the receivable is governed by the law of the seller's country, (c) the seller and the purchaser choose the law of the seller's country to govern the receivables purchase agreement, and (d) the sale complies with the requirements of the seller's country, will a court in your jurisdiction recognise that sale as being effective against the obligor and other third parties (such as creditors or insolvency administrators of the obligor) without the need to comply with your jurisdiction's own sale requirements?

Please refer to questions 3.1 and 3.2 above on the law applicable to the assignment agreement, to the conditions under which the assignment may be invoked against the obligor and the effectiveness of such assignment against third parties.

Provided that the transfer agreement complies with the chosen applicable law (the law of the country where the seller is located), a Spanish court would recognise that sale as being effective against the obligor. However, that foreign law should be evidenced to the Spanish court.

In addition, since the obligor is located in Spain, it would be advisable, in order to ensure recognition by Spanish courts, to comply not only with the requirements under the law of the seller's country but also with the requirements that Spanish law imposes regarding the enforceability of the transfer *vis-à-vis* third parties.

3.6 Example 5: If (a) the seller is located in your jurisdiction (irrespective of the obligor's location), (b) the receivable is governed by the law of your jurisdiction, (c) the seller sells the receivable to a purchaser located in a third country, (d) the seller and the purchaser choose the law of the purchaser's country to govern the receivables purchase agreement, and (e) the sale complies with the requirements of the purchaser's country, will a court in your jurisdiction recognise that sale as being effective against the seller and other third parties (such as creditors or insolvency administrators of the seller, any obligor located in your jurisdiction and any third party creditor or insolvency administrator of any such obligor)?

Please refer to questions 3.1 and 3.2 above on the law applicable to the assignment agreement, to the conditions under which the assignment may be invoked against the obligor and the effectiveness of such assignment against third parties.

Provided that the transfer agreement complies with the chosen applicable law (the law of the country where the purchaser is

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located), a Spanish court would recognise that sale as being effective against the seller. However, that foreign law should be evidenced to the Spanish court.

In addition, since the seller is located in Spain and the receivable is governed by Spanish law, it would be advisable, in order to ensure recognition by Spanish courts, to comply not only with the requirements under the law of the purchaser's country but also with the requirements that Spanish law imposes regarding the enforceability of the transfer *vis-à-vis* third parties.

4 Asset Sales

4.1 Sale Methods Generally. In your jurisdiction what are the customary methods for a seller to sell receivables to a purchaser? What is the customary terminology – is it called a sale, transfer, assignment or something else?

There are three different methods to assign receivables under Spanish law, depending on the characteristics of the assignor and the assignee:

(1) ordinary assignment pursuant to the Commercial Code and the Civil Code;

(2) assignment pursuant to the Third Additional Provision of Act 1/1999, of 5 January, on Capital-Risk Entities ("**Act 1/1999**"); and

(3) assignment to a Spanish securitisation fund ("**FT**") or to a "*Fondo de Activos Bancarios*" ("**FAB**").

Each of these assignments needs to be executed in an agreement setting out the transfer of the relevant receivables.

(1) **Ordinary assignments**. Pursuant to the Commercial Code and the Civil Code, the seller remains liable *vis-à-vis* the purchaser for the existence of the receivable and validity of the legal title of the seller. On the other hand, unless so expressly agreed in the assignment agreement between the parties, the purchaser will not have recourse against the seller, i.e., the seller will not be liable before the purchaser in case of insolvency of the obligor.

(2) **Special assignments**. As set out in question 6.3 below, assignments under the Third Additional Provision of Act 1/1999 shall be subject to a special regime for insolvency purposes. Although these assignments are normally structured as an ordinary assignment, in order to benefit from the mentioned special regime, assignments must meet the following conditions:

   (a) the assignor shall be an entrepreneur and the assigned receivables shall arise from its business activity;

   (b) the assignee shall either be a credit institution or a securitisation fund;

   (c) the receivables to be assigned shall either (i) exist on the date that the assignment agreement is executed, or (ii) arise from the business activity of the assignor within a maximum period of one year from the execution date of the assignment agreement (or, alternatively, the assignment agreement shall clearly identify the obligors under those receivables);

   (d) the assignee shall pay to the assignor the agreed price either upon closing or on a deferred basis, excluding the cost of the services provided; and

   (e) in the case the assignment agreement does not envisage the recourse against the seller in case of insolvency of the obligor, it must be evidenced that the purchaser has paid to the seller, in whole or in part, the agreed price prior to the maturity of the assigned receivables.

(3) **FTs**. The Act 5/2015 on promoting business financing ("**Act 5/2015**") sets out the regime for Spanish securitisation funds, that is, special purpose vehicles which may purchase a portfolio of receivables and issue asset-backed notes. This kind of assignment is subject to a special tax and insolvency regime, set out in question 4.3 below. Spanish securitisation funds need the prior authorisation of and registration with the Spanish National Stock Market Commission (the "**CNMV**").

   Pursuant to article 17 of Act 5/2015, the assignment of receivables to FTs is subject to the following requirements:

   (a) the assignor shall have audited annual accounts for the last two financial years;

   (b) the assignor shall set out in its annual reports the assignment transactions (whether regarding present or future receivables) it has performed;

   (c) assignment transactions shall be executed in a written document; and

   (d) any new incorporation of assets shall be informed to the CNMV.

(4) **FABs**. Act 9/2012, November 14, on restructuring and resolutions of credit institutions ("**Act 9/2012**") sets out the regime of the FABs. FABs are special purpose vehicles, lacking legal personality, subject to a privileged legal and tax regime whose assets were originally bank assets. The assignor of the assets to be purchased by an FAB is exclusively the Company for the Management of Assets Proceeding from Restructuring of the Banking System ("**SAREB**"). SAREB is a partially government-owned company. In the context of the nationalisation and restructuring of certain Spanish credit institutions, SAREB purchased the problematic assets originated by those institutions. SAREB may divest such assets by transferring them to the mentioned special purpose vehicles (i.e., the FABs).

4.2 Perfection Generally. What formalities are required generally for perfecting a sale of receivables? Are there any additional or other formalities required for the sale of receivables to be perfected against any subsequent good faith purchasers for value of the same receivables from the seller?

There are no formalities generally required for perfecting a sale of receivables, regardless of whether it is an ordinary assignment, a special assignment or an assignment to a FT (except for those set forth in question 4.1 above) or to a FAB. Notwithstanding the foregoing, written form is standard in Spain.

Additionally, pursuant to article 1280 of the Spanish Civil Code, in case the receivables are executed in a public document, any party may legally require the other party to execute the assignment of those receivables by means of a public document. However, in case that assignment is not executed in a public document, it will not affect the validity of the assignment between the parties.

In addition, pursuant to article 1526 of the Spanish Civil Code, the assignment of a receivable will be fully effective *vis-à-vis* third parties upon the date deemed certain. In this regard, articles 1218 and 1227 of the Spanish Civil Code set out that the execution date of a document will be deemed certain in case such document is executed before a Spanish Public Notary.

4.3 Perfection for Promissory Notes, etc. What additional or different requirements for sale and perfection apply to sales of promissory notes, mortgage loans, consumer loans or marketable debt securities?

Payment Instruments. In Spain, payment instruments ("**Payment**

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Instruments") include bills of exchange ("*letras de cambio*"), promissory notes ("*pagarés*") and other analogous instruments ("*efectos cambiarios*") included in Act 19/1985, July 16, of Exchange and Cheques ("**Act 19/1985**"), which regulates the issuance and transfer of such instruments. In general, Payment Instruments may be transferred by means of:

(1) ***Endorsement***. Endorsement ("*endoso*") is the expression that Act 19/1985 uses when referring to a written statement issued by the seller in the title itself. A Payment Instrument may be endorsed by placing the signature of the endorser on the back of the Payment Instrument and delivering it to the endorsee. The payee is the first possible endorser. The endorsee becomes the holder of the instrument and, thus, it has the right to claim payment of the Payment Instrument at the maturity date. An endorsee also has the right to endorse the instrument again. In the endorsement, the endorser may set out a particular endorsee or endorse the Payment Instrument in blank (i.e., by a mere signature on the back of the Payment Instrument).

(2) ***Ordinary assignment***. The maker may include in a Payment Instrument the words "not to order", or an equivalent expression such as "not transferable" or "not negotiable". In this case, the instrument cannot be endorsed and it can only be transferred by ordinary assignment in a different contract by means of which the credit is transferred.

Although there is no risk of losing the fast-track proceedings that Spanish civil procedural law foresees to claim for the credit included in the Payment Instrument (i.e., "*procedimiento cambiario*"), transferring through endorsement brings more advantages than the ordinary assignment (no personal causes of opposition may be alleged by the debtor/to initiate an action the endorsee only needs the Payment Instrument to justify itself as a legitimate creditor).

Regarding the tax regime of the transfer of these "*efectos cambiarios*", please see question 9.3 below.

Mortgage loans. The requirements for the sale of a mortgage loan include the execution of the transfer in a public document executed before a Spanish Public Notary and the registration of that transfer within the relevant Land Registry. In case the sale of the mortgage loan does not meet the two mentioned conditions, the transfer of the loan will not be effective *vis-à-vis* third parties and the enforcement of the mortgage may be seriously hindered. On the other hand, in case the loan was secured by a mortgage or a non-possessory pledge over movable assets, the previous conditions (public document and registration) would apply as well. However, in such case the registration shall be within the Movable Assets Registry ("*Registro de Bienes Muebles*") instead of the Land Registry.

On the tax side, the transfer of a mortgage loan (either over a property or over a movable asset) in a public deed ("*escritura*") accrues stamp duty tax. Unlike mortgage loans, loans secured by non-possessory pledges may be transferred by means of a notarial document (i.e., the "*póliza*") before a Spanish Public Notary, different from the public deed. The execution of that agreement in a "*póliza*" would avoid the accrual of stamp duty tax.

In case mortgage loans are granted by a credit institution and secured by a mortgage over a property, Act 2/1981 on the Mortgage Market Act ("**Act 2/1981**") sets out a privileged regime for the transfer of the credit rights arising from those mortgage loans through the issuance of a special type of transferable security. In this regard, Act 2/1981 and its development regulation (Royal Decree 716/2009, of April 24, "**RD 716/2009**") set out the requirements mortgage loans shall meet so that the credit rights thereunder may be transferred by the issuance and subscription of those special transferable securities, the mortgage participations ("*participaciones hipotecarias*"), hereinafter, "**PH**". Mortgage loans may be transferred by means of the issuance by credit institutions and the subscription of PH if, among others, the following requirements are met:

- Loans shall be secured with first-ranking mortgages.
- The value of the secured loans shall not exceed 60% of the appraised value of the property (or 80% in case of residential property).
- Mortgaged properties need to be insured against damages.
- Loans cannot be secured by assets expressly excluded according to RD 716/2009; this includes loans secured with mortgages granted over usufruct rights, administrative concessions and surface rights.

Pursuant to the Fourth Additional Provision of Act 5/2015, in case the mortgage loans do not meet all the requirements set forth in Chapter II to Act 2/1981 and of RD 716/2009, the credit rights may be transferred by means of a different type of transferable security: mortgage transfer certificates ("*certificados de transmission de hipoteca*"), hereinafter, "**CTH**".

Both PH and CTH are subject to a privileged regime for registration, tax and insolvency purposes:

- *Registration with the land registry*. In case subscription and possession of PH and CTH are restricted to professional investors (such as FTs), pursuant to paragraph two of article 29.1 of RD 716/2009, the issuance of PH or CTH shall not be subject to a marginal notation with the Land Registry. However, in any event, the issuer of the PH and CTH remains the lender on record in the Land Registry, even though the holder of the CTH or the PH becomes the beneficial owner of those mortgage loans.
- *Tax regime*. The issuance and transfer of PH and CTH is a transaction exempt from stamp duty tax.
- *Insolvency regime*. In the case of insolvency of the credit institution, the issuance of the PH or the CTH would only be subject to the challenge by the insolvency authorities if they prove fraud.

Pursuant to Act 2/1981 and RD 716/2009, the issuer of the PH or CTH is required to provide custody and administration of the mortgage loans. Accordingly, the issuer shall transfer to the holders of the PH and the CTH any amounts received regarding the underlying loans, in the amount corresponding to the percentage of its participation in the mortgage loan. In the event the obligor fails to pay the mortgage loan, the holder of the PH or CTH has certain powers as holder of the credit rights regarding the underlying mortgage loan. For example, the holder of the PH or the CTH, as the case may be, may compel the issuer to commence foreclosure on the mortgage and has a subsidiary power to enforce the mortgage in the amount corresponding to the percentage of its participation in the mortgage loan in the case the issuer of the PH or CTH does not commence the procedure within 60 days.

Consumer loans. There are no particular requirements for sale and perfection regarding consumer loans. However, pursuant to article 31 of Act 16/2011, in the case the original lender ceases to be the servicer under that loan, the assignment shall be notified to the consumer.

Debt securities. Debt securities represented in book-entry form shall be transmitted by accounts transfer in addition to the execution of the transfer agreement.

Debt securities represented in registered form shall be transferred either through endorsement of the relevant title or by means of an ordinary assignment.

Debt securities represented in bearer form shall be transmitted by physical delivery of the title.

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4.4 Obligor Notification or Consent. Must the seller or the purchaser notify obligors of the sale of receivables in order for the sale to be effective against the obligors and/or creditors of the seller? Must the seller or the purchaser obtain the obligors' consent to the sale of receivables in order for the sale to be an effective sale against the obligors? Whether or not notice is required to perfect a sale, are there any benefits to giving notice – such as cutting off obligor set-off rights and other obligor defences?

Consent of the obligor is not required to perfect a valid transfer of a receivable, unless otherwise agreed by the parties of the original contract. Where consent is required in accordance with the original contract, it is unclear under Spanish law whether a transfer made without such consent remains valid and enforceable against the obligor (who will have a legal action against the original creditor for breaching the contractual provision requiring the consent), or whether the lack of consent renders the transfer invalid and, therefore, not enforceable against the obligor. Case law has not provided a consistent answer to this question.

Notwithstanding the foregoing, the consent of the government (or the government agency, as the case may be) is required in case of transfer of future government receivables.

Notification is not required to perform a valid transfer of a receivable. However, an obligor will be deemed to have validly discharged its obligations under a receivable if it has made the payment to the original creditor before it is notified, or it becomes aware, of the transfer. An obligor may also set off its obligations under a receivable against the original creditor until it is notified of the transfer. In both cases, the new creditor would not have any legal action against the obligor to claim the amount paid (or set-off) and would only be entitled to claim from the original creditor the amount received by it from the obligor, or (as applicable) the amount set off. Therefore, serving a notice of the transfer to the obligor is advisable and enhances the legal position of the new creditor.

4.5 Notice Mechanics. If notice is to be delivered to obligors, whether at the time of sale or later, are there any requirements regarding the form the notice must take or how it must be delivered? Is there any time limit beyond which notice is ineffective – for example, can a notice of sale be delivered after the sale, and can notice be delivered after insolvency proceedings have commenced against the obligor or the seller? Does the notice apply only to specific receivables or can it apply to any and all (including future) receivables? Are there any other limitations or considerations?

Spanish law does not require any specific formality in connection with servicing a notice of transfer. However, as a matter of practice, it is advisable to serve notices in a manner that helps to evidence in court the date of the notice, the date of reception of the notice by the obligor and the consent of the same. Standard procedures for such purpose include requesting a Notary Public to serve the notice or via a special mail system "burofax", which is offered by "Correos" (the Spanish Mail).

A notice may be served after the sale and no limitations apply. The parties may notify the transfer of all future receivables arising from an existing contract.

If the obligors are individuals and there is a transfer of personal data, the transfer and the notice must comply with the requirements under the Organic Act 15/1999, of December 13, on Personal Data Protection (basically, properly informing the affected individuals about their data being included in a new file as well as about other relevant circumstances – such as those responsible for that file, purposes of use, mention to the rights of access, amendment, cancellation and opposition, etc.). Although these obligations will still be in force after May 25, 2018 (when the new General Data Protection Regulation will be fully applicable), it should be noted that the Spanish Parliament is currently drafting a new piece of legislation that may modify those obligations.

Finally, it is under debate whether certain regional regulations on residential mortgage lending require, in those cases, the delivery of a notice to the borrowers under those loans.

4.6 Restrictions on Assignment – General Interpretation. Will a restriction in a receivables contract to the effect that "None of the [seller's] rights or obligations under this Agreement may be transferred or assigned without the consent of the [obligor]" be interpreted as prohibiting a transfer of receivables by the seller to the purchaser? Is the result the same if the restriction says "This Agreement may not be transferred or assigned by the [seller] without the consent of the [obligor]" (i.e., the restriction does not refer to rights or obligations)? Is the result the same if the restriction says "The obligations of the [seller] under this Agreement may not be transferred or assigned by the [seller] without the consent of the [obligor]" (i.e., the restriction does not refer to rights)?

The effect of the three proposed clauses above would not be the same.

The first and the second clause may be interpreted as prohibiting the transfer of receivables under the Agreement as both would prevent the transfer of both rights and obligations.

On the other hand, the third clause would only prevent the transfer of obligations, but not rights. Hence, in accordance with the third clause, no consent of the obligor would be required to transfer receivables under the contract.

4.7 Restrictions on Assignment; Liability to Obligor. If any of the restrictions in question 4.6 are binding, or if the receivables contract explicitly prohibits an assignment of receivables or "seller's rights" under the receivables contract, are such restrictions generally enforceable in your jurisdiction? Are there exceptions to this rule (e.g., for contracts between commercial entities)? If your jurisdiction recognises restrictions on sale or assignment of receivables and the seller nevertheless sells receivables to the purchaser, will either the seller or the purchaser be liable to the obligor for breach of contract or tort, or on any other basis?

Please refer to the answer in question 4.4 above.

4.8 Identification. Must the sale document specifically identify each of the receivables to be sold? If so, what specific information is required (e.g., obligor name, invoice number, invoice date, payment date, etc.)? Do the receivables being sold have to share objective characteristics? Alternatively, if the seller sells *all* of its receivables to the purchaser, is this sufficient identification of receivables? Finally, if the seller sells *all* of its receivables *other than* receivables owing by one or more specifically identified obligors, is this sufficient identification of receivables?

Spanish law requires that an asset to be transferred (in this case, a receivable) is properly identified in the sale and purchase contract.

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However, no specific rule determines how a receivable should be identified. Hence, the identification of the receivable in the sale and purchase contract could be made in any manner that allows a court to be able to properly identify the receivable. As a matter of practice, receivables are normally identified by, at least, the name of the obligor and the invoice number or contract details.

The receivables to be sold do not have to share the same characteristics.

Where the receivables are to be transferred to a FT, Act 5/2015 sets out that a description of the assets to be transferred, setting out their characteristics, shall be provided. That said, Act 5/2015 does not specify which data would be deemed sufficient in order to comply with those requirements. On the other hand, article 22 of Act 5/2015 sets out that, amongst the requirements for the incorporation of an FT, an audit report on the securitised assets (issued either by the managing company or by an external audit) shall be provided. Pursuant to that requirement, in principle, a detailed description on the receivables (containing data such as outstanding balances, yields, financial flows, collection terms, amortisation schedule and maturity dates) should be provided.

In the case of a transfer of credit rights under a mortgage loan to the FT through the issuance and subscription of PH and CTH, RD 716/2009 sets out that the title representing those transferable securities shall set out, for each mortgage loan, the initial loan principal, its maturity date, its amortisation schedule, its financial flows, its maturity date and the data of its registration in the relevant Land Registry. Accordingly, in the case of a transfer of credit rights pursuant to the issuance of PH and CTH, the mentioned data will be required.

Finally, regarding the common objective characteristics regarding the receivables to be sold to an FT, unlike the former regulation applicable to those funds, Act 5/2015 does not provide that the assets must be of a homogeneous nature.

A global sale of all of its receivables (or of all of its receivables, but some) are generally valid under Spanish law, although the actual transfer of the ownership of a receivable arising from a contract entered after the date of the sale may require an additional action (please see the answer to question 4.10 below).

4.9 Recharacterisation Risk. If the parties describe their transaction in the relevant documents as an outright sale and explicitly state their intention that it be treated as an outright sale, will this description and statement of intent automatically be respected or is there a risk that the transaction could be characterised by a court as a loan with (or without) security? If recharacterisation risk exists, what characteristics of the transaction might prevent the transfer from being treated as an outright sale? Among other things, to what extent may the seller retain any of the following without jeopardising treatment as an outright sale: (a) credit risk; (b) interest rate risk; (c) control of collections of receivables; (d) a right of repurchase/redemption; (e) a right to the residual profits within the purchaser; or (f) any other term?

A court may enquire into the economic characteristics of the transaction. Although the description of a contract as an outright sale could help a court to construe the contract as such, Spanish courts are not bound by the legal name given by the parties to a contract; instead, they could analyse the underlying real economics and nature of the transaction. Following that analysis, they may determine a different characterisation of the contract.

In performing that analysis, the court may take into consideration not only a single clause or declaration of the parties made in the contract, but also all the other provisions of that contract, the terms and conditions of ancillary contracts and even the behaviour of the parties when performing their obligations or legal rights under the same.

Credit risk and payment of the purchase price. Normally, without taking into account whether the transfer is agreed on a recourse or non-recourse basis, the courts have generally respected the true sale treatment of the transaction given by the parties as long as the purchase price is paid by the purchaser in full or in substantial part. Failure to advance any significant funds may lead to the courts considering that the risk attached to the receivables has not been transferred and, accordingly, the transfer may not be deemed a true sale. Equally, subjecting the obligation to pay the purchase price to the existence of sufficient collections may endanger the true sale objective.

Control of collections. The fact that the assignor and the assignee agree that the former retains collection responsibilities does not alter the above views. For example, in the case of a transfer of receivables to an FT, the assignor may retain collection responsibilities, either:

(1) under legal compulsion, in the case of credit rights arising under mortgage loans, since RD 716/2009 sets out that the issuer of the PH and CTH shall retain collection responsibilities; or

(2) by agreement between the assignor and the FT, in case credit rights are not assigned by way of the PH and CTH. Under those circumstances, although pursuant to Act 5/2015 the managing company remains legally responsible for the collection tasks, it is customary that the assignor and the FT enter into a servicing agreement by virtue of which the assignor undertakes to perform such collection duties.

Credit risk and right of repurchase. In addition, regarding the FT, the former regulation expressly prohibited the assignor to grant any guarantee to the FT or underwrite the transaction. In contrast, Act 5/2015 expressly envisages in article 17 that the assignor shall specify in its annual reports all the deals entered into in order to underwrite that particular assignment transaction. Accordingly, the new regulation applicable to the FT permits more flexibility on the retention on credit risk and on the existence of a right of repurchase.

Interest rate risk. Regarding the interest rate risk, the assignor and the FT may enter into a hedging agreement by which the assignor retains that risk and, in exchange, the FT undertakes to satisfy to the assignor either a fixed interest rate or a floating rate different from that applicable to the credit rights assigned to the FT.

That said, under Spanish account and capital adequacy rules, the characterisation of the transfer transaction may not coincide with the legal characterisation or the effect of that particular transaction. In this regard, certain elements of the transaction (such as the credit risk retention) shall be taken into account in order to determine whether, under account and capital adequacy rules, the transaction may be considered a true sale and, therefore, whether a sale of receivables can benefit from off-balance sheet treatment.

Residual profits. Pursuant to article 1528 of the Civil Code, the assignment of the main obligation entails the transfer of any right ancillary to it, such as security interests. Accordingly, as long as residual profits are ancillary rights under the receivable (for example, interests due because of late payment under the receivable, or any compensation due by the obligor), they would be assigned, by operation of law, to the purchaser. However, it is possible for the parties to agree otherwise, i.e., the purchaser may retain any residual profit to the seller, without necessarily jeopardising the treatment as an outright sale.

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4.10 Continuous Sales of Receivables. Can the seller agree in an enforceable manner to continuous sales of receivables (i.e., sales of receivables as and when they arise)? Would such an agreement survive and continue to transfer receivables to the purchaser following the seller's insolvency?

Yes, the parties may agree to continuous sales of receivables. However, under Spanish law, it is arguable whether it is possible to effectively transfer legal title over a future receivable until the relevant receivable actually exists, or the contract from which the receivable will arise has been entered into. Therefore, such continuous sale would constitute a binding obligation of the parties to enter into future sales, but it may not have the legal effect of transferring the legal title of the future receivable unless an actual transfer is also signed after the future receivable (or the underlying contract) has come into existence (please see the answer to question 4.11 below for further reference). A continuous sale may survive a declaration of insolvency, but it will be subject to several restrictions in case of insolvency of the seller.

4.11 Future Receivables. Can the seller commit in an enforceable manner to sell receivables to the purchaser that come into existence after the date of the receivables purchase agreement (e.g., "future flow" securitisation)? If so, how must the sale of future receivables be structured to be valid and enforceable? Is there a distinction between future receivables that arise prior to *versus* after the seller's insolvency?

Ordinary assignment. As mentioned in the answer to question 4.10, a contract of sale of future receivables creates valid obligations binding upon the parties. However, the actual transfer of the title over future receivables may not occur until the future receivable, or the contract underlying to the future receivable, actually exists. Some scholars, as well as case law, have argued that the purchaser may be considered as the owner of a future receivable *ab initio*, as soon as the future receivable comes into life, and hence that the future receivable already arises as an asset of the purchaser and not as an asset of the seller. As a matter of practice, it is advisable to agree in connection with a sale and purchase of future receivables, from time to time, to enter into actual transfer documents of such future receivables (e.g., every month, at the end of every quarter, semi-annually or annually). This would help to prevent any legal debate on whether the original sale and purchase agreement actually transfers the receivables only existing at the time each transfer document is signed.

Special assignment. The Third Additional Provision of Act 1/1999 expressly envisages the assignment of future receivables. As referred to above in question 4.1, these receivables shall either:

(1) exist on the execution date of the assignment agreement; or

(2) arise as a result of the business activity of the assignor within a maximum period of one year from the execution of the assignment agreement or, alternatively, shall be receivables whose future obligors are clearly identified in the assignment agreement.

FT. Article 16 of Act 5/2015 expressly envisages the assignment of future receivables to the FT. These receivables shall be collections of an already known or estimated amount. The assignment needs to be executed in a way that evidences, in a credible and unambiguous way, that the transfer of ownership has taken place. Act 5/2015 sets out examples of future receivables such as flows arising out of toll road projects or any other credit rights that CNMV determines by circular letter.

Please note that Act 5/2015, in its Eight Transitional Provision, envisages a new circular to be issued by CNMV replacing Order EHA/3536/2005, of 10 November. To this day, this new circular has not been enacted yet, and therefore Order EHA/3536 /2005 remains in force.

Order EHA/3536/2005 sets out that the transfer of future receivables shall meet certain requirements, such as that the assignment has to be full and unconditional ("*plena e incondicionada*") and that the incorporation deed of the FT shall specify:

(1) the terms or the activity under which those receivables will be generated;

(2) the powers of the assignor over those receivables;

(3) the conditions of that assignment; and

(4) the risk allocation between the assignor and the assignee.

Regarding the distinction between future receivables arising prior to or after the seller's insolvency, please see questions 6.1 and 6.5 below.

4.12 Related Security. Must any additional formalities be fulfilled in order for the related security to be transferred concurrently with the sale of receivables? If not all related security can be enforceably transferred, what methods are customarily adopted to provide the purchaser the benefits of such related security?

Spanish law provides that *in rem* security interests are ancillary to the main secured obligation and, hence, the transfer of the main secured obligation automatically entails the transfer of the security interests ancillary to it.

However, it is advisable for enforcement purposes to notarise the assignment so that the assignee may evidence, for enforcement purposes, that it benefits from the security (otherwise, the assignee may not have access to direct enforcement proceedings). If the security is a mortgage, a chattel mortgage or a chattel pledge, it is necessary, for the same enforcement purposes, to register the transfer in the Land Registry or the Moveable Assets Registry (as appropriate). Finally, real estate law provides that (unless otherwise agreed) the transfer of an obligation secured by a real estate mortgage should be notified to the obligor.

4.13 Set-Off; Liability to Obligor. Assuming that a receivables contract does not contain a provision whereby the obligor waives its right to set-off against amounts it owes to the seller, do the obligor's set-off rights terminate upon its receipt of notice of a sale? At any other time? If a receivables contract does not waive set-off but the obligor's set-off rights are terminated due to notice or some other action, will either the seller or the purchaser be liable to the obligor for damages caused by such termination?

Spanish law allows an obligor to set off against amounts it owes to a creditor if both the amounts owed by, and to, the creditor, are due and payable ("*deudas líquidas, vencidas y exigibles*"). Set-off occurs automatically and without the need of any notice by any of the parties to the other. If the requirements for setting off have been fulfilled before an obligor is served with the notice of an assignment, such obligor would be entitled to oppose to the purchaser any set-off already occurring before such notice. After the notice of assignment, an obligor would be entitled to oppose set-off against any amount it may owe to the purchaser. The above assumes that the assignment is not prohibited by the original contract. If the assignment is prohibited, an obligor (in addition to any claim that

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the obligor may have as result of an assignment made in breach of the prohibition) may continue setting off against any amount owed to the original seller.

Regarding the last question, in case a receivables contract does not waive set-off rights neither the seller nor the purchaser are liable to the obligor for damages caused by the termination of set-off rights.

4.14 Profit Extraction. What methods are typically used in your jurisdiction to extract residual profits from the purchaser?

Ordinary and special assignment. The assignment agreement may envisage that the purchaser shall transfer to the seller any residual profit (for example, any fee due by the obligor) with immediate effect.

FTs. In case the portfolio is assigned to an FT pursuant to Act 5/2015, since the fair value of the FT shall be zero, it is customary to envisage the payment to the seller of the residual profits on the last position of the cash flow waterfall. That is, once the claims of each and every creditor have been satisfied, the FT transfers to the seller the residual profits arising under the transaction. This amount is typically referred to as the intermediation margin ("*margen de intermediación*").

5 Security Issues

5.1 Back-up Security. Is it customary in your jurisdiction to take a "back-up" security interest over the seller's ownership interest in the receivables and the related security, in the event that an outright sale is deemed by a court (for whatever reason) not to have occurred and have been perfected (see question 4.9 above)?

This is not usual under Spanish practice.

5.2 Seller Security. If it is customary to take back-up security, what are the formalities for the seller granting a security interest in receivables and related security under the laws of your jurisdiction, and for such security interest to be perfected?

This is not applicable (please see the answer to question 5.1 above).

5.3 Purchaser Security. If the purchaser grants security over all of its assets (including purchased receivables) in favour of the providers of its funding, what formalities must the purchaser comply with in your jurisdiction to grant and perfect a security interest in purchased receivables governed by the laws of your jurisdiction and the related security?

Under Spanish law, receivables can be attached to three different types of security interests: (i) possessory pledges; (ii) non-possessory pledges; and (iii) subject to certain limitations, financial collaterals.

Perfection of possessory pledges require that the pledgor "transfers the possession" of the receivable to the pledgee or to a third party (as appointed by pledgor and pledgee (e.g., a security agent)). Spanish law is not clear as to how this transfer of possession should be made in connection with a receivable, as Spanish general security interest regulations only foresee the transfer of tangible assets. As a matter of practice, it is generally accepted that the notarisation of the pledge, plus serving a notice of the creation of the pledge to the obligor, is sufficient to perfect a possessory pledge. When the parties prefer to avoid serving a notice to the obligors due to commercial reasons (e.g., due to confidentiality or reputational issues, etc.), alternative manners of transferring the possession of the receivable could be available.

Non-possessory pledges must be registered with the relevant Movable Assets Registry ("*Registro de Bienes Muebles*"). For these purposes, non-possessory pledges are signed in front of a Spanish Notary Public and are notarised in the form of a public document (as a matter of practice, in this case a "*póliza intervenida*").

Certain types of receivables could be also attached to financial collateral (as provided by RDL 5/2005). RDL 5/2005 provides that financial collateral must be in written form and no additional formality should be required to perfect financial collaterals. RDL 5/2005 also provides that the delivery by a pledgor to the pledgee of a list of receivables in writing is sufficient to consider the receivables transferred to the pledgee. As a matter of practice, it is customary to perform the same perfection requirements explained for possessory pledges when creating a financial collateral (i.e., a notarial document and notice to the obligor).

5.4 Recognition. If the purchaser grants a security interest in receivables governed by the laws of your jurisdiction, and that security interest is valid and perfected under the laws of the purchaser's jurisdiction, will the security be treated as valid and perfected in your jurisdiction or must additional steps be taken in your jurisdiction?

A security interest validly created over a receivable and governed by a law other than Spanish law could be recognised as valid by a Spanish court on the basis of article 14.3 of the Rome I Regulation.

According to the Rome I Regulation, Spanish law would govern the assignability of the receivables, the relationship between the pledgee and the debtor of the receivable, the conditions under which the pledge can be invoked against the debtor, and the conditions under which the debtor's obligations could be discharged. This entails that it would be advisable to comply with the perfection requirements, in the same terms and in the same conditions as if it was a Spanish law-governed pledge. Therefore, it would be advisable to have the foreign law-governed pledge notarised in Spain, and the debtor notified of the creation of the pledge (please see the answer to question 5.3 above).

It remains unclear to what extent a pledge created over Spanish law governed receivables would be fully recognised *vis-à-vis* third creditors of the pledgor (for example, in the case of an insolvency proceeding) if the pledge is governed by a law different from Spanish law. Common opinion, however, suggests that if the Spanish perfection requirements have been met, a Spanish insolvency court may not reject the recognition of that pledge, even in the case of insolvency.

5.5 Additional Formalities. What additional or different requirements apply to security interests in or connected to insurance policies, promissory notes, mortgage loans, consumer loans or marketable debt securities?

Except for certain limited cases, no requirements in addition to those generally applicable to security over receivables apply in connection with the perfection of pledges over insurance policies, mortgage loans or consumer loans.

Security interests over promissory notes could require the endorsement by way of security over the same to perfect the security

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interest (if the promissory note has been issued in registered form), or the delivery of the same to the pledgee (if the promissory note has been issued in bearer form).

Security interests over marketable debt securities could require the following additional perfection requirements: (i) if the marketable debt securities are represented by book entries, the registration of the security interest in the relevant registry is required; (ii) if marketable debt securities have been issued in registered form, it is required that the pledgor endorses as security the relevant debt certificate; and (iii) if marketable debt securities have been issued in bearer form, the pledgor must deliver the relevant debt certificate to the pledgee.

5.6 Trusts. Does your jurisdiction recognise trusts? If not, is there a mechanism whereby collections received by the seller in respect of sold receivables can be held or be deemed to be held separate and apart from the seller's own assets (so that they are not part of the seller's insolvency estate) until turned over to the purchaser?

Spanish law is not familiar with the concept of "trust", and it does not recognise the creation of a dual ownership (beneficial owner and legal owner). Therefore, trusts are not used in the Spanish practice. Although it would not have the same effects as a "trust", it is possible (and common in Spanish practice) to create a pledge in favour of the purchaser over the bank account/s of the seller where the collections are credited. This pledge would confer upon the buyer a legal preference over the amount standing to the credit in such bank account in case of default or insolvency of the seller. This mechanism, however, may not be useful for collections received by the seller after a declaration of insolvency, as there are cases where insolvency courts have taken the view that a pledge over a bank account only attaches the balance standing to the credit in such bank account as of the date the insolvency is declared. Irrevocable instructions given by the seller to the obligors, or the account bank, may not survive the declaration of insolvency of the seller.

5.7 Bank Accounts. Does your jurisdiction recognise escrow accounts? Can security be taken over a bank account located in your jurisdiction? If so, what is the typical method? Would courts in your jurisdiction recognise a foreign law grant of security (for example, an English law debenture) taken over a bank account located in your jurisdiction?

Escrow accounts are customary in Spanish practice. Security can be taken over a bank account located in Spain under Spanish law, in the form of a possessory pledge or, eventually, a financial collateral (please see the answer to question 5.3 above).

Although it is not usual in practice, a security interest validly created under English law over a bank account located in Spain could be recognised by a Spanish court on the basis of article 14 of the Rome I Regulation. In that case, Spanish law would govern the assignability of the bank account receivables, the relationship between the pledgee and the account bank, the conditions under which the pledge can be invoked against the account bank, and the conditions under which the account bank's obligations could be discharged (see question 5.3 above).

5.8 Enforcement over Bank Accounts. If security over a bank account is possible and the secured party enforces that security, does the secured party control all cash flowing into the bank account from enforcement forward until the secured party is repaid in full, or are there limitations? If there are limitations, what are they?

Except as provided below, generally, no limitations apply. The pledgee would, upon enforcement of the pledge, be entitled to appropriate (or to set-off, as applicable) the balance standing to the credit in the bank account from time to time.

The above assumes that the pledgor has not been declared insolvent. If the pledgor has been declared insolvent under a Spanish insolvency proceeding, the pledgee may not be entitled to funds flowing into the bank account after the declaration of insolvency. If the pledgor has been declared insolvent under a law different than Spain, the rules governing the main insolvency proceeding may also limit the legal rights of the pledgee.

Regarding security interests created over a bank account as a financial collateral, a recent judgment from the European Court of Justice has ruled that in order to benefit from the privileged regime envisaged in the Financial Collateral Directive (Directive 2202/47/EC, transposed by RDL 5/2005 in Spain), funds under the bank account must not be available for the pledgor.

5.9 Use of Cash Bank Accounts. If security over a bank account is possible, can the owner of the account have access to the funds in the account prior to enforcement without affecting the security?

Yes, the parties may agree that the owner of the account shall have access to the funds in the account prior to the enforcement. This would not affect the security. The parties would normally agree that a minimum balance should be left in the bank account at all times (e.g., 100 Euros, or a similar amount), as some scholars have argued that a pledge over a bank account could be considered extinguished if the balance standing to the credit of such bank account is, or becomes, zero, or if the account is overdrawn.

It is also usual to agree in project finance facilities agreements, restrictions on the use of the funds deposited into the account of the borrower(s) from time to time. These restrictions are contractual undertakings of the borrower(s), which would not be binding upon the account bank unless the account bank, the pledgor and the pledgee enter into a direct agreement. Finally, unlike other jurisdictions, it is not usual under Spanish law to vest the pledgee (nor the security agent) with signing rights over the account of the pledgor, as this could be considered by a court, evidence that the pledge is, or acts as, a *de facto* director of the owner of the account.

Notwithstanding the foregoing, as referred to in question 5.8 above, a recent judgment from the European Court of Justice has ruled that in order to benefit from the privileged regime envisaged in the Financial Collateral Directive, the owner of the account must not have access to the funds.

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6 Insolvency Laws

6.1 Stay of Action. If, after a sale of receivables that is otherwise perfected, the seller becomes subject to an insolvency proceeding, will your jurisdiction's insolvency laws automatically prohibit the purchaser from collecting, transferring or otherwise exercising ownership rights over the purchased receivables (a "stay of action")? If so, what generally is the length of that stay of action? Does the insolvency official have the ability to stay collection and enforcement actions until he determines that the sale is perfected? Would the answer be different if the purchaser is deemed to only be a secured party rather than the owner of the receivables?

To the extent that the sale of receivables is a true sale and is otherwise perfected and executed before bankruptcy declaration, the purchaser would have a right to carve out the receivables from the estate. However, if seller acts as servicer, there is a risk of the proceeds being commingled with the estate.

On the other hand, if the contract is executory for both parties at bankruptcy declaration, the debtor or the bankruptcy officer (depending on the degree of intervention) could reject the contract, in which case the purchaser would hold a damages claim, which would earn the treatment of administrative expenses (pre-deduction from the estate).

Subsequent purchase and sale contracts would be subject to the bankruptcy officer's authorisation (or direct consent, depending on the degree of intervention on the debtor's managing abilities). Court approval may be also required, insofar as the scope of the transaction exceeds the ordinary course of business.

Regarding security interests over receivables, the pledge shall vest the lender with secured treatment, so long as the receivables stem from a contract that has been perfected prior to bankruptcy declaration. The pledge shall not be effective, on the other hand, with respect to contracts entered into after bankruptcy declaration. Besides, if the receivables are deemed to be an asset needed for the ordinary course of business, the enforcement shall be stayed for one year, unless the debtor approves a plan of reorganisation or liquidation starts first. The only exception thereof is that the pledge is subject to special regime on financial collateral (in which case it is exempt from the application of the general insolvency provisions) or the receivables are deemed to be located in a foreign state (in which case foreign law may apply, unless it is an EU Member State, in which case the enforcement will escape the automatic stay).

6.2 Insolvency Official's Powers. If there is no stay of action, under what circumstances, if any, does the insolvency official have the power to prohibit the purchaser's exercise of its ownership rights over the receivables (by means of injunction, stay order or other action)?

See question 6.1 above. Furthermore, the purchase and sale agreement of receivables could be subject to clawback (see question 6.3 below).

6.3 Suspect Period (Clawback). Under what facts or circumstances could the insolvency official rescind or reverse transactions that took place during a "suspect" or "preference" period before the commencement of the seller's insolvency proceedings? What are the lengths of the "suspect" or "preference" periods in your jurisdiction for (a) transactions between unrelated parties, and (b) transactions between related parties? If the purchaser is majority-owned or controlled by the seller or an affiliate of the seller, does that render sales by the seller to the purchaser "related party transactions" for purposes of determining the length of the suspect period? If a parent company of the seller guarantee's the performance by the seller of its obligations under contracts with the purchaser, does that render sales by the seller to the purchaser "related party transactions" for purposes of determining the length of the suspect period?

Under Spanish law, acts and transactions entered into within two years prior to bankruptcy declaration, may be subject to clawback (and thus avoided), so long as:

(1) the debtor does not receive reasonably equivalent value in exchange at the time the transaction is perfected – or there is not a sound business reason for the detriment caused to the estate; or

(2) certain creditors are preferred to others when the company is already insolvent (i.e., unable to regularly pay its debts as they are due).

Hence, Act 22/2003 on Insolvency (the "**Insolvency Act**") does not distinguish between voidable preferences and fraudulent transfers. There is one action only, whereby the regime is the same for both purposes. The reach-back period is two years. The clawback action can only be filed once there is a bankruptcy proceeding in place.

The standing to bring a clawback action corresponds to the bankruptcy officer. Creditors (any creditor – no threshold is required) only have alternative standing if they prompt the filing of a clawback action and the bankruptcy officer does not bring it within two months. In such a case, creditors litigate at their own account. However, they may demand reimbursement of expenses up to the amount of the proceeds in case of success. This alternative standing does not apply to certain ring-fenced out-of-court workouts.

The Insolvency Act sets forth certain safe harbours, as well as rebuttable and non-rebuttable presumptions of acts and transactions that are preferential or detrimental to the estate (and hence avoidable).

Safe harbours are fundamentally: (i) acts and transactions done within the ordinary course of business according to standard conditions; and (ii) certain ring-fenced out-of-court workouts. In our experience, courts' construction of the ordinary course of business is restrictive.

Rebuttable presumptions (i.e., admitting evidence to the contrary, whose proof corresponds to the defendant) are: (i) onerous acts and transactions entered into with insiders (specially related persons or connected parties); (ii) the perfection of security interests in favour of antecedent debt (except for certain public claims); and (iii) early payment of secured claims with maturity subsequent to bankruptcy declaration.

Hence, whilst the length of the hardening period is the same, "related party transactions" are presumed to be detrimental to the estate.

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If the purchaser is majority owned or controlled by the seller or an affiliate of the seller, that renders sales by the seller to the purchaser "related party transactions", so long as the seller and purchaser belong to the same group of companies (i.e., the seller directly or indirectly owns more than 50% of the shares or has the ability to appoint the majority of directors).

If a parent company of the seller guarantees the performance by the seller of its obligations under contracts with the purchaser, that does not render sales by the seller to the purchaser "related party transactions".

However, the guarantee would be deemed a related party transaction for clawback purposes – it is deemed that the seller would not have been able to close the transaction had its parent company not guarantee the transaction).

Non-rebuttable presumptions are (i) gifts and other acts or transactions without consideration, and (ii) early payment of unsecured claims with maturity subsequent to bankruptcy declaration.

Actual intent or fraud is not required to bring a clawback action successfully (except as to security interests subject to the special financial collateral regulation). The only requisite thereof is (i) lack of reasonably equivalent value or sound business reason when the transaction is perfected, or (ii) preferential payments when the company is already insolvent.

Yet in cases of actual fraud, the reach-back period to bring a fraudulent conveyance action is four years. Acts and transactions without consideration are presumed to be fraudulent. This action, which cannot be filed if there are other available recovery mechanisms, can be brought even if the insolvency proceeding has not been declared yet.

Causation-in-fact is also not required to successfully bring a clawback action. Likewise, preferential payments may be avoided even if the creditor demonstrates that the recovery does not exceed what it would obtain in liquidation. The link between the clawed back act or transaction and the generation or aggravation or insolvency may be significant though for classification purposes as per directors (e.g., potential liability for the impaired claims) or third parties (potential liability for aiding and abetting).

As per the outcome of a clawback action, the general rule (as per bilateral contracts with reciprocal obligations) is that the creditor obtains an administrative expense in exchange for the returning obligation, unless there is bad faith (i.e., actual or constructive knowledge that the act or transaction would be detrimental to the estate), in which case the claim is subordinated. If the creditor has transferred the collateral to a third party acting with good faith, there is an obligation to return the asset's value at the avoided transaction's time plus legal interests (and damages in case of bad faith).

Under European and Spanish insolvency conflicts of laws rules, the Insolvency Act would apply to a clawback action filed by a company whose bankruptcy proceeding is declared in Spain (because of the location of its centre of main interests therein). However, creditors can object to the filing of the clawback action subject to Spanish law by showing that the act or transaction would not be avoidable under the applicable law. More precisely, creditors can challenge the filing of the clawback action in the answer, by demonstrating:

(1) that the act or transaction is subject to foreign law (i.e., non-Spanish); and

(2) that the act or transaction would be ring-fenced under such foreign law.

6.4 Substantive Consolidation. Under what facts or circumstances, if any, could the insolvency official consolidate the assets and liabilities of the purchaser with those of the seller or its affiliates in the insolvency proceeding? If the purchaser is owned by the seller or by an affiliate of the seller, does that affect the consolidation analysis?

In the case of debtors belonging to the same group of companies (which would be the case of the purchaser owned by the seller or by an affiliate controlled by the seller), Spanish law establishes (i) the possibility of filing a joint petition, and (ii) procedural coordination of the proceedings. Yet, the assets and claims of each company are not commingled with those of the remaining companies. Hence, the default rule is that there is no substantive consolidation. The proceeds of the assets of each company are only applied to settle such company's claims. Substantive consolidation may only take place when the estates are so blended that it is rendered unfeasible to carve out debtors' claims and estates, without incurring unjustifiable delay and cost.

6.5 Effect of Insolvency on Receivables Sales. If insolvency proceedings are commenced against the seller in your jurisdiction, what effect do those proceedings have on (a) sales of receivables that would otherwise occur after the commencement of such proceedings, or (b) on sales of receivables that only come into existence after the commencement of such proceedings?

With regard to (a), to the extent that the contract is executory for both parties, there is risk of rejection (see question 6.1).

With regard to (b), consent of the bankruptcy officer and, so long as the transaction exceeds the ordinary course of business, court approval, would be required.

6.6 Effect of Limited Recourse Provisions. If a debtor's contract contains a limited recourse provision (see question 7.3 below), can the debtor nevertheless be declared insolvent on the grounds that it cannot pay its debts as they become due?

Yes, it can.

7 Special Rules

7.1 Securitisation Law. Is there a special securitisation law (and/or special provisions in other laws) in your jurisdiction establishing a legal framework for securitisation transactions? If so, what are the basics? Is there a regulatory authority responsible for regulating securitisation transactions in your jurisdiction?

Although envisaging, in certain aspects, a subsequent regulatory development, Act 5/2015, enacted in April 2015, sets out a unified legal regime for securitisation transactions in Spain, repealing former regulations on securitisation funds, which until April 2015 was set out in different laws and regulations.

The vehicle used in Spain and ruled by Act 5/2015 is the FT, as defined in question 4.1 above. FTs are separate pools of assets lacking legal personality, whose fair value is zero. Managing companies of these FTs, which shall act in the best interest of the

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FT's creditors and bondholders, subscribe on behalf of the FT any agreement to which the FT is a party, such as the servicing agreement on the underlying assets, or the loans and credit facilities agreements granted to the FT.

In addition to the general case, the Spanish legislation also permits the incorporation of "private" funds, that is, FTs whose bonds will not be listed in the Spanish official secondary markets and whose holding will be restricted to qualified investors. In such cases, a prospectus will not be legally required (only the deed of incorporation of the FT).

However, please note that certain regulatory developments in the European Union will have a material impact on securitisation transactions in Spain. Please refer to question 8.7 below to have more information on the European regulation recently passed on a general framework for securitisation and creating a specific framework for simple, transparent and standardised securitisation. Please find below a summary of the main aspects applying to the legal regime of the FTs:

1. Assignment of receivables to an FT

The assignment of receivables to an FT is analysed in questions 4.1, 4.2 and 4.11 above.

2. Types of FT

FTs may be incorporated either as closed funds or as open funds, depending on whether additional assets or liabilities may be incorporated to the FT:

(i) **Closed FTs**: In case the FT is incorporated as a closed fund, the deed of incorporation of the FT will not envisage the inclusion of additional assets or liabilities after the creation of the FT. However, the deed of incorporation may set out a four-month ramp-up period during which additional assets and liabilities may be transferred to the FT up to a certain limit. Additionally, replacements may take place in certain cases, such as in the case of non-eligible assets.

(ii) **Open FTs**: In case the FT is designed as an open fund, its assets, its liabilities, or both of them, may be modified (renewed) and/or extended after the incorporation of the FT. For instance, the FT may issue new securities, new credit facilities may be granted to the FT, or new assets may be assigned to the FT. In addition, and as an innovation of Act 5/2015, the public deed of incorporation of the FT and the relevant prospectus, when applicable (in case the FT is not private), may envisage that the assets of the FT may be actively managed. That is, the terms in which those assets can be modified in order to maximise the profitability of the FT, safeguard the quality of its assets, perform a proper risk treatment or keep the initial conditions of the FT set out in the incorporation deed.

3. Funding of FTs

The liabilities side of the FT comprises the fixed income securities issued by the FT and the facilities granted by third parties to the FT.

(i) **Fixed income securities**. The incorporation deed of the FT sets out the terms of the issuance of the securitisation bonds ("*bonos de titulización*"), dividing them into different series with different levels of seniority. The securitisation bonds may be traded in an official secondary market (public FT) or in a multilateral trading facility (private FT).

The incorporation deed of the FT normally sets out a pass-through model for the repayment of the securitisation bonds. Accordingly, the cash flow generated by the underlying assets included in the FT repays according to the order or priority, simultaneously and by the same amount, the interests and principal that correspond to the bondholders.

(ii) **Other liabilities**. Aside from the securitisation bonds, liabilities of the FTs may include loans and facilities granted by any third party (Act 5/2015 does not impose any restriction on the characteristics of the FT's creditor).

With respect to the interests of bondholders and creditors of the FT, unlike other jurisdictions, the Spanish legislation does not envisage the creation of a trust. Instead, Act 5/2015 sets out that the managing company shall act in the best interest of both bondholders and creditors, being accountable for its responsibilities (whether under the relevant contracts or legal duties) *vis-à-vis* them.

In addition to this role of the managing company, the incorporation deed of the FT may envisage the creation of a creditors' meeting ("*junta de acreedores*"), setting out its powers and the terms under which it may operate. The creditors' meeting represents the interests of both bondholders and creditors, although the incorporation deed may set out different participation terms depending on the type of creditor or bondholder.

4. Incorporation of an FT

The incorporation of an FT is subject to the prior compliance of the following requirements:

- Written authorisation request to CNMV.
- Approval and registration by CNMV of a prospectus. The prospectus will not be required in case of private funds, that is, in case the securitisation bonds are (i) exclusively addressed to qualified investors, and (ii) not intended to be listed in the Spanish official secondary markets.
- An audit report on the securitised assets shall be issued either by the managing company or by an external audit.
- Approval and registration by CNMV of (i) the draft of the incorporation deed, (ii) supporting documentation on the assets to be assigned to the FT, and (iii) any other supporting documentation required by CNMV.

With the adoption of Act 5/2015, the granting of a credit rating to the securitisation bonds with respect to a public FT has ceased to be a requirement in order to incorporate the FT.

5. Managing company

The managing company of an FT ("*Sociedad Gestora de Fondos de Titulización*") shall be a public limited company duly authorised by CNMV for these purposes. They are entitled to manage not only Spanish FTs (and FABs) but also foreign analogous vehicles. The managing company is responsible for the incorporation, management and representation of the FT. On the other hand, the managing company acts on behalf of the FT and has the duty to safeguard the interests of the bondholders and the other creditors of the FT, as mentioned above. As an innovation of the new legal regime of Spanish securitisations, Act 5/2015 expressly sets out that the managing company is responsible for the management of the securitised portfolio of assets. However, regarding the PHs and/or CTHs assigned to the FT, as referred to above in question 4.3, the responsibility for the management of the underlying assets (mortgage loans) remains in the issuer of the PH/CTH.

6. Compartments

As an innovation of Act 5/2015, independent compartments may be created within the same FT. Each of those compartments may have its own issuance of bonds and its own independent obligations. That is, each compartment will be liable of its own costs, expenses and debts. On the other hand, the incorporation deed of the FT may envisage the separate liquidation of each of those compartments.

7. Regulatory authority

As referred to in sections 4 ("*Incorporation of an FT*") and 5 ("*Managing company*") above, Spanish securitisation funds need the prior authorisation of and registration with the CNMV in Spain,

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and managing companies of an FT ("*Sociedad Gestora de Fondos de Titulización*") require a prior authorisation of the CNMV in order to incorporate, manage and represent Spanish FTs.

7.2 Securitisation Entities. Does your jurisdiction have laws specifically providing for establishment of special purpose entities for securitisation? If so, what does the law provide as to: (a) requirements for establishment and management of such an entity; (b) legal attributes and benefits of the entity; and (c) any specific requirements as to the status of directors or shareholders?

On the requirements for establishment and management of such entities, please see question 7.1 above for the regime applicable to the securitisation funds incorporated in Spain (FT) and the managing companies entitled to manage such vehicles.

On the other hand, FTs are subject to a privileged tax and insolvency regime, as referred to in the answer to question 4.3 above.

Since FTs are not legal entities, they do not have any directors or shareholders, so no specific requirements apply in this regard.

However, the companies managing those FTs are regulated entities, subject to CNMV's surveillance. In order to grant the relevant authorisation to a managing company, CNMV examines the suitability of the directors and significant shareholders (i.e., those holding at least 10% of the share capital of the company or voting rights) of the managing company.

7.3 Location and form of Securitisation Entities. Is it typical to establish the special purpose entity in your jurisdiction or offshore? If in your jurisdiction, what are the advantages to locating the special purpose entity in your jurisdiction? If offshore, where are special purpose entities typically located for securitisations in your jurisdiction? What are the forms that the special purpose entity would normally take in your jurisdiction and how would such entity usually be owned?

In case the portfolio has a financial nature (especially in case of mortgage loans), it is customary to establish an SPV in Spain by means of the incorporation of a FT, a special purpose vehicle subject to the prior authorisation of and registration with the CNMV. As referred to in question 4.1 above, assignments to these special purpose vehicles are subject to a special tax and insolvency regime:

In particular, the assignment of the portfolio to a FT has a competitive edge with respect to ordinary assignments, where the ordinary clawback regime (as referred to in question 6.3 below) applies. In contrast, in case of assignment to a FT, the insolvency official shall prove fraud in order to challenge the assignment and any good faith third party's rights would not be affected.

Additionally, as mentioned in question 4.3 above, when a credit institution sells mortgage loans and certain requirements under Act 2/1981 and RD 716/2009 are met, credit rights under that portfolio may be transferred by the issuance and subscription of PH and CTH. Such transfers are subject to a privileged regime for registration, tax (the issuance is exempt from stamp duty tax) and insolvency purposes (the assignment may only be challenged in case the insolvency official proves fraud).

7.4 Limited-Recourse Clause. Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) limiting the recourse of parties to that agreement to the available assets of the relevant debtor, and providing that to the extent of any shortfall the debt of the relevant debtor is extinguished?

Yes; in principle, a court in Spain would give effect to that contractual provision.

7.5 Non-Petition Clause. Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) prohibiting the parties from: (a) taking legal action against the purchaser or another person; or (b) commencing an insolvency proceeding against the purchaser or another person?

Spanish law contemplates the waiving of rights, to the extent that it is not detriment to a third party or contrary to public order. Having said that, the waiver of the right to seek insolvency relief or the right to take any legal action against the purchaser is unlikely to be upheld by a court (particularly in the context of an insolvent seller), notwithstanding any remedy (damages) corresponding to the non-breaching party.

7.6 Priority of Payments "Waterfall". Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) distributing payments to parties in a certain order specified in the contract?

In principle, a court in Spain would give effect to a contractual provision on payment waterfall, if that provision does not conflict with compulsory rules.

The Insolvency Act does not recognise subordination agreements unless *vis-á-vis* all creditors of the debtor. As such, the most likely outcome in a bankruptcy proceeding is that the officer and the court distribute the proceeds pursuant to compulsory priority rules, notwithstanding the enforceability of the subordination agreement as a turn-over provision in a separate proceeding.

7.7 Independent Director. Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) or a provision in a party's organisational documents prohibiting the directors from taking specified actions (including commencing an insolvency proceeding) without the affirmative vote of an independent director?

The Insolvency Act sets forth the duty to file for bankruptcy within two months as from debtor's insolvency situation (inability to regularly pay debts as they are due), with the exception of the so-called "5 *bis*" notice, which provides an extra four-month period to negotiate with creditors out-of-court. Otherwise, directors may be held liable for the accrued claims as from the onset of insolvency that turn out to be impaired if the company is liquidated, or the late petition is found to be the cause for that impairment.

If, however, the articles of incorporation do require a majority of directors to petition for bankruptcy (for instance, three joint directors), there is case law on the dismissal of bankruptcy petitions if the internal corporate resolution is not valid (only two out of three joint directors adopt the decision).

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In practice, the most efficient way to avoid a bankruptcy petition is the enforcement of step-in rights, which vest lenders with voting rights to change directors. This must be included in the articles of incorporation in order to be enforceable against third parties.

7.8 Location of Purchaser. Is it typical to establish the purchaser in your jurisdiction or offshore? If in your jurisdiction, what are the advantages to locating the purchaser in your jurisdiction? If offshore, where are purchasers typically located for securitisations in your jurisdiction?

Commercial receivables. In case of commercial receivables or non-performing loans, it is customary that the purchaser is established in an EU Member State, such as Luxembourg, Netherlands or Ireland, for operational, commercial, tax, regulatory and other business reasons.

Financial assets. Please refer to the answer in question 7.3 above.

8 Regulatory Issues

8.1 Required Authorisations, etc. Assuming that the purchaser does no other business in your jurisdiction, will its purchase and ownership or its collection and enforcement of receivables result in its being required to qualify to do business or to obtain any licence or its being subject to regulation as a financial institution in your jurisdiction? Does the answer to the preceding question change if the purchaser does business with more than one seller in your jurisdiction?

As referred to above in the preceding section, securitisation funds incorporated in Spain (FTs) and their managing companies are subject to the Spanish capital markets regulation, to the prior administrative authorisation of the CNMV and to surveillance of the mentioned supervisor.

Aside from these two entities, whose special regime has been analysed in the preceding section, in general, the purchase of portfolios of receivables does not require any prior licence in Spain, regardless of whether the purchaser does business with other sellers in Spain.

However, in case the purchaser of a consumer loan portfolio subrogates itself into the lender's position, there is a risk that Spanish consumer authorities and/or Spanish courts consider that Act 2/2009, March 31, on mortgage loans and mortgage credits granted to consumers and on intermediary services regarding mortgage loans and mortgage credits ("**Act 2/2009**") should apply likewise in these circumstances, although article 1 of Act 2/2009 sets out that it shall apply to professionals "granting" such mortgage loans and credits (which, strictly speaking, would not be the case).

In case Spanish consumer authorities and/or Spanish courts held the interpretation mentioned in the preceding paragraph, this would involve, essentially: (i) the mandatory registration of the purchaser of the loans within the special registry held by the Spanish consumer authorities, which should be prior to the purchase of the relevant portfolio; and (ii) the need to comply with certain consumer regulations, which basically relate to the information obligations to be fulfilled at the time of granting the loan or credit. In any case, it should be noted that the application of Act 2/2009 does not involve being subject to regulation as a financial institution in Spain.

The same consequences (i) and (ii) mentioned in the preceding paragraph may apply in case a non-Spanish fund or their managing companies, or any other kind of investor, systematically bought loan portfolios granted to consumers.

8.2 Servicing. Does the seller require any licences, etc., in order to continue to enforce and collect receivables following their sale to the purchaser, including to appear before a court? Does a third-party replacement servicer require any licences, etc., in order to enforce and collect sold receivables?

Neither the seller nor any third party performing collection tasks regarding the assigned portfolio of receivables are subject to any prior licence in order to collect those receivables. As an exception to the foregoing, a prior licence will be required when the administration activities are, because of their nature, subject to that prior requirement. For example, in the case of collection of receivables under a portfolio of mortgage loans, when the administration activities necessarily involve holding the obligors' bank accounts, the servicing activity will be indirectly subject to prior authorisation since the gathering of reimbursable funds from the public is activity reserved to financial institutions. Likewise, in case the collection of receivables involves providing payment services, the servicing activity will be indirectly subject to prior authorisation since the provision of payment services is an activity reserved to certain financial entities (mainly, credit institutions, electronic money institutions and payment institutions).

On the enforceability of such receivables, in order to appear in court on behalf of the assignee:

- In the case of a third-party replacement, the third party will need the relevant power of attorney granted by the purchaser in order to appear in court on behalf of the purchaser.
- In the case that, despite serving notification of the assignment to the obligor, the seller remains responsible for the collection tasks, in order to appear in court on behalf of the purchaser, the seller will need a power of attorney granted by the purchaser.

In addition to the foregoing and regardless of who is performing the servicing activities, in order to appear in court, the assistance of a court agent ("*procurador*") is required in Spain.

8.3 Data Protection. Does your jurisdiction have laws restricting the use or dissemination of data about or provided by obligors? If so, do these laws apply only to consumer obligors or also to enterprises?

Yes. The Organic Act 15/1999, of December 13, on Personal Data Protection ("**Organic Act 15/1999**") and the regulation developing this act, approved by Royal Decree 1720/2007, of December 21, set out restrictions on the processing and transfer of personal data. For these purposes, personal data is any information relating to an identified or identifiable natural person (the data subject), therefore affecting obligors who are individuals (consumer obligors and sole traders).

In general, data subjects' consent is required to process their data, although there are exceptions to this rule, such as when the personal data refers to the parties of an administrative, employment or business relationship contract or pre-contract, and it is necessary for its maintenance of fulfilment. Consent must be informed and, depending on the circumstances, it may be implicit, express or written.

In order to transfer personal data to a third party, the data controller (i.e., any natural or legal person, whether public or private, or administrative body that makes decisions on the purposes, content and use of personal data processing) must have previously informed the data subject of the transfer, identifying the data recipients and

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specifying the purpose of the transfer. In addition, the data controller must obtain the data subject's consent, unless an exception provided by law applies, for example:

- when the transfer is authorised by law;
- when the transfer results from the free and legitimate acceptance of a legal relationship whose development, fulfilment and control implies such transfer; and
- when the transfer satisfies a legitimate interest of the controller or the party to whom the personal data is transferred, provided that such interest is not overridden by the data subject's interests or fundamental rights and freedoms.

The requirements above do not apply when the data recipient acts as the data processor, processing the personal data exclusively on behalf of the data controller and under its instructions to render a service to the data controller. In this case, the data processing must be regulated in a contract specifying the conditions established under article 12 of the Organic Act 15/1999.

Additionally, when the data is transferred to a country whose level of protection has not been declared adequate by the relevant authorities (any country outside the European Economic Area, with some exceptions), the transfer must be notified to the Spanish Data Protection Agency ("*Agencia Española de Protección de Datos*") and authorised by the director of that agency. Article 34 of the Organic Act 15/1999 establishes specific exceptions to the authorisation requirement. These exceptions include: when the data subject has unequivocally given consent to the data transfer; and when the transfer is necessary for the performance of a contract between the data subject and the data controller, or to adopt pre-contractual measures at the data subject's request.

Note that the above-described regime will remain in force until May 28, 2018. At that date, the EU General Data Protection Regulation will fully enter into force, setting forth additional requirements in connection with the processing of personal data and the international transfers of personal data.

Firstly, implied consent will no longer be deemed valid and it will be necessary to either cancel the personal data or obtain affected individuals' consent for processing said data beyond May 28, 2018. In addition, further information will have to be provided to data subjects, such as, for instance, contact details of the so-called data protection officer (if any), the legal basis for the data processing, data retention periods, or the new rights granted to data subjects, amongst other information. Secondly, the data processing agreements entered into with any third parties providing services to the data controller and gaining access to personal data as a result of any such access will have to be in line with article 28 of the General Data Protection Regulation, which includes stricter obligations than the ones contemplated in national law (i.e., to cooperate with the data controller in order to allow it to comply with certain obligations under the new piece of legislation, amongst others). Thirdly, transfer of data to any country outside the European Economic Area will no longer require the prior authorisation of the Spanish Data Protection Agency, as long as it is based in the standard contractual clauses as approved by the European Commission, or relies on any of the other exemptions set forth by law (such as the implementation of binding corporate rules).

Although these rules only apply to individuals' personal data, other regulations (e.g., on banking secrecy) may also impose restrictions on the use and dissemination of sole traders' and enterprises' data.

8.4 Consumer Protection. If the obligors are consumers, will the purchaser (including a bank acting as purchaser) be required to comply with any consumer protection law of your jurisdiction? Briefly, what is required?

According to the first paragraph of article 31 of Act 16/2011, in case the lender under a consumer loan agreement assigns the credit rights thereunder, the borrower (consumer) shall be entitled to raise before the assignee the same defences that would have corresponded to that obligor *vis-à-vis* the original lender, including set-off, in case those credit rights had not been assigned.

In addition, the second paragraph of article 31 of Act 16/2011 sets out that the assignment shall be notified to the borrower except when the original lender continues providing servicing services. In any case, as referred to above, the borrower will be entitled to raise before the assignee any exception the consumer had *vis-á-vis* the original lender, including set-off.

However, please bear in mind that in Spain there are regional regulations that, in terms of consumer protection, must be taken into account (in Spain there are 17 regions, the "*Comunidades Autónomas*"). In particular, regarding the protection of the mortgage debtor, some of these regional rules impose, for example, an obligation to notify to the debtor the assignment of the mortgage loan, so that the assignee of the credit right has then *locus standi* in a foreclosure scenario. Notwithstanding the foregoing, and in relation to questions 4.2 and 4.3 above on the requirements for the validity of this assignment, these consumer protection rules do not challenge the validity of the assignment.

8.5 Currency Restrictions. Does your jurisdiction have laws restricting the exchange of your jurisdiction's currency for other currencies or the making of payments in your jurisdiction's currency to persons outside the country?

No, there are no restrictions on the exchange of the euro for other currencies or the making of payments in euros to persons outside of Spain.

On the other hand, although not being a currency restriction, Spanish residents are subject to certain reporting obligations before the Bank of Spain regarding their cross-border positions. In particular, Spanish residents shall inform the Bank of Spain of their payment transactions (monthly, quarterly or annually, depending on the amount of such transactions during the preceding year) and the amount of the balance of assets and liabilities abroad.

In any case, the breach of this information obligation by a Spanish resident on a particular transaction will not deem that transaction invalid, regardless of any other implication from an administrative perspective.

8.6 Risk Retention. Does your jurisdiction have laws or regulations relating to "risk retention"? How are securitisation transactions in your jurisdiction usually structured to satisfy those risk retention requirements?

Regulation (EU) No 575/2013 of the European Parliament and of the Council of 26 June, 2013, on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012 ("**Regulation 575/2013**"), applicable in Spain, sets certain requirements for the mentioned institutional investors. Amongst those requirements, there is a rule on the retained interest

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of the issuer. In this regard, an institution, other than when acting as an originator, a sponsor or original lender, shall be exposed to the credit risk of a securitisation position in its trading book or non-trading book only if the originator, sponsor or original lender has explicitly disclosed to the institution that it will retain, on an ongoing basis, a material net economic interest which, in any event, shall not be less than 5%.

Regulation 575/2013 sets out a list of situations that qualify as the retention of a material net economic interest. These include: (i) the retention of not less than 5% of the nominal value of each of the tranches sold or transferred to the investors; or (ii) the retention of the first loss tranche and, if necessary, other tranches having the same or a more severe risk profile than those transferred or sold to investors and not maturing earlier than those transferred or sold to investors, so that the total retention percentage is above 5% of the nominal value of the securitised exposures.

Additionally, Regulation 575/2013 sets out that net economic interest is measured at origination and shall be maintained on an ongoing basis. The net economic interest, including retained positions, interest or exposures, shall not be subject to any credit risk mitigation or any short positions or any other hedge and shall not be sold. The net economic interest shall be determined by the notional value for off-balance sheet items.

Notwithstanding the foregoing, it should be noted that the exposed risk retention rule will be slightly adjusted, as further explained in question 8.7 below, by virtue of Regulation (EU) No 2017/2402 of the European Parliament and of the Council, of 12 December, 2017, laying down a general framework for securitisation and creating a specific framework for simple, transparent and standardised securitisation, and amending Directives 2009/65/EC, 2009/138/EC and 2011/61/EU and Regulations (EC) No 1060/2009 and (EU) No 648/2012. Once this new regulation enters into in force, the risk retention rule will be a direct legal obligation for originators, sponsors or original lenders.

8.7 Regulatory Developments. Have there been any regulatory developments in your jurisdiction which are likely to have a material impact on securitisation transactions in your jurisdiction?

Securitisation Regulation. The European Parliament recently passed a new regulation on securitisation, Regulation (EU) No 2017/2402 of the European Parliament and of the Council, of 12 December 2017, laying down a general framework for securitisation and creating a specific framework for simple, transparent and standardised securitisation, and amending Directives 2009/65/EC, 2009/138/EC and 2011/61/EU and Regulations (EC) No 1060/2009 and (EU) No 648/2012 ("**Securitisation Regulation**").

Although the Securitisation Regulation requires further development by way of regulatory technical standards, it lays down a general framework for securitisation in the European Union with the following characteristics:

- **Due diligence obligation for institutional investors**, as they must verify some aspects of the origination of the loans.
- **Direct risk-retention rules** applicable to the originator, sponsor or original lender, as referred to in question 8.6 above.
- **New transparency obligations** for originators, sponsors and original lenders, as they must make available to holders of a securitisation position, competent authorities and potential investors, a minimum list of information.
- Creation of a specific framework for simple, transparent and standardised securitisations ("**STS Securitisations**"). The Securitisation Regulation envisages a more risk-sensitive prudential framework for STS Securitisations (i.e., true-sale securitisations which meet a number of requirements), provided that the originator, the sponsors or the Securitisation Special Purpose Entity have notified the STS Securitisation designation to investors, competent authorities and to European Securities and Markets Authority ("**ESMA**").
- **Ban on re-securitisation**, with certain exceptions.
- **Credit-granting standards**, as originators, sponsors and original lenders shall apply to exposures to be securitised the same sound and well-defined criteria for credit-granting which they apply to non-securitised exposures.
- **Securitisation repository** to be designated by each European Member State with supervisory, investigative and sanctioning powers. This repository will provide the investors with a single and supervised source of the data necessary for performing their due diligence.

The Securitisation Regulation will apply to securitisations the securities of which are issued on or after 1 January, 2019.

CRR Amendment Regulation. Regulation (EU) No 2017/2401 of the European Parliament and of the Council, of 12 December, 2017, amending Regulation (EU) No 575/2013 on prudential requirements for credit institutions and investment firms (hereinafter, the "**CRR Amendment Regulation**").

The CRR Amendment Regulation implements the revised Basel securitisation framework, envisaging a hierarchy of three different calculation methods, with specific rules on prudential treatment for credit institutions investing in STS securitisations.

9 Taxation

9.1 Withholding Taxes. Will any part of payments on receivables by the obligors to the seller or the purchaser be subject to withholding taxes in your jurisdiction? Does the answer depend on the nature of the receivables, whether they bear interest, their term to maturity, or where the seller or the purchaser is located? In the case of a sale of trade receivables at a discount, is there a risk that the discount will be recharacterised in whole or in part as interest? In the case of a sale of trade receivables where a portion of the purchase price is payable upon collection of the receivable, is there a risk that the deferred purchase price will be recharacterised in whole or in part as interest? If withholding taxes might apply, what are the typical methods for eliminating or reducing withholding taxes?

Whether any part of the payments on receivables made to the purchaser by Spanish obligors would be subject to withholding taxes in Spain depends on: (i) the characterisation, for tax purposes, of the income received by the purchaser; and (ii) the jurisdiction where the purchaser resides for tax purposes.

Although the characterisation of the income obtained by the non-Spanish tax resident purchaser is not clearly defined, in our opinion it would be deemed to be either (a) interest income, or (b) capital gains.

According to the Spanish Non-Resident Income Tax Act, regardless of whether the referred income is characterised as interest or capital gains, such income would be tax exempt in Spain to the extent the purchaser: (i) is resident for tax purposes in an EU Member State, other than a tax haven territory; and (ii) does not act, in regards to the purchase of the receivables, through a permanent establishment located in Spain or outside the EU.

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Residence for tax purposes in an EU Member State must be accredited through a certificate of tax residency issued by the relevant tax authorities. Tax residency certificates are valid for a one-year period.

In case the purchaser is resident for tax purposes in a non-EU Member State, it may be subject to withholding tax in Spain in accordance with the provisions set forth in the relevant convention for the avoidance of double taxation.

Residency in a particular jurisdiction for the purposes of the application of a reduced or a nil withholding tax in accordance with a specific convention must be accredited through a certificate of tax residency, issued by the relevant tax authorities. These certificates are valid for a one-year period.

In case the purchaser can neither accredit to be tax resident in an EU Member State nor in a jurisdiction with which Spain has a convention for the avoidance of double taxation in force, the purchaser would be subject to withholding tax on the income derived from the transaction at the general current tax rate of 19%.

Whether any part of the payments made by the obligor to the seller is subject to withholding tax in Spain depends, in the case the seller is a Spanish company, on the nature of such payments. In principle, payments made in remuneration of a delivery of goods or of the rendering of services are not subject to withholding tax in Spain. However, interest paid as remuneration of the deferral on the payment of a commercial transaction would be subject to withholding tax in Spain at the general tax rate of 19%.

Withholding taxes cannot be eliminated or reduced other than through the domestic law exemption or the relevant convention for the avoidance of double taxation – and provided that the purchaser is entitled to benefit from any of them.

9.2 Seller Tax Accounting. Does your jurisdiction require that a specific accounting policy is adopted for tax purposes by the seller or purchaser in the context of a securitisation?

The seller would be subject to the provisions set forth in the Spanish General Accounting Plan and the General Accepted Accounting Principles (“**GAAP**”) with regards to (i) the initial recognition of a credit against the obligor, and (ii) the recognition of the transfer of such credit to the purchaser. Note that the Spanish General Accounting Plan regulation is aligned, in general terms, with the provisions set forth in the International Financial Reporting Standards (“**IFRS**”).

Generally, the seller would recognise, for accounting purposes, the transfer of the receivable at the time of the transfer of the risks and benefits inherent to the creditor position against the obligor.

Spanish tax legislation does not establish any speciality in this regard; rather it follows the regulations foreseen under the Spanish General Accounting Plan and the GAAP.

9.3 Stamp Duty, etc. Does your jurisdiction impose stamp duty or other transfer or documentary taxes on sales of receivables?

According to the Spanish tax legislation, the issuance of bills of exchange (*letras de cambio*) and documents issued with the purpose of transferring funds (*título valor, documento cambiario* or *documentos que realicen la función de giro*), are subject to stamp duty. Promissory notes (*pagarés*) and any other analogous instruments issued in series with a maturity shorter than 18 months are subject to stamp duty but exempt.

The tax due depends on (i) the total amount represented on such document, and (ii) the maturity. The taxpayer would be the issuer of these instruments or, in case such instruments are issued abroad, the first holder in the Spanish territory of such instruments.

In addition, anyone intervening in the negotiation or collection of these instruments would be jointly and severally liable for the payment of the tax due and not paid by the issuer.

Transfer Tax would not apply to the extent the seller is a VAT taxpayer and the transfer of the receivables is subject to VAT.

9.4 Value Added Taxes. Does your jurisdiction impose value added tax, sales tax or other similar taxes on sales of goods or services, on sales of receivables or on fees for collection agent services?

Under Spanish Value Added Tax legislation, the transfer of the creditor position would be VAT exempt to the extent the seller fully transfers the risks and benefits which would derive from an eventual insolvency of the obligor. Similarly, transactions relating to bills of exchanges, documents issued with the purposes of transferring funds, promissory notes and any other analogous instruments would also be VAT exempt.

Note that the services rendered by the seller to the purchaser, consisting of the collection of the payments on receivables made by the obligors, would represent an independent transaction to the transfer of the creditor position and/or to the transfer of any documents issued with the purpose of transferring funds.

According to the Spanish general VAT location rules, those collection services would be deemed to be located in the jurisdiction where the purchaser is established for VAT purposes. Therefore, to the extent that the purchaser: (i) is not established, for VAT purposes, within the Spanish VAT territory; and (ii) does not have a permanent establishment within the Spanish VAT territory to which the service is supplied, collection services would not be subject to VAT in Spain.

9.5 Purchaser Liability. If the seller is required to pay value-added tax, stamp duty or other taxes upon the sale of receivables (or on the sale of goods or services that give rise to the receivables) and the seller does not pay, then will the taxing authority be able to make claims for the unpaid tax against the purchaser or against the sold receivables or collections?

Under the Spanish General Taxation Act, any entity or individual causing or actively collaborating with any tax infringement would be jointly and severally liable for the payment of any tax debts derived from the transactions.

Likewise, any entity or individual causing or collaborating on the occultation or transfer of assets and rights belonging to the tax debtor would also be jointly and severally liable for the payment of the tax debts of such debtor.

Entities or individuals not attending attachment orders issued over assets or rights, issued by the Spanish tax authorities, would also be jointly and severally liable for the payment of the unpaid tax debts as a consequence of such inattention. This may be the case if the purchaser receives communication from the Spanish tax authorities informing that any payments to the seller must be made, instead, to the tax authorities for the payment of unpaid tax debts of the seller and the purchaser neglects the order.

In addition to the above, Spanish Value Added Tax legislation regulates specific scenarios of tax responsibility.

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In particular, the recipient of a supply of goods and/or services would be joint and severally liable for the payment of VAT chargeable in the transaction if, as a result of a wilful or negligent act or omission, the correct application of the tax is prevented.

Furthermore, a recipient of a supply of goods and/or services acting as an entrepreneur or professional for the purposes of such supply would be liable for the payment of the VAT chargeable in a transaction, if such recipient should have reasonably presumed that the supplier was not going to pay the VAT to the Spanish tax authorities. Spanish Value Added Tax legislation considers that an individual should reasonably presume that the VAT charged in a supply of goods or services is not going to be paid to the relevant tax authorities if the price paid is notoriously below what could be considered a normal price.

Note that, in principle, the above-mentioned VAT responsibility would not be applicable on the proposed transaction to the extent the purchase of receivables would be VAT exempt and the collection services would not be located within the Spanish VAT territory in the terms described in question 9.4 above.

9.6 Doing Business. Assuming that the purchaser conducts no other business in your jurisdiction, would the purchaser's purchase of the receivables, its appointment of the seller as its servicer and collection agent, or its enforcement of the receivables against the obligors, make it liable to tax in your jurisdiction?

In general terms, a non-Spanish tax resident would be deemed to have a permanent establishment in Spain if such non-Spanish resident has empowered a Spanish tax resident individual to enter into agreements with third parties on their behalf.

Note that the appointment of the seller as the collection agent of the purchaser would require the granting certain powers to the seller for the purposes of rendering such collection services.

In principle, the empowerment to the seller for the purposes of acting as a mere collection agent should not imply that such seller acts as a dependant agent of the purchaser. Therefore, in principle, the seller, acting as a collection agent of the purchaser, would not be deemed to constitute a permanent establishment of the purchaser in Spain.

In any case, in order to ensure that the seller is not deemed to be a Spanish dependant agent of the purchaser, special attention must be paid to the content and nature of the authorities granted to the seller in the particular power of attorney. Only administrative faculties related to the mere cash collection of the receivables and not others related to the core business of the purchaser should be granted to the seller.

9.7 Taxable Income. If a purchaser located in your jurisdiction receives debt relief as the result of a limited recourse clause (see question 7.3 above), is that debt relief liable to tax in your jurisdiction?

Debt relief to a Spanish tax resident purchaser would trigger taxable income in Spain to that purchaser. However, if the debt forgiveness is granted by an affiliate to the purchaser, it may be treated as an equity contribution or a dividend distribution, as the case may be.

Acknowledgment

The authors would like to acknowledge the following people for their help in creating this chapter:

- **Jaime de la Torre**, a partner at Cuatrecasas. He provides advice on securitisation transactions, national and international, and has participated in many debt instrument issues, derivative transactions and many issues of preferred shares and warrants. He has recently been involved in many issues of corporate and high-yield bonds.

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Amongst other transactions, Héctor Bros advised lenders in the €2.5bn financing of Tranches I, II and IV of the Barcelona Metro Line 9, the €900m financing of the AP-1, AP-8 GI-632 hard toll highways in the Basque Country, the €400m project debt restructuring of the Vallvidrera ans Cadí tunnels and the €1.4bn regional infrastructure debt restructuring of the *Generalitat de Catalunya*. He has also participated in high-profile international project finance transactions, such as the $19bn Sadara petrochemical project in Saudi Arabia, where he advised the Spanish Corporate Internationalisation Fund (FIEM), and the €600m non-recourse financing to Abertis in connection with the acquisition of the Italian A-19 "Serenissima" toll road.

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With over 900 lawyers, Cuatrecasas is a law firm present in 12 countries. We advise on all areas of business law, applying a sectoral approach and covering all types of business. We have 16 offices on the Iberian Peninsula and 11 international offices, as well as five international desks and 20 country groups. We represent companies that are leaders in their sectors, advising them on their investments in the major markets, and we offer the most sophisticated advice, both in recurring matters as well as in complex transactions and litigation proceedings. In 2017, we were considered the third most innovative firm in Continental Europe in the *Financial Times* Innovative Lawyers Awards. We have also been acknowledged by international directories such as *Chambers* or *The Legal 500* as number one in the main legal practices.

The firm's Finance Practice consists of over 50 lawyers based in Madrid, Barcelona, Lisbon, London, Mexico City and Bogotá, with expert knowledge and extensive experience in complex national and international financial transactions. The lawyers work seamlessly from different locations, ensuring a wide coverage for their clients, wherever they are based. The team has extensive expertise advising sponsors and banks in all types of domestic and foreign, corporate and structured, financial and debt capital markets transactions. Among other aspects, such transactions consist of: structured and project finance facilities; refinancing, acquisition finance and other sorts of repackaging; synthetic and mortgage-backed securitisation; credit assignments; issuance of fixed-interest securities and other financial instruments; and consumer credits. We also deal with bankruptcy issues in order to efficiently ensure bankruptcy remoteness and an adequate security package structure, extending the scope of our advice to the restructuring of debt. In addition, we advise on matters and relevant issues related to equity requirements for credit institutions, as well as for other entities.

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Sweden

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1 Receivables Contracts

1.1 Formalities. In order to create an enforceable debt obligation of the obligor to the seller: (a) is it necessary that the sales of goods or services are evidenced by a formal receivables contract; (b) are invoices alone sufficient; and (c) can a binding contract arise as a result of the behaviour of the parties?

(a) No, sales of goods or services are not generally subject to any formal requirements. There are certain instances – such as the purchase of real estate and consumer credit – where writing or some other durable and retrievable medium is required. It is always advisable to reduce contractual terms to writing or another durable or retrievable medium for evidentiary purposes.

(b) Although invoices can serve as evidence of a claim, their unilateral nature seldom makes them sufficient evidence on their own.

(c) Yes, provided the behaviour, taken in its context, could be reasonably construed as an intention to make an agreement.

1.2 Consumer Protections. Do your jurisdiction's laws: (a) limit rates of interest on consumer credit, loans or other kinds of receivables; (b) provide a statutory right to interest on late payments; (c) permit consumers to cancel receivables for a specified period of time; or (d) provide other noteworthy rights to consumers with respect to receivables owing by them?

(a) No. However, in egregious cases very high interest rates may be revised by the courts as being usurious.

(b) Yes, the Swedish Act on Interest (*räntelagen*) provides a fall-back statutory right to interest on late payments in the absence of contrary contractual stipulations. Unless the parties have agreed on a different rate, the default interest rate will be the Swedish Central Bank's reference rate (which is determined semi-annually and which was set at -0.50% on 1 January 2017) with an addition of eight percentage points.

(c) A consumer has the right to withdraw from and cancel the credit within 14 days from the date of agreement or (if later) the date upon receipt of certain specified information and contractual documentation. In addition, the consumer generally has the right to repay the credit in advance ahead of schedule.

(d) Consumers are entitled to receive certain basic information (such as the identity of the creditor, the effective interest rate, fees, cancellation rights, etc.) in the standard European format and the contractual information in writing or another durable and retrievable medium. A consumer will retain the same right to set-off and the right to make the same objections against a transferee as it had towards the originator. It is not permitted to document consumer credit purchases as negotiable promissory notes.

1.3 Government Receivables. Where the receivables contract has been entered into with the government or a government agency, are there different requirements and laws that apply to the sale or collection of those receivables?

Government receivables are not subject to any specific regime in respect of sale or collection. However, public agencies of local, regional and central Government enjoy immunity from execution in Sweden (but not immunity from jurisdiction).

2 Choice of Law – Receivables Contracts

2.1 No Law Specified. If the seller and the obligor do not specify a choice of law in their receivables contract, what are the main principles in your jurisdiction that will determine the governing law of the contract?

The governing law of the contract of non-negotiable receivables will be determined in accordance with the Rome I Regulation. The basic principle is that the parties may choose the governing law of their contract. The choice shall be made expressly or clearly demonstrated by the terms of the contract or the circumstances of the case. By their choice the parties can select the law applicable to the whole or to only part of the contract. The parties may at any time agree to subject the contract to a law other than that which previously governed it, whether as a result of an earlier choice or of other provisions of the Regulation. Any change in the law to be applied that is made after the conclusion of the contract shall not prejudice its formal validity or adversely affect the rights of third parties. Where all other 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 the parties shall not prejudice the application of provisions of the law of that other country (including provisions of EU law, where appropriate, as implemented in a Member State) which cannot be derogated from by agreement.

The existence and validity of a contract, or of any term of a contract, shall be determined by the law which would govern it under the Regulation if the contract or term were valid. Nevertheless, a party,

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in order to establish that he did not consent, may rely upon the law of the country in which he has his habitual residence if it appears from the circumstances that it would not be reasonable to determine the effect of his conduct in accordance with the law specified in the preceding sentence. The form of consumer contracts shall be governed by the law of the country where the consumer has his habitual residence. In other cases, a contract concluded between persons who, or whose agents, are in the same country at the time of its conclusion is formally valid if it satisfies the formal requirements of the law which governs it in substance under the Regulation or of the law of the country where it is concluded. A contract concluded between persons who, or whose agents, are in different countries at the time of its conclusion is formally valid if it satisfies the formal requirements of the law which governs it in substance under the Regulation, or of the law of either of the countries where either of the parties or their agent is present at the time of conclusion, or of the law of the country where either of the parties had his habitual residence at that time. A unilateral act intended to have legal effect relating to an existing or contemplated contract is formally valid if it satisfies the formal requirements of the law which governs or would govern the contract in substance under the Regulation, or of the law of the country where the act was done, or of the law of the country where the person by whom it was done had his habitual residence at that time.

Notwithstanding the above, a contract (the subject matter of which is a right *in rem* in immovable property or a tenancy of immovable property) shall be subject to the requirements of form of the law of the country where the property is situated if by that law: (a) those requirements are imposed irrespective of the country where the contract is concluded and irrespective of the law governing the contract; and (b) those requirements cannot be derogated from by agreement.

In a contract concluded between persons who are in the same country, a natural person, who would have capacity under the law of that country, may invoke his incapacity resulting from the law of another country, only if the other party to the contract was aware of that incapacity at the time of the conclusion of the contract or was not aware thereof as a result of negligence.

The choice of law is limited in respect of consumer contracts, contracts of carriage, individual employment contracts and insurance contracts.

To the extent that the law applicable to the contract has not been chosen by the parties, the law governing the contract shall be determined, *inter alia*, as follows: (a) a contract for the sale of goods shall be governed by the law of the country where the seller has his habitual residence; (b) a contract for the provision of services shall be governed by the law of the country where the service provider has his habitual residence; (c) a contract relating to a right *in rem* in immovable property or to a tenancy of immovable property shall be governed by the law of the country where the property is situated; (d) a franchise contract shall be governed by the law of the country where the franchisee has his habitual residence; and (e) a distribution contract shall be governed by the law of the country where the distributor has his habitual residence. Where the contract is not covered by the preceding sentence or where the elements of the contract would be covered by more than one of the lettered points in that sentence, the contract shall be governed by the law of the country where the party required to effect the characteristic performance of the contract has his habitual residence. Where it is clear from all the circumstances of the case that the contract is manifestly more closely connected with a country other than that indicated in the preceding sentences, the law of that other country shall apply. Where the law applicable cannot be determined pursuant to the first two sentences in this paragraph, the contract shall be governed by the law of the country with which it is most closely connected.

2.2 Base Case. If the seller and the obligor are both resident in your jurisdiction, and the transactions giving rise to the receivables and the payment of the receivables take place in your jurisdiction, and the seller and the obligor choose the law of your jurisdiction to govern the receivables contract, is there any reason why a court in your jurisdiction would not give effect to their choice of law?

No, there is not.

2.3 Freedom to Choose Foreign Law of Non-Resident Seller or Obligor. If the seller is resident in your jurisdiction but the obligor is not, or if the obligor is resident in your jurisdiction but the seller is not, and the seller and the obligor choose the foreign law of the obligor/seller to govern their receivables contract, will a court in your jurisdiction give effect to the choice of foreign law? Are there any limitations to the recognition of foreign law (such as public policy or mandatory principles of law) that would typically apply in commercial relationships such as that between the seller and the obligor under the receivables contract?

As explained in the answer to question 2.1, according to the Rome I Regulation, a contract shall be governed by the law chosen by the parties. The parties' choice may, however, not prejudice the application of mandatory provisions of EU law; Swedish mandatory provisions will apply in the event that all relevant circumstances relate to Sweden; and the choice of law will not be upheld by a Swedish court if the provisions of that foreign law contravene Swedish *ordre public* or international mandatory provisions. The concept of *ordre public* is a dynamic one and cannot at any one time be fully specified. However, the Swedish courts have proved loath to invoke *ordre public* in practice. A Swedish court may also give effect to mandatory provisions of the law of the country where the performance of the contractual obligations will take place.

3 Choice of Law – Receivables Purchase Agreement

3.1 Base Case. Does your jurisdiction's law generally require the sale of receivables to be governed by the same law as the law governing the receivables themselves? If so, does that general rule apply irrespective of which law governs the receivables (i.e., your jurisdiction's laws or foreign laws)?

No, in respect of the receivables purchase agreement, the parties are generally free to choose a different law than the law governing the receivables. However, pursuant to the Rome I Regulation the relationship between assignor and assignee under a voluntary assignment shall be governed by the law that applies to the contract between the assignor and assignee under the Regulation. The law governing the assigned claim shall determine its *assignability*, the relationship between the assignee and the obligor, the conditions under which the assignment can be invoked against the obligor and whether the obligor's obligations have been discharged. The assignee and assignor cannot change the governing law or the terms of the agreement between assignor and obligor without the obligor's consent. The concept of "assignment" here includes

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outright transfers of claims, transfers of claims by way of security and pledges or other security rights over claims.

3.2 Example 1: If (a) the seller and the obligor are located in your jurisdiction, (b) the receivable is governed by the law of your jurisdiction, (c) the seller sells the receivable to a purchaser located in a third country, (d) the seller and the purchaser choose the law of your jurisdiction to govern the receivables purchase agreement, and (e) the sale complies with the requirements of your jurisdiction, will a court in your jurisdiction recognise that sale as being effective against the seller, the obligor and other third parties (such as creditors or insolvency administrators of the seller and the obligor)?

The relationship between the seller and the obligor (or the seller and the purchaser) is governed by the Rome I Regulation (as set out above). The relationship to third parties is not expressly addressed in Swedish statutory law. However, the predominant view is that applicable law will be the law of the country where the relevant asset is situated (the *lex rei sitae*) and that a receivable is "situated" in the obligor's domicile. A Swedish court would be likely to apply the perfection requirements set out in the substantive law of the obligor's domicile. The answers of Examples 1–5 below are based on this view. However, where the perfection requirements differ between the relevant jurisdictions, it is common as a precautionary matter to comply with the requirements in all relevant jurisdictions.

In Example 1, since the obligor is located in Sweden, a Swedish court would recognise a sale as being effective against third parties, provided that the sale has been properly perfected under Swedish law. As regards requirements for the sale to be perfected under Swedish law, please refer to the answers to questions 4.2 and 4.3.

3.3 Example 2: Assuming that the facts are the same as Example 1, but either the obligor or the purchaser or both are located outside your jurisdiction, will a court in your jurisdiction recognise that sale as being effective against the seller and other third parties (such as creditors or insolvency administrators of the seller), or must the foreign law requirements of the obligor's country or the purchaser's country (or both) be taken into account?

As set out in the answer to question 3.2, if the obligor is situated in a jurisdiction outside Sweden, it is likely that a Swedish court would conclude that the receivables are situated in the obligor's domicile, and, accordingly, that the law of that jurisdiction shall apply. Therefore, the sale will be effective against third parties only if the perfection requirements of that other jurisdiction have been respected.

3.4 Example 3: If (a) the seller is located in your jurisdiction but the obligor is located in another country, (b) the receivable is governed by the law of the obligor's country, (c) the seller sells the receivable to a purchaser located in a third country, (d) the seller and the purchaser choose the law of the obligor's country to govern the receivables purchase agreement, and (e) the sale complies with the requirements of the obligor's country, will a court in your jurisdiction recognise that sale as being effective against the seller and other third parties (such as creditors or insolvency administrators of the seller) without the need to comply with your jurisdiction's own sale requirements?

As set out in the answer to question 3.2, it is likely that a Swedish court would conclude that the perfection requirements should be subject to the substantive law of the obligor's domicile. Provided that the perfection requirements of that jurisdiction have been respected, a Swedish court would recognise the sale as being effective against third parties also for the purposes of Swedish law.

3.5 Example 4: If (a) the obligor is located in your jurisdiction but the seller is located in another country, (b) the receivable is governed by the law of the seller's country, (c) the seller and the purchaser choose the law of the seller's country to govern the receivables purchase agreement, and (d) the sale complies with the requirements of the seller's country, will a court in your jurisdiction recognise that sale as being effective against the obligor and other third parties (such as creditors or insolvency administrators of the obligor) without the need to comply with your jurisdiction's own sale requirements?

As set out in the answer to question 3.2, it is likely that a Swedish court will apply Swedish law since the obligor is located in Sweden. Accordingly, the sale will not be effective against third parties unless the Swedish perfection requirements have been respected.

3.6 Example 5: If (a) the seller is located in your jurisdiction (irrespective of the obligor's location), (b) the receivable is governed by the law of your jurisdiction, (c) the seller sells the receivable to a purchaser located in a third country, (d) the seller and the purchaser choose the law of the purchaser's country to govern the receivables purchase agreement, and (e) the sale complies with the requirements of the purchaser's country, will a court in your jurisdiction recognise that sale as being effective against the seller and other third parties (such as creditors or insolvency administrators of the seller, any obligor located in your jurisdiction and any third party creditor or insolvency administrator of any such obligor)?

As set out in the answer to question 3.2, it is likely that a Swedish court would base its analysis on the perfection requirements on the substantive law of the obligor's domicile.

4 Asset Sales

4.1 Sale Methods Generally. In your jurisdiction what are the customary methods for a seller to sell receivables to a purchaser? What is the customary terminology – is it called a sale, transfer, assignment or something else?

A variety of terms may be and are used, both in English and in Swedish. The most common ones are probably "assignment" (*överlåtelse*) or "sale" (*försäljning*). "Assignment" (in English) is sometimes also used to denote a security transfer (see the discussion in the answer to question 4.9).

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4.2 Perfection Generally. What formalities are required generally for perfecting a sale of receivables? Are there any additional or other formalities required for the sale of receivables to be perfected against any subsequent good faith purchasers for value of the same receivables from the seller?

Swedish law makes a distinction between receivables evidenced in negotiable and non-negotiable promissory notes for the purpose of the perfection requirements. In the case of non-negotiable promissory notes, a sale of receivables is perfected through notification to the obligor. In relation to receivables evidenced in negotiable promissory notes, the seller must deliver the original bearer document to the buyer or to a third party acting on the buyer's instructions.

While notification is not a requirement to perfect a sale of negotiable promissory notes, a buyer in the financial sector must (according to recent Supreme Court case law) inquire with the obligor before the transfer if the obligor has made any payment or reached any other settlement with the seller, which is not recorded on the promissory note. Should the buyer neglect to perform such an inquiry, it will bear the risk of the promissory note that may be encumbered by undisclosed earlier payments or settlements.

In respect of dematerialised instruments held according the rules of a Central Securities Depositary in Sweden, registration of the assignment (in respect of directly held instruments) on the CSD accounts or (in respect of instruments held through a nominee) notice to the nominee would be required for perfection.

4.3 Perfection for Promissory Notes, etc. What additional or different requirements for sale and perfection apply to sales of promissory notes, mortgage loans, consumer loans or marketable debt securities?

We refer to question 4.2 regarding the general perfection requirements for promissory notes, which also apply to mortgage loans, consumer loans and marketable debt securities.

If a negotiable promissory note is sold by a credit institution, or by an investment firm, the sale is perfected, notwithstanding that the promissory note has been left in the custody of the seller for safekeeping.

4.4 Obligor Notification or Consent. Must the seller or the purchaser notify obligors of the sale of receivables in order for the sale to be effective against the obligors and/or creditors of the seller? Must the seller or the purchaser obtain the obligors' consent to the sale of receivables in order for the sale to be an effective sale against the obligors? Whether or not notice is required to perfect a sale, are there any benefits to giving notice – such as cutting off obligor set-off rights and other obligor defences?

Yes, either the seller or buyer needs to notify the obligors, unless the relevant receivables are evidenced by negotiable promissory notes (in which case notification would still be recommended and common).

Unless the circumstances indicate otherwise, a contract that is silent on assignability will be taken to permit assignment. If assignment is expressly prohibited (or even prohibited by implication) the prohibition will be respected and any assignments made in contravention thereof would be void. In respect of receivables documented as non-negotiable promissory notes, notice would prevent the obligor from continuing to be able to discharge its obligations by paying to the seller. Notice will also, except for consumer credit contracts, cut off the obligor's right to set off a counterclaim against the purchaser if such counterclaim was (i) acquired after receipt of the notice, or (ii) if such counterclaim falls due for payment after both the receivable and receipt of the notice.

4.5 Notice Mechanics. If notice is to be delivered to obligors, whether at the time of sale or later, are there any requirements regarding the form the notice must take or how it must be delivered? Is there any time limit beyond which notice is ineffective – for example, can a notice of sale be delivered after the sale, and can notice be delivered after insolvency proceedings have commenced against the obligor or the seller? Does the notice apply only to specific receivables or can it apply to any and all (including future) receivables? Are there any other limitations or considerations?

There are no requirements to the form or method of delivery of the notice. However, the burden of proof lies with the sender, so the notice should be unambiguous and it should be verified that it is actually received by the obligor. It is common to send the notice by courier producing a receipt of delivery, which will be kept as evidence of the delivery.

The notice cannot be delivered after insolvency proceedings against the seller have commenced. The notice can be delivered after insolvency proceedings against the obligor have commenced, provided that the purchaser has time to make himself known as a creditor in the obligor's insolvency. The notice can apply also to future receivables, although it is arguable (on the basis of Supreme Court case law that is now regarded as being rather dated) that the notice would not become effective until the future receivables have been "earned" (or accrued).

4.6 Restrictions on Assignment – General Interpretation. Will a restriction in a receivables contract to the effect that "None of the [seller's] rights or obligations under this Agreement may be transferred or assigned without the consent of the [obligor]" be interpreted as prohibiting a transfer of receivables by the seller to the purchaser? Is the result the same if the restriction says "This Agreement may not be transferred or assigned by the [seller] without the consent of the [obligor]" (i.e., the restriction does not refer to rights or obligations)? Is the result the same if the restriction says "The obligations of the [seller] under this Agreement may not be transferred or assigned by the [seller] without the consent of the [obligor]" (i.e., the restriction does not refer to rights)?

Unless the circumstances indicate otherwise, contractual language prohibiting the assignment of the seller's rights or obligations under an agreement will be taken to mean that the rights may not and, therefore, cannot be assigned. Similarly, contractual language prohibiting the "agreement" from being assigned will also be construed as a prohibition against the assignment of the seller's rights, which, therefore, could not be assigned.

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4.7 Restrictions on Assignment; Liability to Obligor. If any of the restrictions in question 4.6 are binding, or if the receivables contract explicitly prohibits an assignment of receivables or "seller's rights" under the receivables contract, are such restrictions generally enforceable in your jurisdiction? Are there exceptions to this rule (e.g., for contracts between commercial entities)? If your jurisdiction recognises restrictions on sale or assignment of receivables and the seller nevertheless sells receivables to the purchaser, will either the seller or the purchaser be liable to the obligor for breach of contract or tort, or on any other basis?

Yes, such restrictions are generally enforceable with no general exceptions and assignments against explicit or clearly implied prohibitions will be void. The seller will be liable to the obligor for breach of contract.

4.8 Identification. Must the sale document specifically identify each of the receivables to be sold? If so, what specific information is required (e.g., obligor name, invoice number, invoice date, payment date, etc.)? Do the receivables being sold have to share objective characteristics? Alternatively, if the seller sells *all* of its receivables to the purchaser, is this sufficient identification of receivables? Finally, if the seller sells *all* of its receivables *other than* receivables owing by one or more specifically identified obligors, is this sufficient identification of receivables?

There are no requirements, except a general requirement that it must be possible to clearly identify the receivables being sold.

4.9 Recharacterisation Risk. If the parties describe their transaction in the relevant documents as an outright sale and explicitly state their intention that it be treated as an outright sale, will this description and statement of intent automatically be respected or is there a risk that the transaction could be characterised by a court as a loan with (or without) security? If recharacterisation risk exists, what characteristics of the transaction might prevent the transfer from being treated as an outright sale? Among other things, to what extent may the seller retain any of the following without jeopardising treatment as an outright sale: (a) credit risk; (b) interest rate risk; (c) control of collections of receivables; (d) a right of repurchase/redemption; (e) a right to the residual profits within the purchaser; or (f) any other term?

Swedish law accords central importance to the common intent of the parties in construing the meaning of a contract, having due regard to the justified expectations of the parties in the relevant circumstances. However, a Swedish court may also enquire into the economic characteristics of the transaction (often seeking to apply substance over form), which could lead to the recharacterisation of an intended sale (true sale) as a security assignment. However, as mentioned in the answer to question 5.1, the perfection requirements are substantially the same for both outright sales and security arrangements and the main result would not be that the sale/security is unperfected, but that the seller has right to any excess in the value of the receivables assigned over the purchase price.

The current state of the law does not allow a complete enumeration of all the elements that a Swedish court will assess in determining whether a sale is a true sale. However, it is clear that such a court would consider: each and all of the credit risks; the interest rate risk; the control of collections of receivables; and any right of repurchase/redemption. However, it is probably fair to say that if the seller retains the credit and interest rate risk, controls the collection of receivables (especially if collections are made in its own name) and it retains an option of repurchase, a Swedish court would be more inclined to reject a construction of the arrangement as a true sale, as all of those elements would not be easily reconciled with such a sale.

4.10 Continuous Sales of Receivables. Can the seller agree in an enforceable manner to continuous sales of receivables (i.e., sales of receivables as and when they arise)? Would such an agreement survive and continue to transfer receivables to the purchaser following the seller's insolvency?

Yes. However, it is arguable that, notwithstanding prospective notice having been given, the notice will only become effective once the receivables have been "earned" (see the answer to question 4.5). To the extent that this would occur after the commencement of the seller's bankruptcy, the transfer of receivables being "earned" in future would not be capable of perfection.

4.11 Future Receivables. Can the seller commit in an enforceable manner to sell receivables to the purchaser that come into existence after the date of the receivables purchase agreement (e.g., "future flow" securitisation)? If so, how must the sale of future receivables be structured to be valid and enforceable? Is there a distinction between future receivables that arise prior to *versus* after the seller's insolvency?

Yes, the answer is the same as the answer to question 4.10.

4.12 Related Security. Must any additional formalities be fulfilled in order for the related security to be transferred concurrently with the sale of receivables? If not all related security can be enforceably transferred, what methods are customarily adopted to provide the purchaser the benefits of such related security?

Receivables can usually be sold together with any related security. The assignment would be perfected in accordance with the relevant rules for negotiable or non-negotiable promissory notes and the transfer of the security would be perfected in the manner appropriate to the relevant kind of asset being used as security.

4.13 Set-Off; Liability to Obligor. Assuming that a receivables contract does not contain a provision whereby the obligor waives its right to set-off against amounts it owes to the seller, do the obligor's set-off rights terminate upon its receipt of notice of a sale? At any other time? If a receivables contract does not waive set-off but the obligor's set-off rights are terminated due to notice or some other action, will either the seller or the purchaser be liable to the obligor for damages caused by such termination?

The obligor will retain its set-off rights in respect of receivables documented as non-negotiable promissory notes. Exceptions to this rule are discussed in the answer to question 4.4. In respect of receivables documented as negotiable promissory notes, the set-off right generally terminates upon the perfected transfer of the notes. The due diligence requirements incumbent on buyers in the

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financial sector in respect of payments may also apply in respect of set-off. However, the obligor will retain the right to set-off if: (i) the counterclaim originates from the same legal relationship; or (ii) there is a risk that the obligor will not receive payment from the seller as a result of the transfer, and the purchaser was aware of the obligor's counterclaim and the effect that the transfer could have thereon. The obligor's set-off rights cannot be terminated by the seller or the purchaser other than as described above, and such termination will not make the seller or the purchaser liable for damages (although the obligor will still hold its counterclaim against the seller).

4.14 Profit Extraction. What methods are typically used in your jurisdiction to extract residual profits from the purchaser?

Profit is often extracted as fees for the provisioning of services (at arm's-length terms), holding of junior debt tranches, or deferred purchase price.

5 Security Issues

5.1 Back-up Security. Is it customary in your jurisdiction to take a "back-up" security interest over the seller's ownership interest in the receivables and the related security, in the event that an outright sale is deemed by a court (for whatever reason) not to have occurred and have been perfected (see question 4.9 above)?

No. Under Swedish law, the perfection requirements for a sale of receivables and the granting of a security interest over receivables are substantially the same.

5.2 Seller Security. If it is customary to take back-up security, what are the formalities for the seller granting a security interest in receivables and related security under the laws of your jurisdiction, and for such security interest to be perfected?

Please refer to the reply to questions 4.2 and 4.3 regarding the receivables, and to question 4.12 regarding related security.

5.3 Purchaser Security. If the purchaser grants security over all of its assets (including purchased receivables) in favour of the providers of its funding, what formalities must the purchaser comply with in your jurisdiction to grant and perfect a security interest in purchased receivables governed by the laws of your jurisdiction and the related security?

Under Swedish law, the perfection requirements for a sale of receivables and the granting of a security interest over receivables are substantially the same – these are described in the answers to questions 4.2 and 4.3. Please see the answer to question 4.12 in relation to related security.

For a Swedish pledgor, it is possible to grant security over substantially all of the pledgor's property (including receivables) through a pledge of corporate mortgages (*företagshypotek*). The corporate mortgage is, however, limited to the assets of the pledgor at the time of enforcement and up to the face amount of mortgage certificates issued in respect of the registration of the mortgage with an addition of 15%. A corporate mortgage ranks below more specific security interests (such as pledges) in assets for which they compete. Stamp duty, at a rate of 1% of the face amount of any corporate mortgage issued, will be payable. As stamp duty is frequently changed, the rate should always be checked before a transaction involving corporate mortgages is consummated.

5.4 Recognition. If the purchaser grants a security interest in receivables governed by the laws of your jurisdiction, and that security interest is valid and perfected under the laws of the purchaser's jurisdiction, will the security be treated as valid and perfected in your jurisdiction or must additional steps be taken in your jurisdiction?

The law governing the contractual elements of the receivables would, in principle, be independent of the law that applies to the perfection as against third parties of a security interest created over the receivables. If the obligor, or the negotiable promissory note, is situated outside Sweden and the security interest has been perfected in accordance with the laws of that place, the perfection would be recognised also for the purposes of Swedish law as long as the obligor or the promissory note is not permanently removed from that place. As Swedish law distinguishes between the initial perfection of a security interest, on the one hand, and the maintenance of that perfection over time, on the other, a change in the situation of the obligor or the negotiable promissory note after the initial perfection would entail a change in the law governing the maintenance of the perfection. Please refer to the answers to questions 4.2 and 4.3 for perfection requirements under Swedish law.

5.5 Additional Formalities. What additional or different requirements apply to security interests in or connected to insurance policies, promissory notes, mortgage loans, consumer loans or marketable debt securities?

The perfection requirement in relation to insurance policies is notification to the relevant insurance company.

The perfection requirements for promissory notes, loans and marketable debt securities are described in the answer to question 4.3.

5.6 Trusts. Does your jurisdiction recognise trusts? If not, is there a mechanism whereby collections received by the seller in respect of sold receivables can be held or be deemed to be held separate and apart from the seller's own assets (so that they are not part of the seller's insolvency estate) until turned over to the purchaser?

The concept of a trust is not recognised under Swedish law. However, there are various legal mechanisms (such as mandate/power of attorney and escrow) that can be used to largely replicate the common economic and practical effects of a trust.

5.7 Bank Accounts. Does your jurisdiction recognise escrow accounts? Can security be taken over a bank account located in your jurisdiction? If so, what is the typical method? Would courts in your jurisdiction recognise a foreign law grant of security (for example, an English law debenture) taken over a bank account located in your jurisdiction?

Swedish law recognises escrow accounts. The use of an escrow account will be governed by an agreement between the parties and the account bank.

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Security over bank accounts located in Sweden (that is, that are being maintained by a Swedish or foreign bank from a branch in Sweden) may be taken by entering into a pledge agreement and notifying the relevant account bank.

A Swedish court would require that Swedish perfection requirements with respect to bank accounts are met, regardless of any perfection actions taken under the English law debenture.

Please refer to the answer to question 5.9 regarding the use of bank accounts while subject to a pledge.

5.8 Enforcement over Bank Accounts. If security over a bank account is possible and the secured party enforces that security, does the secured party control all cash flowing into the bank account from enforcement forward until the secured party is repaid in full, or are there limitations? If there are limitations, what are they?

Yes. The account bank has set-off rights with respect to the cash held on the account, unless the bank has agreed to waive those rights.

5.9 Use of Cash Bank Accounts. If security over a bank account is possible, can the owner of the account have access to the funds in the account prior to enforcement without affecting the security?

No. The pledgor must be prevented from being able to make withdrawals or in any other way deal with monies credited to the pledged account. However, the pledgee may agree, on a case-by-case basis, to release amounts covered by the pledge (provided, however, that such agreement is not granted as a matter of course).

If the pledgor needs to access the funds in order to operate its day-to-day business, a common solution is to include a provision that the pledgor will only be cut off from access to the account upon the occurrence of an event of default (or similar). Such arrangement may be vulnerable to a claw-back action on the basis that the perfection of the security has been delayed (please refer to the answer to question 6.3).

6 Insolvency Laws

6.1 Stay of Action. If, after a sale of receivables that is otherwise perfected, the seller becomes subject to an insolvency proceeding, will your jurisdiction's insolvency laws automatically prohibit the purchaser from collecting, transferring or otherwise exercising ownership rights over the purchased receivables (a "stay of action")? If so, what generally is the length of that stay of action? Does the insolvency official have the ability to stay collection and enforcement actions until he determines that the sale is perfected? Would the answer be different if the purchaser is deemed to only be a secured party rather than the owner of the receivables?

There is no automatic stay of action and the bankruptcy administrator is not empowered to perform collection and enforcement actions whether in relation to perfected sales or in relation to security arrangements. Please refer to the answer to question 6.3 regarding claw-back.

6.2 Insolvency Official's Powers. If there is no stay of action, under what circumstances, if any, does the insolvency official have the power to prohibit the purchaser's exercise of its ownership rights over the receivables (by means of injunction, stay order or other action)?

The bankruptcy administrator does not have the power to prohibit the purchaser's exercise of its rights.

6.3 Suspect Period (Clawback). Under what facts or circumstances could the insolvency official rescind or reverse transactions that took place during a "suspect" or "preference" period before the commencement of the seller's insolvency proceedings? What are the lengths of the "suspect" or "preference" periods in your jurisdiction for (a) transactions between unrelated parties, and (b) transactions between related parties? If the purchaser is majority-owned or controlled by the seller or an affiliate of the seller, does that render sales by the seller to the purchaser "related party transactions" for purposes of determining the length of the suspect period? If a parent company of the seller guarantee's the performance by the seller of its obligations under contracts with the purchaser, does that render sales by the seller to the purchaser "related party transactions" for purposes of determining the length of the suspect period?

If a sale of receivables is effective on arm's-length terms, which means that the consideration is in line with the market valuation of the receivables and the other terms of the agreement are those of unrelated parties, there would normally not be any risk of claw-back. If the arrangement is recharacterised as a security arrangement (or is intended to be a security arrangement) the hardening period is three months for security granted for old debt or security where perfection has been delayed for a period that is often taken to be more than two weeks (although the matter has not been finally settled by case law) and the delay in granting or perfection of the security has not been "ordinary". An action can broadly be said not to be "ordinary" if it would not have been taken but for the impending insolvency of the debtor.

In order for a claw-back action – brought by the bankruptcy administrator or, exceptionally, the creditors – to be successful, the claimant(s) would have to prove that the sale had been effected in an improper manner resulting in: (a) one creditor being favoured in preference to the other creditors; *or* (b) the withdrawal of the seller's assets from the creditors; *or* (c) the increase of seller's debts. A successful action further requires that: (x) the seller was, or by the completion of the sale (alone or in combination with another related circumstance) became insolvent; *and* (y) the purchaser knew or ought to have known of the seller's insolvency and the circumstances rendering the action improper (a party connected to the obligor is deemed to have such knowledge, unless it can show that it is likely that it neither knew nor ought to have known about the relevant circumstances).

The claw-back period is five years from the "relevant date" (broadly the date when a petition for bankruptcy was filed) for unrelated parties. There are no limitations to the claw-back period for transactions between related parties. If the purchaser is majority-owned or controlled by the seller or an affiliate of the seller, the sales by the seller to the purchaser would constitute "related party transactions" for purposes of determining the length of the suspect

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period. Only the fact that a parent company of the seller guarantees the performance by the seller of its obligations under contracts with the purchaser would *not* render the sales "related party transactions" for purposes of determining the length of the suspect period.

6.4 Substantive Consolidation. Under what facts or circumstances, if any, could the insolvency official consolidate the assets and liabilities of the purchaser with those of the seller or its affiliates in the insolvency proceeding? If the purchaser is owned by the seller or by an affiliate of the seller, does that affect the consolidation analysis?

There are no provisions in Swedish law providing for substantive consolidation. Each company will be strictly treated as an isolated economic entity. The courts may even appoint different administrators to the various companies in a group. It does therefore not matter whether the purchaser is owned by the seller or an affiliate of the seller.

6.5 Effect of Insolvency on Receivables Sales. If insolvency proceedings are commenced against the seller in your jurisdiction, what effect do those proceedings have on (a) sales of receivables that would otherwise occur after the commencement of such proceedings, or (b) on sales of receivables that only come into existence after the commencement of such proceedings?

If an agreement regarding the sale of receivables (existing or future) has been entered into between the seller and the purchaser, but the sale has not been completed prior to the commencement of insolvency proceedings against the seller, the agreement would not automatically be terminated. The bankruptcy estate may, at the bankruptcy administrator's discretion, choose to make the bankruptcy estate a party to the agreement in its own right and complete the sale, on the one hand, or to refrain from fulfilling the agreement, on the other. Should the administrator choose to make the estate party to the contract, the purchaser's rights as to performance arising after that point in time would be treated with preference to other claims against the estate. If the bankruptcy estate does not enter into the agreement within a reasonable time after the purchaser's demand that it do so, the purchaser may terminate the contract. If the purchaser would wish to continue to purchase receivables also after that termination, a new agreement would have to be made with the bankruptcy estate.

6.6 Effect of Limited Recourse Provisions. If a debtor's contract contains a limited recourse provision (see question 7.3 below), can the debtor nevertheless be declared insolvent on the grounds that it cannot pay its debts as they become due?

The question of whether the debtor can or cannot pay its debts as they fall due, and such incapacity is not merely temporary (which is the insolvency test under Swedish law), is a matter of fact and not of law and, as such, will need to be proved by the production of relevant evidence. It is not possible to exclude insolvency as a matter of principle by using any particular contractual language. However, creditors may, by appropriately restricting the debtor's business activities (and assuming that the debtor adheres to those restrictions), reduce the likelihood that the circumstances that would constitute insolvency for the debtor would arise.

7 Special Rules

7.1 Securitisation Law. Is there a special securitisation law (and/or special provisions in other laws) in your jurisdiction establishing a legal framework for securitisation transactions? If so, what are the basics? Is there a regulatory authority responsible for regulating securitisation transactions in your jurisdiction?

In principle no, but the EU Capital Requirements Regulation includes complex provisions regarding capital adequacy and exposure requirements in connection with securitisation. The authorisation requirements and the exemptions (please refer to the authorisation requirements in the answer to question 8.1) are policed by the Swedish Financial Supervisory Authority (*Finansinspektionen*) (the "**SFSA**").

7.2 Securitisation Entities. Does your jurisdiction have laws specifically providing for establishment of special purpose entities for securitisation? If so, what does the law provide as to: (a) requirements for establishment and management of such an entity; (b) legal attributes and benefits of the entity; and (c) any specific requirements as to the status of directors or shareholders?

No. However, please also refer to the authorisation requirements in the answer to question 8.1.

7.3 Location and form of Securitisation Entities. Is it typical to establish the special purpose entity in your jurisdiction or offshore? If in your jurisdiction, what are the advantages to locating the special purpose entity in your jurisdiction? If offshore, where are special purpose entities typically located for securitisations in your jurisdiction? What are the forms that the special purpose entity would normally take in your jurisdiction and how would such entity usually be owned?

Securitisation Entities are located both onshore and offshore. Onshore vehicles, however, have either to be credit institutions or be exempt from authorisation (see further the answer to question 8.1). The exemption limits the number of transactions for which the Securitisation Entity can be used. The limit is not entirely clear but is usually taken to be three. It is common to use a series of Securitisation Entities, each of which will be used for three transactions. Offshore entities are often located in the Channel Islands.

7.4 Limited-Recourse Clause. Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) limiting the recourse of parties to that agreement to the available assets of the relevant debtor, and providing that to the extent of any shortfall the debt of the relevant debtor is extinguished?

Yes, it will.

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7.5 Non-Petition Clause. Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) prohibiting the parties from: (a) taking legal action against the purchaser or another person; or (b) commencing an insolvency proceeding against the purchaser or another person?

Yes. It will most likely be tried but the court will respect the non-petition provision.

7.6 Priority of Payments "Waterfall". Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) distributing payments to parties in a certain order specified in the contract?

Outside bankruptcy, contractual provisions on a payments waterfall will be respected on the terms of any other contractual provisions. In bankruptcy, the waterfall arrangements will remain in force as a matter of contract but will not bind the bankruptcy administrator, in the sense that he will be permitted (and arguably obliged) to make payments of the bankruptcy dividend in accordance with the statutory order.

7.7 Independent Director. Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) or a provision in a party's organisational documents prohibiting the directors from taking specified actions (including commencing an insolvency proceeding) without the affirmative vote of an independent director?

The directors owe certain fiduciary duties towards the company. To the extent that the provision forces a director to act in breach of such fiduciary duties, such provision may be held invalid by a Swedish court. A petition to commence insolvency proceedings can be made either by a creditor to the extent its claims are unsecured or by a simple majority decision by the board of directors.

7.8 Location of Purchaser. Is it typical to establish the purchaser in your jurisdiction or offshore? If in your jurisdiction, what are the advantages to locating the purchaser in your jurisdiction? If offshore, where are purchasers typically located for securitisations in your jurisdiction?

Historically, the purchaser has often been established offshore. For transparency reasons, to avoid reputational risks that may be associated with offshore transactions and to reduce complexity by limiting the number of involved jurisdictions, it has become more common to establish the purchaser in Sweden. The most commonly used offshore jurisdictions for the establishment of the purchaser are Jersey and Ireland.

8 Regulatory Issues

8.1 Required Authorisations, etc. Assuming that the purchaser does no other business in your jurisdiction, will its purchase and ownership or its collection and enforcement of receivables result in its being required to qualify to do business or to obtain any licence or its being subject to regulation as a financial institution in your jurisdiction? Does the answer to the preceding question change if the purchaser does business with more than one seller in your jurisdiction?

Under Swedish law, an entity whose business plan includes "financing business" (*finansieringsrörelse*) requires authorisation as a credit institution from the SFSA. An entity is regarded as engaging in financing business if it intends (i) to receive repayable funds from the public, and (ii) to provide credit, provide security for credit or acquire receivables or lease movable property for financing purposes. An entity engaged in securitisation by acquiring receivables and issuing bonds or notes will, as a main rule, be regarded as engaging in financing business. However, an exemption from the licensing requirement is available for securitisation vehicles that will not raise funds on a "regular basis" (which is believed to mean up to three to five issuances of notes).

The SFSA were, further, of the opinion that if the bonds or notes are issued under an approved prospectus no authorisation would be needed, regardless of whether the company will raise funds on a regular basis and, on some occasions at least, regardless of whether the issuer is Swedish. The SFSA has also on occasion been of the opinion that no authorisation would be required where no prospectus has been published because the securitisation vehicle's issuance benefits from an exemption from the prospectus rules. However, in January 2017 the SFSA stated privately to a number of prominent law firms in Stockholm that it has now revised its views in this regard and that the "prospectus-based exemption" would no longer be available. Given the uncertainty that has ensued as a result, it is generally prudent to obtain a fresh statement from the SFSA on the particular facts of any particular securitisation until more stable guidance is available.

8.2 Servicing. Does the seller require any licences, etc., in order to continue to enforce and collect receivables following their sale to the purchaser, including to appear before a court? Does a third-party replacement servicer require any licences, etc., in order to enforce and collect sold receivables?

Subject to the factual circumstances of each case, the seller replacement servicer could be required to obtain authorisation from the Swedish Data Protection Authority under the Swedish Debt Recovery Act. As a main rule, such authorisation would be required for the enforcement and collection of receivables on behalf of others, or for the collection of receivables that have been taken over for collection. Entities subject to the SFSA's supervision and admitted attorneys at law (*advokater*) are exempted from the licensing requirement.

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8.3 Data Protection. Does your jurisdiction have laws restricting the use or dissemination of data about or provided by obligors? If so, do these laws apply only to consumer obligors or also to enterprises?

The Swedish Personal Data Act applies to all processing (directly and indirectly) of personal data relating to natural persons, including consumer debtors. "Processing" in this context includes, among other things, collection and transfer of personal data. Processing must be in accordance with the requirements under the act. Generally, the affected individual has to give its consent to the processing. An exemption is made where the processor's (or a third party's) interest outweighs the interest in protection of the personal data of the person whose data is being processed.

8.4 Consumer Protection. If the obligors are consumers, will the purchaser (including a bank acting as purchaser) be required to comply with any consumer protection law of your jurisdiction? Briefly, what is required?

Consumer credits are subject to certain mandatory rules under the Swedish Consumer Credit Act, which will apply also to someone acquiring such assets. Please see further the answer to question 1.2.

8.5 Currency Restrictions. Does your jurisdiction have laws restricting the exchange of your jurisdiction's currency for other currencies or the making of payments in your jurisdiction's currency to persons outside the country?

Sweden does not operate any general exchange controls. However, particular transactions may be prohibited by sanctions imposed by the United Nations and/or the European Union.

8.6 Risk Retention. Does your jurisdiction have laws or regulations relating to "risk retention"? How are securitisation transactions in your jurisdiction usually structured to satisfy those risk retention requirements?

There is no general risk retention requirement under Swedish law. However, credit institutions, investment firms and insurance undertakings are themselves subject to risk retention requirements when they securitise and they may only invest in securitisation positions issued by credit institutions and investment firms where the issuer has retained risk, in all cases as stipulated by EU law (the Capital Requirements Regulation and the Solvency II Directive).

8.7 Regulatory Developments. Have there been any regulatory developments in your jurisdiction which are likely to have a material impact on securitisation transactions in your jurisdiction?

Recent regulatory developments have been outlined in our answer to question 8.1. The SFSA has rejected arguments, based on EU law, that securitisation vehicles should not be regarded and treated as credit institutions.

9 Taxation

9.1 Withholding Taxes. Will any part of payments on receivables by the obligors to the seller or the purchaser be subject to withholding taxes in your jurisdiction? Does the answer depend on the nature of the receivables, whether they bear interest, their term to maturity, or where the seller or the purchaser is located? In the case of a sale of trade receivables at a discount, is there a risk that the discount will be recharacterised in whole or in part as interest? In the case of a sale of trade receivables where a portion of the purchase price is payable upon collection of the receivable, is there a risk that the deferred purchase price will be recharacterised in whole or in part as interest? If withholding taxes might apply, what are the typical methods for eliminating or reducing withholding taxes?

No. Sweden does not apply any withholding taxes on interest payments or other payments on receivables in the context of securitisation. It is immaterial if a discount or a deferred purchase price is recharacterised as interest for the purpose of withholding taxation.

9.2 Seller Tax Accounting. Does your jurisdiction require that a specific accounting policy is adopted for tax purposes by the seller or purchaser in the context of a securitisation?

No, it does not.

9.3 Stamp Duty, etc. Does your jurisdiction impose stamp duty or other transfer or documentary taxes on sales of receivables?

No, it does not.

9.4 Value Added Taxes. Does your jurisdiction impose value added tax, sales tax or other similar taxes on sales of goods or services, on sales of receivables or on fees for collection agent services?

Sweden imposes a value added tax (*moms*) (VAT) on almost all consumption of goods and services. The standard tax rate is 25% of the price before VAT. It should be noted that transactions in financial instruments, such as receivables, are exempt from VAT. However, factoring services and services conducted by a collection agent are still liable to VAT.

9.5 Purchaser Liability. If the seller is required to pay value-added tax, stamp duty or other taxes upon the sale of receivables (or on the sale of goods or services that give rise to the receivables) and the seller does not pay, then will the taxing authority be able to make claims for the unpaid tax against the purchaser or against the sold receivables or collections?

No, it will not.

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9.6 Doing Business. Assuming that the purchaser conducts no other business in your jurisdiction, would the purchaser's purchase of the receivables, its appointment of the seller as its servicer and collection agent, or its enforcement of the receivables against the obligors, make it liable to tax in your jurisdiction?

The threshold question of whether a foreign enterprise is liable to pay taxes in Sweden is whether it is deemed to have a permanent establishment in the country. Accordingly, a purchaser, which is not considered to have a permanent establishment in Sweden, is not liable to pay Swedish taxes. In a normal securitisation transaction, tax liability will ordinarily not arise where the purchaser is a non-Swedish entity and the seller acts in its own name and in the ordinary course of its business.

9.7 Taxable Income. If a purchaser located in your jurisdiction receives debt relief as the result of a limited recourse clause (see question 7.3 above), is that debt relief liable to tax in your jurisdiction?

If the debt is written off (and not just postponed), the debt relief will in most situations be taxed as income. There are, however, certain exemptions for debt relief executed through a formal debt composition procedure (*ackord*) or if the purchaser is deemed to be insolvent.

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Switzerland

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1 Receivables Contracts

1.1 Formalities. In order to create an enforceable debt obligation of the obligor to the seller: (a) is it necessary that the sales of goods or services are evidenced by a formal receivables contract; (b) are invoices alone sufficient; and (c) can a binding contract arise as a result of the behaviour of the parties?

Swiss law does not require a specific form for entering into contracts. Accordingly, in order to create an enforceable debt obligation of the obligor to the seller, (a) it is not necessary that the sales of goods or services are evidenced by a formal contract, (b) invoices are sufficient (but not necessarily required) and (c) a binding contract can arise by oral agreement or even as a result of the behaviour of the parties. However, certain contracts require written form by law (e.g. consumer credit agreements) and we note that, as a matter of fact and for evidence purposes, it is standard to enter into written form agreements.

1.2 Consumer Protections. Do your jurisdiction's laws: (a) limit rates of interest on consumer credit, loans or other kinds of receivables; (b) provide a statutory right to interest on late payments; (c) permit consumers to cancel receivables for a specified period of time; or (d) provide other noteworthy rights to consumers with respect to receivables owing by them?

Credit agreements with private persons that are not business related with a loan amount between CHF 500 and CHF 80,000 are subject to the Swiss Consumer Credit Act (CCA). Under the CCA and the related ordinances, rates of interest on consumer credit loans are limited; for overdraft facilities on current accounts and credit cards (with a credit option) the limit is 12% p.a. and for other general consumer credit products governed by the CCA, the limit is 10% p.a. Outside of the scope of the CCA, case law provides for a limitation of 18% p.a. under the rules on usury. Late payments are subject to a default interest of 5% p.a., unless the contractual interest is higher, in which case such contractual interest will continue to apply. It should be noted that an obligor who is in default with the payment of interest must only pay default interest (*Verzugszinsen*) thereon from the day of the demand for official debt enforcement or the filing of a legal action. An agreement to the contrary is to be considered by a Swiss court in accordance with the principles on liquidated damages (*Konventionalstrafe*). Further, no default interest (*Verzugszinsen*) shall be calculated on default interest. The borrower under a consumer credit agreement (subject to the CCA) may withdraw from the contract within 14 days following it having received its original counterpart of the contract. This concern is normally addressed by designing the eligibility criteria to ensure that only receivables, for which the withdrawal period has lapsed are eligible. Consumers have the benefit of further rights, such as special set-off rights (if relevant) or increased standards for contractual waivers (e.g. on banking secrecy, data protection). In addition, mandatory place of jurisdictions apply.

1.3 Government Receivables. Where the receivables contract has been entered into with the government or a government agency, are there different requirements and laws that apply to the sale or collection of those receivables?

This depends on the role under which the government is acting. Whilst the general legal framework for those receivables is the same, enforcement of receivables relating to public assets (*Verwaltungsvermögen*) is limited.

2 Choice of Law – Receivables Contracts

2.1 No Law Specified. If the seller and the obligor do not specify a choice of law in their receivables contract, what are the main principles in your jurisdiction that will determine the governing law of the contract?

To the extent only Swiss parties are involved and absent specific circumstances, Swiss law will apply. In cross-border scenarios, the governing law is to be determined under the Swiss Private International Law Act (PILA). Absent a choice of law clause, a contract will be governed by the laws of the country, with which the contract is "most closely connected". Generally, this is the place of jurisdiction of the party providing the typical consideration for a contract (e.g. sale of assets, the seller; rendering of services, the service provider, etc.). Specific rules apply with regards to real estate, consumer contracts, employment contracts to property and contracts on movable goods.

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2.2 Base Case. If the seller and the obligor are both resident in your jurisdiction, and the transactions giving rise to the receivables and the payment of the receivables take place in your jurisdiction, and the seller and the obligor choose the law of your jurisdiction to govern the receivables contract, is there any reason why a court in your jurisdiction would not give effect to their choice of law?

No, there is no obvious reason (absent abuse of rights and similar circumstances) why a court in Switzerland should not give effect to the choice of law.

2.3 Freedom to Choose Foreign Law of Non-Resident Seller or Obligor. If the seller is resident in your jurisdiction but the obligor is not, or if the obligor is resident in your jurisdiction but the seller is not, and the seller and the obligor choose the foreign law of the obligor/seller to govern their receivables contract, will a court in your jurisdiction give effect to the choice of foreign law? Are there any limitations to the recognition of foreign law (such as public policy or mandatory principles of law) that would typically apply in commercial relationships such as that between the seller and the obligor under the receivables contract?

Yes, under the PILA, parties are generally free to agree in relation to the choice of law. A choice of law must be explicit or, if implicit, be obvious. Swiss courts would give effect to such choice of law, subject to the following limitations:

- a free choice of law is only possible in international matters; and
- a Swiss court (i) will not apply a provision of foreign law if and to the extent that this would, in the court's or authority's view, lead to a result violating Swiss public policy (*ordre public*) or similar general principles, (ii) will apply, notwithstanding a valid choice of law by the parties, any provisions of Swiss law (and, subject to further conditions, of another foreign law) which in the court's or authority's view imperatively demand application in view of their specific purpose (*lois d'application immédiate*), (iii) can find that provisions of a law other than the law chosen by the parties is applicable if important reasons call for such applicability and if the facts are closely linked to such other law, and (iv) will apply Swiss procedural rules; furthermore, a choice of law may not extend to non-contractual obligations.

3 Choice of Law – Receivables Purchase Agreement

3.1 Base Case. Does your jurisdiction's law generally require the sale of receivables to be governed by the same law as the law governing the receivables themselves? If so, does that general rule apply irrespective of which law governs the receivables (i.e., your jurisdiction's laws or foreign laws)?

Generally, parties to a receivables purchase and sale agreement are free with regard to the choice of law. The sale of receivables can be governed by a law other than the governing law of the receivable. However, the sale and purchase always entails the assignment of the receivable and according to Swiss conflict of law rules, the choice of law made by an assignor and an assignee under an assignment agreement with respect to the assignment of claims or receivables under a contract may not be ascertained against the obligor without such obligor's consent (article 145 para. 1 PILA). Hence, from a Swiss perspective and as a basic rule, it is standard that the sale of receivables is governed by the same law as the law governing the receivable.

3.2 Example 1: If (a) the seller and the obligor are located in your jurisdiction, (b) the receivable is governed by the law of your jurisdiction, (c) the seller sells the receivable to a purchaser located in a third country, (d) the seller and the purchaser choose the law of your jurisdiction to govern the receivables purchase agreement, and (e) the sale complies with the requirements of your jurisdiction, will a court in your jurisdiction recognise that sale as being effective against the seller, the obligor and other third parties (such as creditors or insolvency administrators of the seller and the obligor)?

Yes. The parties are free to choose any law and given that the receivable is governed by the same law, such choice of law may also be asserted against the obligor.

3.3 Example 2: Assuming that the facts are the same as Example 1, but either the obligor or the purchaser or both are located outside your jurisdiction, will a court in your jurisdiction recognise that sale as being effective against the seller and other third parties (such as creditors or insolvency administrators of the seller), or must the foreign law requirements of the obligor's country or the purchaser's country (or both) be taken into account?

Yes. The parties are free to choose any law and given that the receivable is governed by the same law, such choice of law may also be asserted against the obligor. From a Swiss perspective, any foreign law requirements of the obligor's country or the purchaser's country there would be irrelevant.

3.4 Example 3: If (a) the seller is located in your jurisdiction but the obligor is located in another country, (b) the receivable is governed by the law of the obligor's country, (c) the seller sells the receivable to a purchaser located in a third country, (d) the seller and the purchaser choose the law of the obligor's country to govern the receivables purchase agreement, and (e) the sale complies with the requirements of the obligor's country, will a court in your jurisdiction recognise that sale as being effective against the seller and other third parties (such as creditors or insolvency administrators of the seller) without the need to comply with your jurisdiction's own sale requirements?

Yes, subject to the general principles outlined in the answer to question 2.3. The parties are free to choose any law and given that the receivable is governed by the same law, such choice of law may also be asserted against the obligor.

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3.5 Example 4: If (a) the obligor is located in your jurisdiction but the seller is located in another country, (b) the receivable is governed by the law of the seller's country, (c) the seller and the purchaser choose the law of the seller's country to govern the receivables purchase agreement, and (d) the sale complies with the requirements of the seller's country, will a court in your jurisdiction recognise that sale as being effective against the obligor and other third parties (such as creditors or insolvency administrators of the obligor) without the need to comply with your jurisdiction's own sale requirements?

Yes, subject to the general principles outlined in the answer to question 2.3. The parties are free to choose any law and given that the receivable is governed by the same law, such choice of law may also be asserted against the obligor.

3.6 Example 5: If (a) the seller is located in your jurisdiction (irrespective of the obligor's location), (b) the receivable is governed by the law of your jurisdiction, (c) the seller sells the receivable to a purchaser located in a third country, (d) the seller and the purchaser choose the law of the purchaser's country to govern the receivables purchase agreement, and (e) the sale complies with the requirements of the purchaser's country, will a court in your jurisdiction recognise that sale as being effective against the seller and other third parties (such as creditors or insolvency administrators of the seller, any obligor located in your jurisdiction and any third party creditor or insolvency administrator of any such obligor)?

Technically yes, subject to the general principles outlined in the answer to question 2.3. However, the choice of law may not be asserted against the obligor, unless the obligor consented to such choice of law. Accordingly, in such cases, it is preferable to choose the law governing the receivable as the governing law of the receivables purchase agreement. Alternatively, the requirements of Swiss law could be complied with or the consent of the obligor could be obtained.

4 Asset Sales

4.1 Sale Methods Generally. In your jurisdiction what are the customary methods for a seller to sell receivables to a purchaser? What is the customary terminology – is it called a sale, transfer, assignment or something else?

The seller and purchaser typically enter into a written receivables purchase agreement under which the seller agrees to sell and assign and the purchaser agrees to purchase and assume the assignment of the receivables. The actual "assignment" is performed by the seller assigning the receivables in written form. The assignment declaration can be embedded in an assignment clause in the receivables purchase agreement. Depending on the nature of the receivables, receivables purchase agreements sometimes foresee that separate offer letters are provided, containing the actual assignment clause.

In terms of terminology, the agreement is normally called the "receivables purchase agreement" and the actual transfer of the receivables is called the "assignment".

4.2 Perfection Generally. What formalities are required generally for perfecting a sale of receivables? Are there any additional or other formalities required for the sale of receivables to be perfected against any subsequent good faith purchasers for value of the same receivables from the seller?

The agreement on the sale and assignment of a receivable must be in writing and must bear the signature of the seller/assignor; however, it is standard practice that the receivables purchase agreement is signed by both parties.

In order for the assignment to be valid, the receivable has to be assignable. In case the underlying agreement relating to the receivable is silent on the question of the assignability and does not contain a ban on assignment, the receivable is freely assignable. Even though not required by law, underlying agreements (e.g. in the general terms and conditions) often contain clauses confirming the assignability of the receivables. In addition, an assignment can be prohibited by law or the nature of the receivables. However, this is only the case in rather exceptional cases (e.g. claims relating to alimonies, etc.). Also future receivables can be assigned, provided that the receivables are identifiable when coming into existence (see also question 4.8). Finally, conditional receivables are assignable as well. A notification of the obligor is not required for purposes of perfecting the assignment, but please refer to question 4.4 below.

4.3 Perfection for Promissory Notes, etc. What additional or different requirements for sale and perfection apply to sales of promissory notes, mortgage loans, consumer loans or marketable debt securities?

Promissory notes: As for the assignment of any other receivable, a valid assignment in writing is required. Whilst some legal scholars claim that the promissory note (*einfacher Schuldschein*) would have to be physically transferred by the assignor to the assignee, a (what seems to be) majority takes a different approach.

Mortgage loans: The assignment of mortgage loans receivables as such requires an assignment in writing. Essentially all mortgage loans are secured by mortgage notes (*Schuldbriefe*); whilst the concept of a mortgage (*Grundpfandverschreibung*) still exists, the volume of mortgage loans secured by a mortgage (*Grundpfandverschreibung*) is rather limited. The assignment of the security provided by way of mortgage note requires the physical delivery of the mortgage notes (in case of the registered mortgage notes, duly endorsed to the assignee (or any formal nominee, acting on its behalf)) or, in the case of register mortgage notes, the registration of the assignee (or any formal nominee, acting on its behalf) as creditor in the land register. There are strong arguments to say that in the case of a pledge over the mortgage notes (rather than a transfer for security purposes), the pledge security would be transferred even without physical transfer on the basis of the concept of accessoriness. However, the factual relevance is rather limited, given that essentially all standard terms and conditions of banks provide for a transfer for security purposes over mortgage notes.

Consumer loans: Unless debt securities or promissory notes have been issued with regard to consumer loans, no specific requirements apply to consumer loans (see also questions 4.2 and 4.3 above).

Marketable debt securities: A transfer of the debt securities is required by either physical delivery (in the case of registered debt securities, duly endorsed in blank or to the assignee) and in the case of intermediated book-entry securities, a proper transfer or instruction to the custodian.

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4.4 Obligor Notification or Consent. Must the seller or the purchaser notify obligors of the sale of receivables in order for the sale to be effective against the obligors and/or creditors of the seller? Must the seller or the purchaser obtain the obligors' consent to the sale of receivables in order for the sale to be an effective sale against the obligors? Whether or not notice is required to perfect a sale, are there any benefits to giving notice – such as cutting off obligor set-off rights and other obligor defences?

Provided that the underlying agreements between the obligors and the seller allow for the free assignment and transfer of the receivables, the obligors do not need to be informed of the assignment and sale. However, prior to notification, the obligors may validly discharge their obligations by paying to the seller (acting on an undisclosed basis as servicer) and in the event of bankruptcy of the seller, such payments would form part of the bankrupt estate of the seller, until the obligors are notified. Also, a valid and unconditional assignment and transfer to the purchaser requires that the purchaser may notify the obligors at any point in time, even when it is the general understanding of the parties that obligors shall only be notified upon occurrence of a specific notification event. To be on the safe side, it is recommended that names and addresses of obligors are provided to the purchaser.

In case the underlying agreement does contain a ban on assignment, obligors' consent must be obtained.

A notification of an obligor is required to cut-off obligors' set-off rights and defences. The obligor may raise any defence it has against the seller also against the purchaser, in case such defence was available already upon the obligor being notified of the assignment. A similar analysis applies to set-off (see also question 4.13).

Whilst it is beneficial to notify obligors as early as possible, we note that under transactions involving the securtisation of a granular portfolio with a larger number of obligors, obligors are normally not notified prior to a predefined trigger event.

4.5 Notice Mechanics. If notice is to be delivered to obligors, whether at the time of sale or later, are there any requirements regarding the form the notice must take or how it must be delivered? Is there any time limit beyond which notice is ineffective – for example, can a notice of sale be delivered after the sale, and can notice be delivered after insolvency proceedings have commenced against the obligor or the seller? Does the notice apply only to specific receivables or can it apply to any and all (including future) receivables? Are there any other limitations or considerations?

No specific requirements as to form apply to notices. However, for evidence purposes, it is highly recommended to send out notices by registered mail or courier; ideally, the purchaser is provided with an acknowledgment of receipt. Notices may be sent out at any point in time.

4.6 Restrictions on Assignment – General Interpretation. Will a restriction in a receivables contract to the effect that "None of the [seller's] rights or obligations under this Agreement may be transferred or assigned without the consent of the [obligor]" be interpreted as prohibiting a transfer of receivables by the seller to the purchaser? Is the result the same if the restriction says "This Agreement may not be transferred or assigned by the [seller] without the consent of the [obligor]" (i.e., the restriction does not refer to rights or obligations)? Is the result the same if the restriction says "The obligations of the [seller] under this Agreement may not be transferred or assigned by the [seller] without the consent of the [obligor]" (i.e., the restriction does not refer to rights)?

Yes, the assignment of receivables stemming from any receivables contract containing such type of restrictions requires the obligor's consent. As the interpretation of such restrictions will have to be done on case-by-case basis, it could be argued that the assignment of receivables is permissible and the restriction was meant to restrict a transfer of the entire agreement only. However, such analysis would be rather vague and hardly acceptable to investors or rating agencies.

4.7 Restrictions on Assignment; Liability to Obligor. If any of the restrictions in question 4.6 are binding, or if the receivables contract explicitly prohibits an assignment of receivables or "seller's rights" under the receivables contract, are such restrictions generally enforceable in your jurisdiction? Are there exceptions to this rule (e.g., for contracts between commercial entities)? If your jurisdiction recognises restrictions on sale or assignment of receivables and the seller nevertheless sells receivables to the purchaser, will either the seller or the purchaser be liable to the obligor for breach of contract or tort, or on any other basis?

Yes, such restrictions are valid and enforceable in Switzerland. Only in case the purchaser has been provided with a written acknowledgment of debt by the obligor not containing a reference to any ban on assignment, the purchaser may rely on the free assignability of the receivable. It should be noted that a ban on assignment contained in the underlying agreement results in the assignment simply not being effective. The seller might, subject to other requirements, become subject to contractual liability or liable on the basis of tort.

4.8 Identification. Must the sale document specifically identify each of the receivables to be sold? If so, what specific information is required (e.g., obligor name, invoice number, invoice date, payment date, etc.)? Do the receivables being sold have to share objective characteristics? Alternatively, if the seller sells *all* of its receivables to the purchaser, is this sufficient identification of receivables? Finally, if the seller sells *all* of its receivables *other than* receivables owing by one or more specifically identified obligors, is this sufficient identification of receivables?

For an assignment to be valid under Swiss law, it is not required that the sale document does specifically identify each single receivable, but the description of the current and future receivables must be

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drafted such that each relevant receivable is identifiable (in the case of future receivables only upon it coming into existence). Whether or not the description is sufficient so that the receivables are identifiable must be determined on a case-by-case basis. Excluding specific obligors is unlikely to cut across the analysis as to whether or not a receivable is identifiable. However, generally speaking, a receivable is considered to be identifiable in case the obligor, the underlying legal basis and the amount of the receivable can be determined. Consequently, it is a prudent approach to request receivables lists (containing the relevant information) prior to a sale of the receivables or to request periodic delivery of receivables list.

4.9 Recharacterisation Risk. If the parties describe their transaction in the relevant documents as an outright sale and explicitly state their intention that it be treated as an outright sale, will this description and statement of intent automatically be respected or is there a risk that the transaction could be characterised by a court as a loan with (or without) security? If recharacterisation risk exists, what characteristics of the transaction might prevent the transfer from being treated as an outright sale? Among other things, to what extent may the seller retain any of the following without jeopardising treatment as an outright sale: (a) credit risk; (b) interest rate risk; (c) control of collections of receivables; (d) a right of repurchase/redemption; (e) a right to the residual profits within the purchaser; or (f) any other term?

There are no statutory or case law-based tests as to when a securitisation transaction qualifies as an effective sale or as a secured loan. The sole designation of a transaction as a true sale does not help, as courts would always analysis the effective mutual intent of the parties.

Whilst no statutory or case law exists, the following elements should be considered, even though each of these elements itself is unlikely to be a decisive element:

- courts are likely to look at the at arm's length analysis of each sale of a receivable;
- the credit risk as such should be transferred to the purchaser;
- the control of collections by the seller does not cut across the true sale analysis, provided the purchaser has notification rights and redirection rights;
- a right of the seller to repurchase certain receivables does not cut across the true sale analysis; however, any obligation to repurchase receivables (to the extent it would go beyond a standard repurchase obligation of ineligible receivables) would have to be analysed on a case-by-case basis; and
- the right to the residual profit does not cut across the true sale analysis.

It should be noted that a standard has been established in Swiss transactions in the last couple of years that was never subject to challenges. Also, true sale legal opinions have been issued in a form satisfactory to investors and rating agencies.

4.10 Continuous Sales of Receivables. Can the seller agree in an enforceable manner to continuous sales of receivables (i.e., sales of receivables as and when they arise)? Would such an agreement survive and continue to transfer receivables to the purchaser following the seller's insolvency?

Yes, under Swiss law, a seller can agree in an enforceable manner to continuous sales of receivables. In fact, given that essentially all Swiss ABS transactions are revolving transactions, this technique is often used. Whilst such an agreement would generally survive the seller's insolvency, it is fair to assume that receivables coming into existence following the opening of bankruptcy over the seller would no longer be assigned to the purchaser (see also question 4.11).

4.11 Future Receivables. Can the seller commit in an enforceable manner to sell receivables to the purchaser that come into existence after the date of the receivables purchase agreement (e.g., "future flow" securitisation)? If so, how must the sale of future receivables be structured to be valid and enforceable? Is there a distinction between future receivables that arise prior to *versus* after the seller's insolvency?

Yes, a seller may commit in an enforceable manner to sell and assign future receivables to the purchaser. Provided the receivables are identifiable (see question 4.8), the assignment is valid and enforceable. However, future claims, which have been assigned but have come into existence only after the opening of bankruptcy proceedings or a moratorium against the seller, fall into the seller's bankrupt estate and do not pass over to the purchaser.

Accordingly, the key question is whether or not a receivable qualifies as future receivable. Receivables for repayment of principal loan amounts are not considered to be future receivables, but rather existing receivables becoming due in the future. Whilst the analysis around interest is less clear, there are still very strong arguments to say that interest receivables can be assigned in a bankruptcy-remote way and legal opinions provided have been acceptable to investors and rating agencies. Given the uncertainty around the analysis of leasing instalments, securitisation transactions involving the securitisations of lease assets normally feature the transfer of the entire lease agreement so that any lease instalment would directly arise with the purchaser.

4.12 Related Security. Must any additional formalities be fulfilled in order for the related security to be transferred concurrently with the sale of receivables? If not all related security can be enforceably transferred, what methods are customarily adopted to provide the purchaser the benefits of such related security?

This depends on the relevant secured asset and the basis under which security has been provided over such asset. To the extent security rights qualify as accessory ancillary rights, such rights are assigned together with the receivable. Other security rights require an explicit transfer clause. To the extent a secured asset is evidenced by a securities instrument, such instrument will have to be transferred as well. For mortgages loans, please refer to question 4.3.

4.13 Set-Off; Liability to Obligor. Assuming that a receivables contract does not contain a provision whereby the obligor waives its right to set-off against amounts it owes to the seller, do the obligor's set-off rights terminate upon its receipt of notice of a sale? At any other time? If a receivables contract does not waive set-off but the obligor's set-off rights are terminated due to notice or some other action, will either the seller or the purchaser be liable to the obligor for damages caused by such termination?

Under Swiss substantive law, the purchaser as assignee only acquires such rights as the seller as assignor possesses; in particular, all defences to the receivables available to an obligor may be used

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by that obligor against the seller if they were already in existence at the time when the obligor obtained knowledge of the assignment; and if a counterclaim of the obligor was not yet due at this time, the obligor may still set off the counterclaim if it does not become due later than the receivable. Consequently, such set-off rights indeed terminate upon the obligor being notified, but only going forward.

In case the obligor is able to set off a claim it has against the seller against the receivable held by the purchaser on the basis of the mechanics described above, the seller would be liable towards the purchaser and have to pay the corresponding amount either as a deemed collection or as a damage. In case the obligor would be precluded from setting off its claim against the receivable, neither the seller nor the purchaser would be liable towards the obligor, but the obligor may still collect and enforce the claim it holds against the seller.

4.14 Profit Extraction. What methods are typically used in your jurisdiction to extract residual profits from the purchaser?

In addition to fees that might be payable to the seller (such as servicing fees, administration fees, etc.), residual profit extractions can be structured as a payment of (i) deferred purchase price, (ii) disbursement on any subordinated loan or other instrument held by the seller, (iii) any other form of fee against providing credit enhancement by the seller and (iv) payment of profit on the equity held by the seller. The key point is to structure such profit extraction in a tax neutral manner. Hence, the amount of profit extracted as a return on equity should normally be as low as possible.

5 Security Issues

5.1 Back-up Security. Is it customary in your jurisdiction to take a "back-up" security interest over the seller's ownership interest in the receivables and the related security, in the event that an outright sale is deemed by a court (for whatever reason) not to have occurred and have been perfected (see question 4.9 above)?

In Swiss securitisation transaction, it is not customary to take a back-up security interest. In the unlikely event of a recharacterisation, the sale of the receivables is very likely to be requalified as a security interest.

5.2 Seller Security. If it is customary to take back-up security, what are the formalities for the seller granting a security interest in receivables and related security under the laws of your jurisdiction, and for such security interest to be perfected?

This is not applicable.

5.3 Purchaser Security. If the purchaser grants security over all of its assets (including purchased receivables) in favour of the providers of its funding, what formalities must the purchaser comply with in your jurisdiction to grant and perfect a security interest in purchased receivables governed by the laws of your jurisdiction and the related security?

Security granted by the purchaser over the receivables held by it is normally provided by way of assignment for security purposes (*Sicherungszession*). Whilst the right of the providers of funding to exercise rights under the receivables so assigned is contractually limited, such assignment still qualifies a full title assignment and accordingly, the analysis around the assignment of the receivable from the seller to the purchaser applies equally to the assignment for security purposes. The same holds true for the assignment of any security rights or other ancillary rights.

5.4 Recognition. If the purchaser grants a security interest in receivables governed by the laws of your jurisdiction, and that security interest is valid and perfected under the laws of the purchaser's jurisdiction, will the security be treated as valid and perfected in your jurisdiction or must additional steps be taken in your jurisdiction?

Please refer to the answers to the questions raised under section 3. On that basis, it is standard practice that the law governing the security agreement follows the governing law of the receivables.

5.5 Additional Formalities. What additional or different requirements apply to security interests in or connected to insurance policies, promissory notes, mortgage loans, consumer loans or marketable debt securities?

Please refer to our answer to question 4.3.

5.6 Trusts. Does your jurisdiction recognise trusts? If not, is there a mechanism whereby collections received by the seller in respect of sold receivables can be held or be deemed to be held separate and apart from the seller's own assets (so that they are not part of the seller's insolvency estate) until turned over to the purchaser?

Swiss law does not provide for the concept of trusts. However, given that the Hague Trust Convention has been recognised by Switzerland, foreign trusts are, subject to certain limitations, enforceable in Switzerland.

However, we would note that it is not standard in Swiss transactions that a trust is declared over collections held by the seller. Rather, the commingling risk is addressed by:

- directing obligors to pay directly into an account of the purchaser;
- introducing short intervals for sweeping collections to the purchaser (daily);
- introducing rating triggers or other notification triggers; if triggered, obligors would be instructed to pay directly into an account of the purchaser; and
- limiting the redirection period by instructing a third-party service provider to send out notices to obligors upon the occurrence of a certain trigger event; for purposes of limiting the period for sending out notices, the seller would have to send to the third-party service provider updated lists of receivables, preferably through an automated interface.

5.7 Bank Accounts. Does your jurisdiction recognise escrow accounts? Can security be taken over a bank account located in your jurisdiction? If so, what is the typical method? Would courts in your jurisdiction recognise a foreign law grant of security (for example, an English law debenture) taken over a bank account located in your jurisdiction?

Escrow accounts are recognised in Switzerland. Also, security

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can be taken over Swiss bank accounts either by way of security assignment or by way of pledge. Legally spoken, security is taken over the claim the account holder holds against the account bank. Again, parties are free to choose the governing law of such security agreement, but the choice of law may not be asserted against the account bank. Hence, it is standard that security agreements relating to Swiss bank accounts are governed by Swiss law.

5.8 Enforcement over Bank Accounts. If security over a bank account is possible and the secured party enforces that security, does the secured party control all cash flowing into the bank account from enforcement forward until the secured party is repaid in full, or are there limitations? If there are limitations, what are they?

The security is validly created over cash standing to the credit of the bank account or being transferred to the bank account prior to the opening of bankruptcy. However, whilst there are arguments to say that cash also flowing to the bank account after the opening of bankruptcy over the security provider would be captured under the security interest, it is prudent to assume that such cash would form part of the bankrupt estate of the security provider.

5.9 Use of Cash Bank Accounts. If security over a bank account is possible, can the owner of the account have access to the funds in the account prior to enforcement without affecting the security?

Yes, this is possible and standard. This requires authority to be granted by the secured party to the holder of the bank account. Such authority is subject to revocation by the secured party.

6 Insolvency Laws

6.1 Stay of Action. If, after a sale of receivables that is otherwise perfected, the seller becomes subject to an insolvency proceeding, will your jurisdiction's insolvency laws automatically prohibit the purchaser from collecting, transferring or otherwise exercising ownership rights over the purchased receivables (a "stay of action")? If so, what generally is the length of that stay of action? Does the insolvency official have the ability to stay collection and enforcement actions until he determines that the sale is perfected? Would the answer be different if the purchaser is deemed to only be a secured party rather than the owner of the receivables?

No, subject to clawbacks (see question 6.3 below) or other challenges, the perfected assignment of existing receivables is valid and binding and receivables already assigned would not form part of the bankrupt estate of the seller. Accordingly, there is neither an automatic prohibition of collecting, transferring or otherwise exercising ownership rights over the purchased receivables nor would the seller's insolvency official have the ability to stay collection and enforcement actions until he determines that the sale is perfected. However, the seller's insolvency official may try to obtain an injunctive relief prohibiting the purchaser to dispose of the receivables, but this would require a valid plausibility check with regard to the merits of the case.

The situation is different for future receivables, and on the basis of the analysis made under questions 4.8 and 4.11, it can be expected that the insolvency official will ensure that all such receivables will be registered in the inventory as assets belonging to the bankrupt estate.

The answer would be the same in case of a recharacterisation of the transaction as a secured financing.

6.2 Insolvency Official's Powers. If there is no stay of action, under what circumstances, if any, does the insolvency official have the power to prohibit the purchaser's exercise of its ownership rights over the receivables (by means of injunction, stay order or other action)?

Upon the opening of bankruptcy over the seller, the insolvency official will identify all of the seller's assets as such assets form part of the bankrupt estate. This includes any receivables not properly sold and assigned to the purchaser upon the opening of bankruptcy. Thus, any receivable arising after the opening of bankruptcy will no longer be assigned to the purchaser (see question 4.11 above) and the insolvency official may dispose over such receivables.

However, an insolvency official does not have the power to prohibit the purchaser's exercise of its ownership rights over the receivables as such, but an insolvency official might try to argue that a receivable has not been validly assigned to the purchaser on the basis of defect in the underlying agreement, clawback or similar mechanics.

6.3 Suspect Period (Clawback). Under what facts or circumstances could the insolvency official rescind or reverse transactions that took place during a "suspect" or "preference" period before the commencement of the seller's insolvency proceedings? What are the lengths of the "suspect" or "preference" periods in your jurisdiction for (a) transactions between unrelated parties, and (b) transactions between related parties? If the purchaser is majority-owned or controlled by the seller or an affiliate of the seller, does that render sales by the seller to the purchaser "related party transactions" for purposes of determining the length of the suspect period? If a parent company of the seller guarantee's the performance by the seller of its obligations under contracts with the purchaser, does that render sales by the seller to the purchaser "related party transactions" for purposes of determining the length of the suspect period?

In case of the seller and/or the purchaser being adjudicated bankrupt, the insolvency official or, under certain conditions, creditors of the seller and/or the purchaser, may challenge the sale and assignment of receivables to the purchaser and/or the subsequent creation of any security interest by the purchaser, subject to the conditions of articles 285 *et seq.* Swiss Debt Enforcement and Bankruptcy Act (DEBA) being satisfied. Articles 285 *et seq.* DEBA provide that a transaction may be subject to challenge if no or no equivalent consideration is given ("transaction at an undervalue" as described in article 286 DEBA), if the party granting security or discharging a debt was over-indebted ("voidability for over-indebtedness" as described in article 287 DEBA) or if the seller and/or the purchaser (as applicable) had the intention to disfavour or favour certain of its creditors or should reasonably have foreseen such result and this intention was or must have been known to the purchaser ("preference" as described in article 288 DEBA).

Every transaction at an undervalue may be challenged if it has been consummated during a suspect period of one year before the adjudication of bankruptcy. The same one-year suspect period is

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applicable to an avoidance action for over-indebtedness. For a preference, the suspect period is five years prior to the adjudication of bankruptcy. In cases where there has been a prior restructuring proceeding or a decree of protective measures, the duration of the previous restructuring proceeding or the period since the decree of protective measures does not count towards the calculation of the respective suspect period. For the suspect period, it is irrelevant whether the transaction is among affiliates or between independent third parties.

In connection with a challenge under article 286 DEBA ("transaction at an undervalue") that aims to challenge a transaction among affiliates, the burden of proof to show that there was no undervalue is with the affiliated counterparty to the insolvent company.

In connection with a challenge under article 288 DEBA ("preference") that aims to challenge a transaction among affiliates, the burden of proof to show that the intention to disfavour or favour certain creditors was not or should not have been known to the counterparty to the insolvent party, will be on said counterparty.

6.4 Substantive Consolidation. Under what facts or circumstances, if any, could the insolvency official consolidate the assets and liabilities of the purchaser with those of the seller or its affiliates in the insolvency proceeding? If the purchaser is owned by the seller or by an affiliate of the seller, does that affect the consolidation analysis?

A consolidation of the assets and liabilities with the seller would only be possible in extraordinary circumstances involving the challenge of the true sale or fraudulent behaviour of the parties involved. There is no concept of substantive consolidation under Swiss law even in case the purchaser is wholly owned by the seller (subject to extraordinary cases, such as fraud and abuse of rights) and a bankruptcy of the seller as the sole shareholder of the purchaser would, as a matter of Swiss law, not result in a consolidation of its assets and/or liabilities with those of the purchaser.

6.5 Effect of Insolvency on Receivables Sales. If insolvency proceedings are commenced against the seller in your jurisdiction, what effect do those proceedings have on (a) sales of receivables that would otherwise occur after the commencement of such proceedings, or (b) on sales of receivables that only come into existence after the commencement of such proceedings?

Following the opening of bankruptcy over the seller, the seller may no longer dispose of its assets, and any sale and assignment that would otherwise occur after such opening would no longer be consummated. Also, future receivables sold and assigned prior to the opening of bankruptcy that come into existence only after the opening of bankruptcy would not be validly assigned to the purchaser, but would become part of the seller's bankrupt estate.

6.6 Effect of Limited Recourse Provisions. If a debtor's contract contains a limited recourse provision (see question 7.3 below), can the debtor nevertheless be declared insolvent on the grounds that it cannot pay its debts as they become due?

First, it should be noted that there might be creditors of the debtor that are not a party to an agreement and that have not agreed to limited recourse, such as tax authorities, the statutory auditors, and non-contractual creditors of the debtor, who are not subject to limited recourse. With regard to the relevant Swiss tax administration, it must be noted that tax rulings are normally issued confirming the tax treatment of a transaction and which will prevent them from making any claim outside the tax rulings.

Limited recourse provisions are generally enforceable under Swiss law, subject to the standard limitations applying to enforceability more generally, even though we note that we are not aware of any relevant judicial precedent dealing with limited recourse provisions. In any event, the debtor will, in case of relevant steps initiated by a person in violation of the limited recourse undertaking entered into by it, have to take appropriate legal steps (such as obtaining an injunctive relief) to enforce the undertaking.

7 Special Rules

7.1 Securitisation Law. Is there a special securitisation law (and/or special provisions in other laws) in your jurisdiction establishing a legal framework for securitisation transactions? If so, what are the basics? Is there a regulatory authority responsible for regulating securitisation transactions in your jurisdiction?

Securitisation has developed in Switzerland without specific supporting legislation, and there is no regulatory authority for securitisation transactions. Accordingly, the general legal framework is relevant as for any other financing transaction, such as the Swiss Code of Obligations, in particular in relation to matters relating to the formation of the special purpose entity and the transfer of the receivables and the asset as such, as well as general capital markets regulations and regulatory regulations.

Also, no specific listing rules apply to asset-backed securities, and the SIX Swiss Exchange generally applies the same listing rules as for issuance of bonds. However, issuing special purpose entities benefit from certain relaxed standards in the approval process.

Whilst there is no specific regulatory authority for securitisation transactions, various regulatory authorities are relevant in the context of Swiss securitisation transactions, such as the SIX Exchange Regulation of the SIX Swiss Exchange for listing-related matters, the Swiss Financial Market Supervisory Authority (FINMA) for certain regulatory matters (i.e, confirmation of non-licensing requirements, non-consolidation in bankruptcy, non-application of anti-money laundering considerations (depending on the structure of the transaction and the underlying asset category), in each case as relevant) and cantonal regulators for consumer credit licensing, if relevant. In addition, transactions are typically presented and signed off by relevant tax authorities by way of tax ruling.

7.2 Securitisation Entities. Does your jurisdiction have laws specifically providing for establishment of special purpose entities for securitisation? If so, what does the law provide as to: (a) requirements for establishment and management of such an entity; (b) legal attributes and benefits of the entity; and (c) any specific requirements as to the status of directors or shareholders?

No, there are no such specific laws in Switzerland and special purposes entities are generally established within the general Swiss corporate legal framework (see questions 7.1 and 7.3).

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7.3 Location and form of Securitisation Entities. Is it typical to establish the special purpose entity in your jurisdiction or offshore? If in your jurisdiction, what are the advantages to locating the special purpose entity in your jurisdiction? If offshore, where are special purpose entities typically located for securitisations in your jurisdiction? What are the forms that the special purpose entity would normally take in your jurisdiction and how would such entity usually be owned?

In Swiss securitisation transactions, we see both special purpose entities formed in Switzerland and abroad. Various considerations should be made, depending on the underlying asset.

Generally, it will be very difficult to use non-Swiss special purpose entities where the underlying asset relates to real estate located in Switzerland, given that cantonal withholding taxes may be incurred on any interest payment secured by Swiss real estate.

Also, it might be the case that the transfer of a receivable abroad is not desirable for other reasons, such as data protection considerations, in particular where the underlying documentation does not provide for a proper waiver of data protection.

On the other hand, it should be noted that interest payments on debt instruments issued by a Swiss special purpose entity to multiple investors attract Swiss withholding tax at a rate of 35 per cent. While Swiss withholding tax is generally recoverable, the process for doing so might be burdensome for non-Swiss investors and even a Swiss investor would suffer a delay in recovering the withholding tax. In case an investor is located in a jurisdiction that does not benefit from favourable double tax treaties or does not otherwise benefit from treaty protection (typically such as tax-transparent funds), Swiss withholding tax might not be fully recoverable or not be recoverable at all. Swiss withholding tax can be structured away if a non-Swiss vehicle is used. However, this adds a lot of complexity to the structuring process given that there will also be a strong focus on the true sale analysis from a tax perspective.

Finally, Swiss originators that do not form a presence abroad normally have the inclination to go with a Swiss special purpose entity for cost-efficiency and organisational purposes.

In Switzerland, a special purpose entity may take the form of a limited liability stock corporation AG or a limited liability company GmbH.

In some transactions, special purpose entities held by independent shareholders have been used. However, wholly owned subsidiary structures under Swiss law have also been acceptable to rating agencies in the past, but it is always a requirement that there is an independent board member with certain veto rights in relation to certain reserved matters. Some transactions feature for golden shareholder structures.

Whilst acceptable to rating agencies in light of the bankruptcy remoteness analysis, wholly owned subsidiary structures should also be careful in relation to assets from an accounting and from a regulatory capital relief perspective (where relevant).

7.4 Limited-Recourse Clause. Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) limiting the recourse of parties to that agreement to the available assets of the relevant debtor, and providing that to the extent of any shortfall the debt of the relevant debtor is extinguished?

Yes, limited recourse provisions are generally enforceable under Swiss law, subject to the standard limitations applying to enforceability more generally, even though we would note that we are not aware of any relevant judicial precedent dealing with limited recourse provisions. In any event, the debtor will, in case of relevant steps initiated by a person in violation of the limited recourse undertaking entered into by it, have to take appropriate legal steps (such as obtaining an injunctive relief) to enforce the undertaking.

7.5 Non-Petition Clause. Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) prohibiting the parties from: (a) taking legal action against the purchaser or another person; or (b) commencing an insolvency proceeding against the purchaser or another person?

Yes, non-petition provisions are generally enforceable under Swiss law, subject to the standard limitations applying to enforceability more generally, even though we would note that we are not aware of any relevant judicial precedent dealing with non-petition provisions as typically set out in securitisation transactions. In any event, the debtor will, in case of relevant steps initiated by a person in violation of the non-petition undertaking entered into by it, have to take appropriate legal steps (such as obtaining an injunctive relief) to enforce the undertaking.

7.6 Priority of Payments "Waterfall". Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) distributing payments to parties in a certain order specified in the contract?

Yes, priority of payments provisions is generally enforceable under Swiss law, subject to the standard limitations applying to enforceability more generally. However, to the extent unsecured claims exist, we note that pursuant to article 219 DEBA all non-secured creditors of a Swiss entity would be part of the same (third) class of creditors in an insolvency. While we are not aware of any relevant judicial precedents, agreements governing the relevant priority of payments among creditors belonging to the same (third) class of creditors are binding on an insolvency official of an estate. Should, however, a Swiss entity become insolvent, it cannot be excluded that the insolvency official would treat all non-secured creditors indiscriminately as third-class creditors and consider the priority of payments as a mere arrangement among creditors of the estate in relation to their respective claims *vis-à-vis* the estate and pay them out on a *pro rata* and *pari passu* basis, in which case the parties to the relevant agreements may have to rely on the redistribution by the creditors among each of them.

7.7 Independent Director. Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) or a provision in a party's organisational documents prohibiting the directors from taking specified actions (including commencing an insolvency proceeding) without the affirmative vote of an independent director?

Subject to general qualifications on enforceability, such provisions would be valid and enforceable in Switzerland. However, to the extent such provisions are only reflected in an agreement (rather than the organisational corporate documents), taking a specified acting without the affirmative vote of the independent director

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would still be valid, even though this would be in breach of such contractual agreement. Accordingly, a relevant counterparty would have to take appropriate legal steps (such as obtaining an injunctive relief) to enforce the undertaking. To the extent such provisions are reflected in the corporate documents of a Swiss entity, taking a specified acting without the affirmative vote of the independent director would result in such action not being covered by the appropriate corporate authorisation, and any director (other than the independent director) would be in breach of its duties, which could ultimately result in director liability.

7.8 Location of Purchaser. Is it typical to establish the purchaser in your jurisdiction or offshore? If in your jurisdiction, what are the advantages to locating the purchaser in your jurisdiction? If offshore, where are purchasers typically located for securitisations in your jurisdiction?

Please refer to question 7.3.

8 Regulatory Issues

8.1 Required Authorisations, etc. Assuming that the purchaser does no other business in your jurisdiction, will its purchase and ownership or its collection and enforcement of receivables result in its being required to qualify to do business or to obtain any licence or its being subject to regulation as a financial institution in your jurisdiction? Does the answer to the preceding question change if the purchaser does business with more than one seller in your jurisdiction?

Generally, the mere purchase, ownership and collection and enforcement of receivables by a Swiss purchaser will not result in any licensing requirement or it being subject to regulations as a financial institution. However, given the level of uncertainty around those questions, it is standard to seek negative confirmations from relevant authorities, such as the Swiss Financial Market Supervisory Authority (FINMA) (e.g. (i) confirmation of non-licensing requirements as a bank, collective investment scheme or otherwise, (ii) non-consolidation in bankruptcy, (iii) non-application of anti-money laundering considerations) or the cantonal regulators for consumer credit licensing questions, where relevant.

Doing business with more than one seller would not change the analysis, provided the structure as such remains unchanged (in particular with regard to the fact that the purchaser does not have the ability to make an active investment decision in relation to receivables to be purchased).

8.2 Servicing. Does the seller require any licences, etc., in order to continue to enforce and collect receivables following their sale to the purchaser, including to appear before a court? Does a third-party replacement servicer require any licences, etc., in order to enforce and collect sold receivables?

Generally, the mere servicing of a receivable will not result in any licensing requirements or it being subject to regulations as a financial institution. The same holds true for any third-party successor servicer.

8.3 Data Protection. Does your jurisdiction have laws restricting the use or dissemination of data about or provided by obligors? If so, do these laws apply only to consumer obligors or also to enterprises?

Third-party obligors' rights are protected under the Swiss Federal Data Protection Act and other secrecy rights (such as under the Swiss Federal Banking Act, if relevant). Whilst the Swiss legal framework is less restrictive than in other jurisdictions, it is generally considered to be a requirement that data protection and other secrecy rights are addressed by obtaining relevant waivers in the underlying agreements or otherwise. While it is important to address such third-party obligors' rights, a breach of these rights in itself would not jeopardise a valid assignment of the relevant receivable, although it would create other issues.

Whilst rights of any party are protected in the Swiss legal framework, the standard is more relaxed in case no personal data are involved.

8.4 Consumer Protection. If the obligors are consumers, will the purchaser (including a bank acting as purchaser) be required to comply with any consumer protection law of your jurisdiction? Briefly, what is required?

The CCA imposes a highly regulated framework with regard to consumer lending. Regulations include rules on credit check, form requirements on the underlying documentation, withdrawal rights of the borrower, maximum interest, ban on aggressive advertisement, etc. However, on the basis that the obligations of the seller as lender have been fully performed (which is a reasonable assumption), the purchaser as lender, whilst still being subject to the legal framework of the CCA, would factually have hardly any further obligation to be complied with. Of course, the obligors would still have the benefit of its rights under the CCA. However, these have always been properly addressed by structuring the transactions accordingly.

8.5 Currency Restrictions. Does your jurisdiction have laws restricting the exchange of your jurisdiction's currency for other currencies or the making of payments in your jurisdiction's currency to persons outside the country?

There are no currency exchange restrictions in Switzerland, except that a hard cash transfer of sums in excess of CHF 10,000 will have to be declared and will be registered.

8.6 Risk Retention. Does your jurisdiction have laws or regulations relating to "risk retention"? How are securitisation transactions in your jurisdiction usually structured to satisfy those risk retention requirements?

There are no risk retention rules in Switzerland. In particular, Regulation (EU) 575/2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) 648/2012 (Capital Requirements Regulation), including Part 5 have not yet been adopted by Switzerland and transposed into Swiss law. However, in order not to negatively affect distribution, a number of transactions impose covenants on the seller to retain, on an ongoing basis, a material net economic interest in the transaction in an amount equal to at least 5% of the nominal value of the assets (or a higher percentage as may be required from time to time in accordance with the applicable Risk Retention Rules). This would

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apply to exemptions, general operating conditions, depositaries, leverage, transparency and supervision, as if Switzerland had implemented:

- Article 405(1)(d) of the Capital Requirements Regulation.
- Article 51 of the Commission Delegated Regulation No. 231/2013 of 19 December 2012 supplementing Directive 2011/61/EU on alternative investment fund managers (AIFM Directive).

8.7 Regulatory Developments. Have there been any regulatory developments in your jurisdiction which are likely to have a material impact on securitisation transactions in your jurisdiction?

There are no reforms pending in Switzerland that would be specifically addressed to securitisation transactions in Switzerland. However, a significant development in the Swiss financial industry in general, and the Swiss debt capital market in particular, is the contemplated overhaul of the Swiss financial markets regulatory framework. The Financial Market Infrastructure Act (FinMIA) entered into force on 1 January 2016 in a general attempt to bring the Swiss regulatory framework in line with international regulations such as:

- Directive 2014/65/EU on markets in financial instruments (MiFID II).
- Directive 2003/71/EC on the prospectus to be published when securities are offered to the public or admitted to trading (Prospectus Directive).

It is further suggested that the Federal Financial Services Act (FinSA) and the Financial Institutions Act (FinIA) replace major portions of the existing regulations. The FinSA and FinIA will aim to:

- Strengthen client protection.
- Promote the competitiveness of the Swiss financial centre.
- Minimise competitive distortions between providers by creating a level playing field.

9 Taxation

9.1 Withholding Taxes. Will any part of payments on receivables by the obligors to the seller or the purchaser be subject to withholding taxes in your jurisdiction? Does the answer depend on the nature of the receivables, whether they bear interest, their term to maturity, or where the seller or the purchaser is located? In the case of a sale of trade receivables at a discount, is there a risk that the discount will be recharacterised in whole or in part as interest? In the case of a sale of trade receivables where a portion of the purchase price is payable upon collection of the receivable, is there a risk that the deferred purchase price will be recharacterised in whole or in part as interest? If withholding taxes might apply, what are the typical methods for eliminating or reducing withholding taxes?

As a general rule, arm's length payments on receivables, including payment of interest and late interest, are not subject to withholding taxes in Switzerland. As an exception, the following interest payments might be subject to Swiss withholding tax:

- interest on Swiss "bank deposits";
- interest on Swiss "bonds" (defined as a fixed term instrument if it cannot be ruled out that it is held at any time by more than 10 creditors which are not banks);
- interest on any funds raised by a Swiss borrower with more than 20 non-banks; and
- interest paid to non-Swiss lenders on any debt secured by mortgages in Swiss real estate.

Securitisation transactions (with a special purposes securitisation entity) in Switzerland will regularly be seen, from a Swiss tax perspective, as an issuance of bonds and will thus trigger Swiss withholding tax (of currently 35%) on any interest payments to the investors (irrespective of the underlying receivables). While Swiss withholding tax is generally recoverable, the process of doing so can be burdensome for non-Swiss investors and even Swiss investors suffer a delay in recovering these amounts. For investors located in a jurisdiction that does not benefit from favourable double tax treaties, or that do not otherwise benefit from treaty protection, even in case a favourable double tax treaty were in place (such as tax-transparent funds), Swiss withholding tax might not be fully recoverable or not recoverable at all. Swiss withholding tax can be avoided (on the level of the securitisation vehicle) by careful structuring if a non-Swiss securitisation vehicle is used, but this adds a lot of complexity to the structuring process given that there will be, among other things, a strong focus on the true sale analysis from a tax perspective.

As mentioned interest payments made to non-Swiss lenders are subject to Swiss withholding tax if the debt is secured by mortgages in Swiss real estate. This causes serious concerns in light of CMBS/RMBS transactions where the instruments are traded. In practice, this concern has been addressed by setting up structures that are unsecured (i.e. the transaction would fully rely on the bankruptcy remoteness of the Swiss special purpose entity, which has been acceptable to investors and rating agencies in the past).

Last, but not least, a deferred purchase price or any other kind of premium might indeed be recharacterised as an interest component. To avoid the risk of a recharacterisation, it is standard practice to approach the tax authorities and seek a tax ruling confirmation ahead of the closing of the transaction.

9.2 Seller Tax Accounting. Does your jurisdiction require that a specific accounting policy is adopted for tax purposes by the seller or purchaser in the context of a securitisation?

A Swiss company is, by law, obliged to use its statutory accounts issued pursuant to the Swiss Code of Obligations for Swiss tax purposes. The Swiss Code of Obligations does, however, not provide for any specific accounting rules in the context of a securitisation.

9.3 Stamp Duty, etc. Does your jurisdiction impose stamp duty or other transfer or documentary taxes on sales of receivables?

No stamp duty is payable on sales of receivables unless such receivables are regarded as bonds, debentures or money market papers and are transferred by, or via, a "securities dealer" (as defined for tax purposes in Swiss stamp tax law).

More generally, from a seller's overall corporate income tax perspective, it is, among other things, absolutely imperative that both:

- the relevant receivables can be transferred to the purchaser without accelerating and triggering any corporate income taxes; and
- the profit and loss potential associated with the underlying business remains with the seller.

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If the transaction involves a Swiss purchaser, the additional (purchaser) entity level corporate income and net equity taxes are typically kept at a (negligible) minimum (of a few thousand CHF *per annum*). Although there are no specific tax legislation and/or tax guidelines, securitisation transactions must be presented and signed off by the relevant tax authorities by way of advance tax rulings.

9.4 Value Added Taxes. Does your jurisdiction impose value added tax, sales tax or other similar taxes on sales of goods or services, on sales of receivables or on fees for collection agent services?

The supply of goods and services for consideration within the Swiss territory, for VAT purposes, is subject to VAT. The sale and purchase of receivables is regarded as a VAT-exempt financial service without credit for input tax. The services of collection agents, if deemed to take place within the Swiss territory according to the applicable VAT place of supply rules, attract VAT at the standard rate of currently 7.7%.

9.5 Purchaser Liability. If the seller is required to pay value-added tax, stamp duty or other taxes upon the sale of receivables (or on the sale of goods or services that give rise to the receivables) and the seller does not pay, then will the taxing authority be able to make claims for the unpaid tax against the purchaser or against the sold receivables or collections?

As a general rule, the taxing authority will not be able to makes such claims. Under certain conditions, however, the taxing authority has a secondary liability claim against the purchaser with regard to the VAT included in receivables sold/assigned and remaining unpaid in the insolvency of the seller. Yet, given that amounts at stake are limited and the likelihood of such a scenario materialising is low, such risk has been considered as immaterial in most transactions.

9.6 Doing Business. Assuming that the purchaser conducts no other business in your jurisdiction, would the purchaser's purchase of the receivables, its appointment of the seller as its servicer and collection agent, or its enforcement of the receivables against the obligors, make it liable to tax in your jurisdiction?

The mere act of the purchaser's purchase of the receivables, the appointment of the seller as its servicer and collection agent, or its enforcement of the receivables against the obligors, does not give rise to a Swiss income tax nexus for the purchaser (assuming that it is not already resident for tax purposes in Switzerland or conducting business here via a Swiss permanent establishment).

9.7 Taxable Income. If a purchaser located in your jurisdiction receives debt relief as the result of a limited recourse clause (see question 7.3 above), is that debt relief liable to tax in your jurisdiction?

If structured correctly from a legal perspective and reflected accordingly in the statutory accounts of the respective entity, a debt relief (or similar arrangement) as the result of a limited recourse clause will not trigger any income tax in Switzerland.

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Walder Wyss is the frontrunner for Swiss structured finance transactions and is involved in essentially all public and private ABS transactions, synthetic transactions, covered bond transactions and other securitisations. In particular in auto lease ABS (and consumer lending more generally) and mortgage loan transactions, Walder Wyss has an extensive industry expertise. Walder Wyss advised Lloyds Bank on the first ever Swiss (private) auto lease ABS transaction and UBS in the establishment of its CHF 15bn covered bond programme. In addition, Walder Wyss advised Valiant Bank on the first ever Swiss domestic covered bond transaction. Further clients include Swisscard, Cembra Money Bank, AMAG Leasing, Multilease and others.

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USA

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Note

To the extent specified therein, the answers to certain questions generally describe the rules provided by the Uniform Commercial Code ("UCC"), a model statute enacted with some variations in each state, and the answers to certain other questions generally describe the rules provided by the U.S. Bankruptcy Code. The U.S. is a signatory to, but has not yet ratified, the United Nations Convention on the Assignment of Receivables in International Trade (the "UNCITRAL Convention").

It is anticipated that the U.S. may ratify the UNCITRAL Convention in the near future. Upon the effectiveness thereof, the UNCITRAL Convention would override the UCC and change many of the answers set forth herein.

The U.S. contains multiple jurisdictions with varying statutory laws, regulations and judicial precedent, in general, where the laws of a particular U.S. jurisdiction are relevant, the following answers assume that the law of the state of New York applies.

1 Receivables Contracts

1.1 Formalities. In order to create an enforceable debt obligation of the obligor to the seller: (a) is it necessary that the sales of goods or services are evidenced by a formal receivables contract; (b) are invoices alone sufficient; and (c) can a binding contract arise as a result of the behaviour of the parties?

With respect to a contract for the sale for goods of $500 or more, some writing is sufficient to indicate that a contract for sale has been made is required. A contract for services is generally required to be in writing if, by its terms, it is not to be completed within one year. However, with respect to contracts for sales of goods, a formal sales contract is not required but rather a contract may be on the basis of exchanged purchase orders, general terms, and invoices, or by a combination of writings which are themselves insufficient to establish a contract coupled with the conduct by both parties which recognizes the existence of a contract.

1.2 Consumer Protections. Do your jurisdiction's laws: (a) limit rates of interest on consumer credit, loans or other kinds of receivables; (b) provide a statutory right to interest on late payments; (c) permit consumers to cancel receivables for a specified period of time; or (d) provide other noteworthy rights to consumers with respect to receivables owing by them?

(a) Each state has different limitations on the permissible rate of interest; however, U.S. federal law permits banks and some other depository institutions to use a uniform nationwide rate, determined by the law of the state where the principal office of the institution is located.

(b) Not to our knowledge.

(c) Certain jurisdictions provide consumers with a period of time to cancel certain types of transactions after entering into a contract; in some cases, these rights only apply when the contract was entered into in a specified context (e.g., when a contract is entered into with a merchant other than at a merchant's regular place of business).

(d) Consumers benefit from a number of protections. For example, restrictions on assignment of consumer loans are generally enforceable. In addition, personally identifiable consumer information cannot be disclosed or used other than in specified manners.

Federal and state consumer protection laws and regulations regulate the relationships among credit card members, credit card issuers and sellers of merchandise and services in transactions financed by the extension of credit under credit accounts. These laws and regulations include the Credit Card Accountability and Disclosure Act, the Federal Truth-in-Lending Act and Fair Credit Billing Act, and the provisions of the Federal Reserve Board's Regulation Z issued under each of them, the Equal Credit Opportunity Act and the provisions of the Federal Reserve Board's Regulation B issued under it, the Fair Credit Reporting Act and the Fair Debt Collection Practices Act. These statutes and regulations require credit disclosures on credit card applications and solicitations, on an initial disclosure statement required to be provided when a credit card account is first opened, and with each monthly billing statement. They also prohibit certain discriminatory practices in extending credit, impose certain limitations on the charges that may be imposed and regulate collection practices.

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In addition, these laws and regulations entitle card members to have payments and credits promptly applied on credit accounts and to require billing errors to be promptly resolved. The Credit Card Accountability and Disclosure Act and the provisions of the regulations that implemented it limit the ability of credit card issuers to increase the interest rates on existing credit card balances, regulate how interest is calculated for each billing cycle, and regulate how payments must be allocated to outstanding balances with different interest rates. A card member may be entitled to assert violations of certain of these consumer protection laws and, in certain cases, claims against the lender or seller, by way of set-off against his or her obligation to pay amounts owing on his account.

For example, under the Federal Truth-in-Lending Act, a credit card issuer is subject to all claims, other than tort claims, and all defences arising out of transactions in which a credit card is used to purchase merchandise or services, if certain conditions are met. These conditions include requirements that the card member make a good faith attempt to obtain satisfactory resolution of the dispute from the person honouring the credit card and meet certain jurisdictional requirements. These jurisdictional requirements do not apply where the seller of the goods or services is the same party as the card issuer, or controls or is controlled by the card issuer directly or indirectly.

These laws also provide that in certain cases a card member's liability may not exceed $50 with respect to charges to the credit card account that resulted from unauthorized use of the credit card. In addition, the Dodd-Frank Act became federal law in 2010 and contains numerous regulations relating to the financial industry and provides for the establishment of the Bureau of Consumer Financial Protection. It is not yet clear how implantation of the Dodd-Frank Act will affect consumer receivables.

The Servicemembers Civil Relief Act allows individuals on active duty in the military to cap the interest rate and fees on debts incurred before the call to active duty at six percent. In addition, subject to judicial discretion, any action or court proceeding in which an individual in military service is involved may be stayed if the individual's rights would be prejudiced by denial of such a stay. Currently, some account holders with outstanding balances have been placed on active duty in the military, and more may be placed on active duty in the future.

1.3 Government Receivables. Where the receivables contract has been entered into with the government or a government agency, are there different requirements and laws that apply to the sale or collection of those receivables?

Yes, if the debtor is the U.S. government or one of its agencies or instrumentalities. In such a case the Federal Assignment of Claims Act will apply to an assignment of receivables and the right of the federal government to exercise set-off. A minority of states have similar laws that apply to obligations of the state or agencies or departments thereof and a few states extend such rules to municipalities and other local governmental entities.

2 Choice of Law – Receivables Contracts

2.1 No Law Specified. If the seller and the obligor do not specify a choice of law in their receivables contract, what are the main principles in your jurisdiction that will determine the governing law of the contract?

Courts generally apply the choice of law rules of the state in which the court is located, and thus answers to choice of law questions may differ depending on the state in which the litigation is prosecuted. Under the Restatement 2nd of Conflicts of Law, the rights and duties of the parties with respect to an issue in contract are determined by the local law of the state which, with respect to that issue, has the most significant relationship to the transaction and the parties. In the absence of an effective choice of law by the parties, the contacts to be taken into account in determining the law applicable to an issue include: (a) the place of contracting; (b) the place of negotiation of the contract; (c) the place of performance; (d) the location of the subject matter of the contract; and (e) the domicile, residence, nationality, place of incorporation and place of business of the parties.

2.2 Base Case. If the seller and the obligor are both resident in your jurisdiction, and the transactions giving rise to the receivables and the payment of the receivables take place in your jurisdiction, and the seller and the obligor choose the law of your jurisdiction to govern the receivables contract, is there any reason why a court in your jurisdiction would not give effect to their choice of law?

The U.S. is a multi-jurisdictional country and the contract needs to select the law of a particular U.S. state (rather than federal law) as the governing law. The choice of the law of a particular state of the U.S. to govern a contract may not be given effect if it does not bear a reasonable relationship with the transaction or parties. A few states, such as New York, permit the choice of their law to govern a contract even in the absence of any contacts if the contract satisfies certain dollar thresholds; however, another U.S. state may not respect this choice of law if litigated in the other U.S. state in the absence of a reasonable relationship. Of course, on the facts specified above, there is no reason that an effective choice of a U.S. state law cannot be made.

2.3 Freedom to Choose Foreign Law of Non-Resident Seller or Obligor. If the seller is resident in your jurisdiction but the obligor is not, or if the obligor is resident in your jurisdiction but the seller is not, and the seller and the obligor choose the foreign law of the obligor/seller to govern their receivables contract, will a court in your jurisdiction give effect to the choice of foreign law? Are there any limitations to the recognition of foreign law (such as public policy or mandatory principles of law) that would typically apply in commercial relationships such as that between the seller and the obligor under the receivables contract?

In general, the choice of law of the parties will be given effect in the circumstances described above. However, each state has somewhat different considerations in determining whether to give effect to a choice of non-U.S. law. Typically such a choice of non-U.S. law will be given effect if: (i) the chosen law has a reasonable and substantial relationship and sufficient contacts with the underlying agreement or the transaction contemplated thereby, and the chosen law has the most significant contacts with the matter in dispute; (ii) the chosen law does not violate or contravene, nor is contrary or offensive to, a public or fundamental policy of the state or of such other jurisdiction whose law would apply in the absence of an effective choice of law by the parties to the underlying agreement (which may be another U.S. state or a foreign jurisdiction); (iii) the chosen law was not induced or procured by fraud; and (iv) the matter of law for which the chosen law is to be applied has been previously addressed by the chosen law and the chosen law differs from the law that would be applied in the absence of the chosen law.

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Under the Restatement 2nd of Conflicts of Law, a court may decline to apply the law of a jurisdiction chosen by the parties to a contract (which may be another U.S. state or a foreign jurisdiction) when (1) it is necessary to protect the fundamental policies of the state, the law of which would otherwise apply, and (2) such state has a materially greater interest in the determination of a particular issue than the state of the chosen law. It is not possible to make a definitive statement of when the fundamental policy exception would apply since each U.S. state and each court will reach its own determinations on a case-by-case basis.

3 Choice of Law – Receivables Purchase Agreement

3.1 Base Case. Does your jurisdiction's law generally require the sale of receivables to be governed by the same law as the law governing the receivables themselves? If so, does that general rule apply irrespective of which law governs the receivables (i.e., your jurisdiction's laws or foreign laws)?

Generally, there is no reason that the law of the state governing the contract giving rise to the receivables needs to be the same as the law of the state governing the sale of the receivables. However, as noted below in response to question 3.4, the sale of the receivables will need to be perfected under the Uniform Commercial Code and the law governing perfection cannot be selected by the parties but, instead, is subject to mandatory choice of law rules.

3.2 Example 1: If (a) the seller and the obligor are located in your jurisdiction, (b) the receivable is governed by the law of your jurisdiction, (c) the seller sells the receivable to a purchaser located in a third country, (d) the seller and the purchaser choose the law of your jurisdiction to govern the receivables purchase agreement, and (e) the sale complies with the requirements of your jurisdiction, will a court in your jurisdiction recognise that sale as being effective against the seller, the obligor and other third parties (such as creditors or insolvency administrators of the seller and the obligor)?

Generally yes, subject to the same considerations referenced in the response to question 2.3 above.

3.3 Example 2: Assuming that the facts are the same as Example 1, but either the obligor or the purchaser or both are located outside your jurisdiction, will a court in your jurisdiction recognise that sale as being effective against the seller and other third parties (such as creditors or insolvency administrators of the seller), or must the foreign law requirements of the obligor's country or the purchaser's country (or both) be taken into account?

Generally yes, subject to the same considerations referenced in the response to question 2.3 above.

3.4 Example 3: If (a) the seller is located in your jurisdiction but the obligor is located in another country, (b) the receivable is governed by the law of the obligor's country, (c) the seller sells the receivable to a purchaser located in a third country, (d) the seller and the purchaser choose the law of the obligor's country to govern the receivables purchase agreement, and (e) the sale complies with the requirements of the obligor's country, will a court in your jurisdiction recognise that sale as being effective against the seller and other third parties (such as creditors or insolvency administrators of the seller) without the need to comply with your jurisdiction's own sale requirements?

Subject to the considerations discussed in the response to question 2.3 above, a court in a U.S. jurisdiction will generally recognize the foreign law determination of whether a "true" sale has occurred as between the parties to the transaction pursuant to which the receivables were sold. However, any transfer of receivables, whether it is characterized as an outright sale or as a conditional transfer for security is classified under the UCC as a "security interest" and such security interest would need to be "perfected" in order to be enforceable against other creditors of the seller and any bankruptcy trustee of the seller. The methods of perfecting this security interest are detailed in the response to question 4.3 below. However, the law governing perfection may not be selected by the parties but rather is subject to mandatory choice of law rules. Where perfection is obtained by the filing of UCC financing statements, the law of the seller's "location" generally governs perfection of a non-possessory security interest in receivables. A seller's location is determined according to a number of factors, including: (a) the type of organization (e.g. corporation, limited partnership or general partnership); (b) whether it is formed under the laws of a foreign country; (c) the location of its chief executive office; and (d) whether the law of the jurisdiction in which its chief executive office is located provides a system of public filing of notices of non-possessory liens on personal property as a condition for having priority over a judgment lien creditor. Although there are some exceptions, for most corporations and limited liability companies that are organized under the laws of any state of the U.S., their "location" for purposes of the UCC (and hence the law governing perfection by filing) will be their state of incorporation.

Where perfection is obtained by possession of the original promissory note or tangible "chattel paper" evidencing the receivable, the law of the jurisdiction where the promissory note or tangible chattel paper is physically located will govern perfection of a possessory security interest. Examples of chattel paper include leases of office equipment, retail auto leases, and many retail instalment sales contracts.

3.5 Example 4: If (a) the obligor is located in your jurisdiction but the seller is located in another country, (b) the receivable is governed by the law of the seller's country, (c) the seller and the purchaser choose the law of the seller's country to govern the receivables purchase agreement, and (d) the sale complies with the requirements of the seller's country, will a court in your jurisdiction recognise that sale as being effective against the obligor and other third parties (such as creditors or insolvency administrators of the obligor) without the need to comply with your jurisdiction's own sale requirements?

Generally, yes.

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3.6 Example 5: If (a) the seller is located in your jurisdiction (irrespective of the obligor's location), (b) the receivable is governed by the law of your jurisdiction, (c) the seller sells the receivable to a purchaser located in a third country, (d) the seller and the purchaser choose the law of the purchaser's country to govern the receivables purchase agreement, and (e) the sale complies with the requirements of the purchaser's country, will a court in your jurisdiction recognise that sale as being effective against the seller and other third parties (such as creditors or insolvency administrators of the seller, any obligor located in your jurisdiction and any third party creditor or insolvency administrator of any such obligor)?

The answer to this question will generally be the same as the answer to question 3.4 above.

4 Asset Sales

4.1 Sale Methods Generally. In your jurisdiction what are the customary methods for a seller to sell receivables to a purchaser? What is the customary terminology – is it called a sale, transfer, assignment or something else?

Sales of receivables in securitization transactions are generally structured as outright sales of all of the seller's right, title and interest in, to and under the receivables and the related assets, and all proceeds of the foregoing. The transfer is valid and enforceable between the parties if the purchaser gives value, the seller owns or has the power to sell the accounts receivable and the sale is evidenced by an otherwise binding and enforceable contract. However, whether the transfer will be respected as a "true sale" or re-characterized as a security interest will depend on a number of factors discussed below in question 4.9. Sale terminology is customarily used to refer to these transactions, although governing documents will often use a combination of terms as a precaution. As described below, regardless of whether the transaction is characterized as a true sale or a secured lending, perfection will be required to make the transfer enforceable against third parties.

4.2 Perfection Generally. What formalities are required generally for perfecting a sale of receivables? Are there any additional or other formalities required for the sale of receivables to be perfected against any subsequent good faith purchasers for value of the same receivables from the seller?

For sales of types of receivables not covered by the answer to question 4.3, the sale is perfected by the filing of a UCC financing statement that identifies the seller, the purchaser and the receivables being sold. The financing statement must be filed in the appropriate filing office of the jurisdiction in which the seller is "located" – determined as provided in the answer to question 3.4.

4.3 Perfection for Promissory Notes, etc. What additional or different requirements for sale and perfection apply to sales of promissory notes, mortgage loans, consumer loans or marketable debt securities?

Receivables evidenced by promissory notes or negotiable instrument, or that constitute "payment intangibles", "chattel paper", or "marketable securities", all have different perfection rules.

Promissory Notes

A sale of "promissory notes" (most residential and commercial mortgage loans are evidenced by promissory notes) is automatically perfected, and no UCC financing statement needs to be filed or other action needs to be taken to perfect the sale. However, automatic perfection would not be applicable in the event that the sale was re-characterized as a security interest rather than a true sale and, accordingly, to protect against this risk, it is customary for a buyer to either take possession of the promissory notes or file a UCC financing statement to ensure that the buyer is perfected in the event of such a re-characterization. In addition, if the purchaser fails to take possession of promissory notes it may be possible for another party who takes possession to obtain superior rights in the promissory notes. In the U.S., most mortgage loans are evidenced by promissory notes.

Payment Intangibles

Mortgage loans that are not evidenced by promissory notes or other instruments are classified under the UCC as "payment intangibles" and are also automatically perfected. Again, it is customary to perfect by filing a financing statement to protect against the risk of re-characterization of the sale as a security interest rather than a true sale. A "payment intangible" is a type of "general intangible" under the UCC, and perfection of security interests in other types of general intangibles can be perfected only by filing a UCC financing statement.

Chattel Paper

In contrast to promissory notes and payment intangibles, a sale of chattel paper must be perfected regardless of whether characterized as a sale or a more traditional security interest. A sale of "tangible" chattel paper (*i.e.*, evidence by traditional, hard copy writing) may be perfected either by filing a UCC financing statement or by the purchaser (or its agent) taking possession of the chattel paper. A sale of "electronic" chattel paper may be perfected either by filing a UCC financing statement or by the purchaser taking control of the chattel paper. In the case of conflicting security interests, a purchaser that gives new value and takes possession (or control in the case of electronic chattel paper) of the chattel paper in good faith, in the ordinary course of the purchaser's business, and without knowledge that doing so violates the rights of another party, will have priority over a purchaser that perfects by filing.

Marketable Debt Securities

Sales of marketable debt securities are governed by Article 8 of the UCC, rather than as a "secured transaction" under Article 9 of the UCC. A purchaser that gives value and obtains "control" of the securities, without notice of any adverse claim, is a "protected purchaser" of the securities. A protected purchaser's ownership interest will be free from attack by any other person claiming a security interest or other property interest in the securities. The necessary steps to achieving "control" over marketable debt securities involve (a) in the case of certificated securities, taking possession of such securities together with a written assignment executed by the seller, (b) in the case of uncertificated securities, either (i) having the securities transferred on the books and records of the issuer into the name of the purchaser, or (ii) having the issuer agree that it will follow the purchaser's instructions regarding disposition or redemption of the securities being sold without the further consent of the seller, and (c) in the case of securities maintained in a securities account, either (i) having the securities transferred and credited to the purchaser's own securities account, or (ii) having a securities intermediary that maintains the securities

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account to which the securities are credited agree that it will follow the purchaser's instructions regarding disposition or redemption of the securities being sold without the further consent of the seller. Control may be obtained by the secured party itself or, in some cases, another person on behalf of the secured party.

With respect to securities maintained in a securities account, the Hague Convention on the Law Applicable to Certain Rights in Respect of Securities held with an Intermediary became effective in the U.S. on April 1, 2017 and such Convention has choice of law rules that may be applicable to securities maintained in a securities account.

4.4 Obligor Notification or Consent. Must the seller or the purchaser notify obligors of the sale of receivables in order for the sale to be effective against the obligors and/or creditors of the seller? Must the seller or the purchaser obtain the obligors' consent to the sale of receivables in order for the sale to be an effective sale against the obligors? Whether or not notice is required to perfect a sale, are there any benefits to giving notice – such as cutting off obligor set-off rights and other obligor defences?

Obligor notification is not required in order for a sale of the sellers' rights in respect of the receivable to be effective as between the seller and the purchaser. However, the general rule under the UCC is that *only* once the obligor receives notice that the receivable has been sold: (i) can the purchaser enforce the payment obligation directly against the obligor; and (ii) must the obligor pay the purchaser in order to be relieved of its payment obligation. In addition, notifying the underlying obligor of the assignment has the advantage of preventing such obligor from exercising against the purchaser a right of set-off or defence that the obligor might have had against the seller and that accrues after the obligor receives notice of the assignment (although an obligor always retains the right of recoupment arising from the transaction that gave rise to the receivable) and, in those cases where the receivable has been fully earned by performance, prevents any amendment to the receivables contract without the consent of the purchaser. If, alternatively, the receivables are evidenced by a "negotiable instrument", a purchaser who becomes a holder in due course may enforce directly against the obligor and takes free and clear of defences arising from the seller's conduct, subject to a few exceptions under consumer protection laws. Similar rights are available to protected purchasers of debt securities.

Generally, a seller or obligor insolvency will not limit the ability of the purchaser of receivables to give notice to the obligors of the assignment of those receivables. The purpose of the notification requirement is to avoid the obligor being required to pay twice.

Unless the contract expressly requires such consent, obligor consent is generally not required under U.S. common law in order for a sale of the sellers' rights in respect of the receivable to be effective as between the seller and the purchaser. The answer to the question of whether the language of the receivables contract changes the general rule depends upon the type of receivables involved. Generally, under the UCC, a provision in a non-consumer account receivable and certain other types of receivables which prohibits or restricts its sale, or which provides that a sale may give rise to a default, breach, right of recoupment, claim, defence, termination or remedy, is ineffective. However, the UCC provides that if a receivable containing such a prohibition is evidenced by a "promissory note" or is classified under the UCC as a "payment intangible", although the sale is effective as between the purchaser and the seller the purchaser cannot enforce the receivable against the obligor and the sale does not impose any duty or obligation on the obligor.

4.5 Notice Mechanics. If notice is to be delivered to obligors, whether at the time of sale or later, are there any requirements regarding the form the notice must take or how it must be delivered? Is there any time limit beyond which notice is ineffective – for example, can a notice of sale be delivered after the sale, and can notice be delivered after insolvency proceedings have commenced against the obligor or the seller? Does the notice apply only to specific receivables or can it apply to any and all (including future) receivables? Are there any other limitations or considerations?

As noted in the response to question 4.4 above, notice to the obligor is required only to the extent of imposing certain obligations on the obligor. There is no specific form specified for delivery of notice other than that the notice must be an "authenticated record", *i.e.*, in a signed writing or the electronic equivalent thereof. Generally, there is no time limit for the delivery of such a notice, though, as noted above, there are advantages in giving the notice sooner rather than later and a seller or obligor insolvency should not limit the ability of the purchaser of receivables to give notice to the obligors of the assignment of those receivables, so long as the assignment was fully consummated before the commencement of the insolvency proceeding. The purpose of the notification requirement is to avoid the obligor being required to pay twice. A notice to an obligor need not be limited to a specific set of receivables and can cover future receivables as long as those receivables are identifiable.

4.6 Restrictions on Assignment – General Interpretation. Will a restriction in a receivables contract to the effect that "None of the [seller's] rights or obligations under this Agreement may be transferred or assigned without the consent of the [obligor]" be interpreted as prohibiting a transfer of receivables by the seller to the purchaser? Is the result the same if the restriction says "This Agreement may not be transferred or assigned by the [seller] without the consent of the [obligor]" (i.e., the restriction does not refer to rights or obligations)? Is the result the same if the restriction says "The obligations of the [seller] under this Agreement may not be transferred or assigned by the [seller] without the consent of the [obligor]" (i.e., the restriction does not refer to rights)?

The first two formulations are likely to be viewed as a contractual restriction on the assignment of the seller's rights, whereas the third formulation is unlikely to be so characterized. However, as discussed in the answer to question 4.4 the UCC will nonetheless override such restriction on assignment either in whole or in part depending on the type of receivable.

4.7 Restrictions on Assignment; Liability to Obligor. If any of the restrictions in question 4.6 are binding, or if the receivables contract explicitly prohibits an assignment of receivables or "seller's rights" under the receivables contract, are such restrictions generally enforceable in your jurisdiction? Are there exceptions to this rule (e.g., for contracts between commercial entities)? If your jurisdiction recognises restrictions on sale or assignment of receivables and the seller nevertheless sells receivables to the purchaser, will either the seller or the purchaser be liable to the obligor for breach of contract or tort, or on any other basis?

Generally, such restrictions will not be effective to prevent the

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granting of the security interest, though, as noted in the answer to question 4.4, in some cases such security interest will not be unenforceable against the underlying obligor.

4.8 Identification. Must the sale document specifically identify each of the receivables to be sold? If so, what specific information is required (e.g., obligor name, invoice number, invoice date, payment date, etc.)? Do the receivables being sold have to share objective characteristics? Alternatively, if the seller sells all of its receivables to the purchaser, is this sufficient identification of receivables? Finally, if the seller sells all of its receivables other than receivables owing by one or more specifically identified obligors, is this sufficient identification of receivables?

No, the sale document need not specifically identify each receivable to be sold, but it must nonetheless provide a means for identifying objectively receivables that have been sold. Under the UCC, a security interest can be created in a broad category of assets (such as accounts receivable). If all receivables have been sold, no further identification should be required.

If all receivables have been sold other than receivables owing by one or more specifically identified obligors, a description of collateral referencing all receivables (other than certain clearly identified excluded receivables) can be an adequate description of collateral.

4.9 Recharacterisation Risk. If the parties describe their transaction in the relevant documents as an outright sale and explicitly state their intention that it be treated as an outright sale, will this description and statement of intent automatically be respected or is there a risk that the transaction could be characterised by a court as a loan with (or without) security? If recharacterisation risk exists, what characteristics of the transaction might prevent the transfer from being treated as an outright sale? Among other things, to what extent may the seller retain any of the following without jeopardising treatment as an outright sale: (a) credit risk; (b) interest rate risk; (c) control of collections of receivables; (d) a right of repurchase/redemption; (e) a right to the residual profits within the purchaser; or (f) any other term?

Whether a receivables transfer will be recognized as a "true sale" (and not as a secured loan), in most states it is determined by judge-made common law. As a result, judicial authority analysing transfers as true sales is not always consistent. Several courts have given presumptive weight to the intent of the parties. Other courts, seeking the "true nature" of a transaction, have regarded the parties' intent as only one attribute of a transaction, and have balanced those attributes of a transaction indicative of a secured loan against those attributes indicative of a sale, in order to determine whether the transaction more closely resembles a sale or a secured loan. Where commercially sophisticated parties have characterized transactions as sales, and acted consistently with that characterization, courts have generally been unwilling to disturb that characterization even though the transactions may also bear certain attributes of secured loans. Upon a showing by "clear and convincing evidence", however, that the transaction had the economic substance of a "disguised financing", courts may invoke their equitable power to re-characterize the transaction accordingly.

Generally, a key element to finding that a sale took place, as opposed to a loan, is that recourse to the seller is limited or non-existent. Recourse to the seller can take several forms. Recourse for the uncollectibility of the receivables and recourse to provide a contracted rate of return are often cited in cases re-characterizing transactions as loans.

On the flip side, if the purported seller retains material benefits of ownership, such as the right to participate in profits from the asset, courts may view such retained benefits as being more indicative of a loan than a sale. Related to that, while not necessarily dispositive, a right of repurchase may adversely affect the characterization of the transaction as a true sale. A small number of states have laws that purport to give effect to the parties stated intent that the transaction constitutes as "true sale" however it is unclear if such laws would be respected in bankruptcy.

Nine states have enacted statues of broad applicability that preclude re-characterization of a sale. For example, Section 9-109(e) of the Texas UCC provides:

(e) The application of this chapter to the sale of accounts, chattel paper, payment intangibles, or promissory notes is not to re-characterize that sale as a transaction to secure indebtedness but to protect purchasers of those assets by providing a notice filing system. For all purposes, in the absence of fraud or intentional misrepresentation, the parties' characterization of a transaction as a sale of such assets shall be conclusive that the transaction is a sale and is not a secured transaction and that title, legal and equitable, has passed to the party characterized as the purchaser of those assets, regardless of whether the secured party has any recourse against the debtor, whether the debtor is entitled to any surplus, or any other term of the parties' agreement.

While the Texas and Louisiana statutes are limited to receivables, the statutes in the other seven states apply to the sale of property of any kind and not just receivables but only if made pursuant to a securitization transaction as defined in such statutes. For example Delaware Code Ann. tit 6, §2703A provides in part:

(a) Notwithstanding any other provision of law, including, but not limited to, § 9-506 of this title, "Debtor's right to redeem collateral," as said section existed prior to July 1, 2001, and § 9-623 of the title, "Right to redeem collateral," which became effective July 1, 2001, to the extent set forth in the transaction documents relating to a securitization transaction:

(1) any property, assets or rights purported to be transferred, in whole or in part, in the securitization transaction shall be deemed to no longer be the property, assets or rights of the transferor;

(2) a transferor in the securitization transaction, its creditors or, in any insolvency proceeding with respect to the transferor or the transferor's property, a bankruptcy trustee, receiver, debtor, debtor in possession or similar person, to the extent the issue is governed by Delaware law, shall have no rights, legal or equitable, whatsoever to reacquire, reclaim, recover, repudiate, disaffirm, redeem or re-characterize as property of the transferor any property, assets or rights purported to be transferred, in whole or in part, by the transferor; and

(3) in the event of a bankruptcy, receivership or other insolvency proceeding with respect to the transferor or the transferor's property, to the extent the issue is governed by Delaware law, such property, assets and rights shall not be deemed to be part of the transferor's property, assets, rights or estate.

....

Nevertheless, because of uncertainty as to whether a bankruptcy court will respect such laws, most securitization transactions seek to comply with the traditional judicial requirements for a true sale described above.

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4.10 Continuous Sales of Receivables. Can the seller agree in an enforceable manner to continuous sales of receivables (i.e., sales of receivables as and when they arise)? Would such an agreement survive and continue to transfer receivables to the purchaser following the seller's insolvency?

Yes, a seller can agree to continuous sales of receivables in the U.S.; however, the bankruptcy code will generally cut-off the purchaser's interest in any receivables that are generated after the seller files for bankruptcy.

4.11 Future Receivables. Can the seller commit in an enforceable manner to sell receivables to the purchaser that come into existence after the date of the receivables purchase agreement (e.g., "future flow" securitisation)? If so, how must the sale of future receivables be structured to be valid and enforceable? Is there a distinction between future receivables that arise prior to versus after the seller's insolvency?

Prior to insolvency, yes, as long as the receivables in question are sufficiently specified by the sale agreement. The effectiveness of sales of receivables arising after the bankruptcy of the seller could be uncertain. If both the seller and the purchaser have continuing duties to perform, the agreement could constitute an "executory contract" which may be rejected by the seller's bankruptcy trustee.

4.12 Related Security. Must any additional formalities be fulfilled in order for the related security to be transferred concurrently with the sale of receivables? If not all related security can be enforceably transferred, what methods are customarily adopted to provide the purchaser the benefits of such related security?

Generally, attachment and perfection of a security interest or sale of receivables in accordance with the formalities described in the answers to questions 4.1, 4.2 and 4.3 will result in automatic attachment and perfection of a security interest in a security interest securing the receivable, the related security or any letter of credit supporting payment of such receivable.

4.13 Set-Off; Liability to Obligor. Assuming that a receivables contract does not contain a provision whereby the obligor waives its right to set-off against amounts it owes to the seller, do the obligor's set-off rights terminate upon its receipt of notice of a sale? At any other time? If a receivables contract does not waive set-off but the obligor's set-off rights are terminated due to notice or some other action, will either the seller or the purchaser be liable to the obligor for damages caused by such termination?

No, the secured party will always take subject to the right of recoupment and the rights of set-off under the contract. However, the right to set-off will only be effective with respect to claims accruing prior to the obligor's receipt of a notice of assignment. The obligor's claims against the assignee are limited to the amount the obligor owes the assignee.

4.14 Profit Extraction. What methods are typically used in your jurisdiction to extract residual profits from the purchaser?

The type of profit extraction used in connection with U.S. securitizations typically vary based on the nature of the assets being sold and/or securitized, the type of credit enhancement being used, the rating agency and timing considerations and accounting and regulatory capital treatment which may be applied. Typical forms of profit extraction include the right to receive distributions from the purchaser, including in the form of junior classes of notes issued by the purchaser or equity interests in the purchaser, or otherwise having a right to receive a deferred purchase price based on collections of the related assets.

However, as noted in our response to question 4.9, a key element to finding that a sale took place, as opposed to a loan, is that the parties intend for the purchaser to assume the economic risk and benefit of the receivables acquired by a purchaser, including the credit risk of the underlying obligors and the benefits otherwise associated therewith. Retention of right to receive residual profits or other forms of recourse by the seller are often cited in cases re-characterizing transactions as loans and therefore such profit extraction is typically limited based on applicable bankruptcy considerations.

5 Security Issues

5.1 Back-up Security. Is it customary in your jurisdiction to take a "back-up" security interest over the seller's ownership interest in the receivables and the related security, in the event that an outright sale is deemed by a court (for whatever reason) not to have occurred and have been perfected (see question 4.9 above)?

Yes, it is customary to take a back-up security interest in the event that the "sale" is not characterized as a true sale.

5.2 Seller Security. If it is customary to take back-up security, what are the formalities for the seller granting a security interest in receivables and related security under the laws of your jurisdiction, and for such security interest to be perfected?

As described in the answers to questions 4.2 and 4.3, the grant of a security interest in a receivable is generally perfected by the filing of a UCC financing statement. For instruments and tangible chattel paper, possession of the original is also available as a method of perfection. If the chattel paper is in electronic form, "control" is also an available method of perfection.

5.3 Purchaser Security. If the purchaser grants security over all of its assets (including purchased receivables) in favour of the providers of its funding, what formalities must the purchaser comply with in your jurisdiction to grant and perfect a security interest in purchased receivables governed by the laws of your jurisdiction and the related security?

The purchaser would be required to comply with the same formalities as did the seller, as provided in the answers to questions 4.2 and 4.3, although different locations of the purchaser and seller may result in the laws of a different jurisdiction being applicable to questions of perfection. Generally, if the relevant security agreement permits the filing of an "all assets" financing statement, and the purchaser has

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appropriately filed such a statement, no additional UCC filing will be required in order for the providers of such purchaser's funding to have a security interest in such receivables.

5.4 Recognition. If the purchaser grants a security interest in receivables governed by the laws of your jurisdiction, and that security interest is valid and perfected under the laws of the purchaser's jurisdiction, will the security be treated as valid and perfected in your jurisdiction or must additional steps be taken in your jurisdiction?

In general the parties' choice of law to govern the creation of the security interest will be respected if it bears a reasonable relationship to the transaction. The law governing perfection is subject to mandatory choice of law rules and the parties will not be able to override the mandatory choice of law rules governing perfection.

5.5 Additional Formalities. What additional or different requirements apply to security interests in or connected to insurance policies, promissory notes, mortgage loans, consumer loans or marketable debt securities?

Please see the answer to question 4.3.

5.6 Trusts. Does your jurisdiction recognise trusts? If not, is there a mechanism whereby collections received by the seller in respect of sold receivables can be held or be deemed to be held separate and apart from the seller's own assets (so that they are not part of the seller's insolvency estate) until turned over to the purchaser?

Yes, trusts of various forms are generally recognized in U.S. jurisdictions; however, if the transaction is classified as a security interest under the UCC (as discussed above, this includes the purchase of most receivables) then simply having the seller agree to hold the assets in trust for the purchaser will not be sufficient to avoid the perfection and other requirements of the UCC.

5.7 Bank Accounts. Does your jurisdiction recognise escrow accounts? Can security be taken over a bank account located in your jurisdiction? If so, what is the typical method? Would courts in your jurisdiction recognise a foreign law grant of security (for example, an English law debenture) taken over a bank account located in your jurisdiction?

Generally, jurisdictions in the U.S. will recognize escrow accounts, although the specific elements required for an escrow account and the specific legal status of an escrow account will vary by state. Generally, security can be taken over a deposit account in U.S. jurisdictions. Typically this is accomplished through a security agreement or pledge agreement with perfection being usually accomplished by an account control agreement whereby the depositary bank, the obligor and the secured party agree that the bank will follow the directions of the secured party rather than the account holder upon the occurrence of certain events. A court in the U.S. should recognize a foreign law grant of security taken over a bank account located in the U.S. as long as the form of security and perfection satisfied the requirement of control under the UCC, notwithstanding the law governing the instrument of control, subject to the choice of law, consideration addressed by the answers to the questions in section 2.

5.8 Enforcement over Bank Accounts. If security over a bank account is possible and the secured party enforces that security, does the secured party control all cash flowing into the bank account from enforcement forward until the secured party is repaid in full, or are there limitations? If there are limitations, what are they?

A secured party with control over a deposit account would have control over all funds thereafter credited to the deposit account; however, any bankruptcy filing by the grantor of the security interest would cut off the secured party's security interest as to funds credited to the account after the bankruptcy filing or within 90 days prior to the filing (one year if the secured party is an insider of the grantor).

5.9 Use of Cash Bank Accounts. If security over a bank account is possible, can the owner of the account have access to the funds in the account prior to enforcement without affecting the security?

Yes, the owner could have such access.

6 Insolvency Laws

6.1 Stay of Action. If, after a sale of receivables that is otherwise perfected, the seller becomes subject to an insolvency proceeding, will your jurisdiction's insolvency laws automatically prohibit the purchaser from collecting, transferring or otherwise exercising ownership rights over the purchased receivables (a "stay of action")? If so, what generally is the length of that stay of action? Does the insolvency official have the ability to stay collection and enforcement actions until he determines that the sale is perfected? Would the answer be different if the purchaser is deemed to only be a secured party rather than the owner of the receivables?

If the sale of receivables was a true sale that occurred prior to the commencement of the seller's insolvency proceeding, then the receivables involved in such a sale would not constitute property of the seller's bankruptcy estate. Accordingly, the automatic stay imposed by section 362 of the Bankruptcy Code would not prohibit the purchaser from exercising ownership rights over the purchased receivables. No insolvency official (such as a debtor-in-possession, bankruptcy trustee, creditors' committee or bankruptcy court) would have the right to stay or otherwise affect the purchaser's rights regarding the receivables while that insolvency official determines whether the sale was perfected. However, the insolvency official can allege during the insolvency proceeding that the sale in fact was a secured loan, rather than a true sale. If the court characterizes the sale as a loan rather than a true sale, the stay would remain in effect for the duration of the bankruptcy proceeding unless the secured party seek and receives a lifting of the stay from the court.

The answer would be different if the purchaser is deemed only to be a secured party, rather than the owner of the receivables. Specifically, if either (a) the transaction was, in fact, a secured loan, or (b) the purchaser was still required (as of the commencement of the seller's insolvency proceeding) to take some action under the sale agreement *vis-à-vis* the seller before it was contractually entitled to collect the receivables, then the receivables would remain property of the seller's bankruptcy estate. Accordingly, the automatic stay would prohibit actions by the purchaser to obtain possession of, or otherwise exercise control over, the receivables.

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The purchaser could file a motion with the bankruptcy court for relief from the automatic stay to allow it to collect or otherwise exercise control over the receivables. However, any party in interest in the insolvency proceeding could object to the motion, and the bankruptcy court could deny the motion.

6.2 Insolvency Official's Powers. If there is no stay of action, under what circumstances, if any, does the insolvency official have the power to prohibit the purchaser's exercise of its ownership rights over the receivables (by means of injunction, stay order or other action)?

If the transaction was a true sale, then the insolvency official normally does not have the power to prohibit the purchaser from exercising its rights as to the receivables purchased. However, the insolvency official conceivably could still request that the bankruptcy court issue an injunction or stay order (particularly if there is a question about whether the transaction was a true sale or if there was an infirmity in the transaction), and the bankruptcy court would have discretion in determining whether or not to grant such a request. The bankruptcy court has some leeway to fashion equitable relief.

6.3 Suspect Period (Clawback). Under what facts or circumstances could the insolvency official rescind or reverse transactions that took place during a "suspect" or "preference" period before the commencement of the seller's insolvency proceedings? What are the lengths of the "suspect" or "preference" periods in your jurisdiction for (a) transactions between unrelated parties, and (b) transactions between related parties? If the purchaser is majority-owned or controlled by the seller or an affiliate of the seller, does that render sales by the seller to the purchaser "related party transactions" for purposes of determining the length of the suspect period? If a parent company of the seller guarantee's the performance by the seller of its obligations under contracts with the purchaser, does that render sales by the seller to the purchaser "related party transactions" for purposes of determining the length of the suspect period?

The debtor-in-possession, bankruptcy trustee or other party with requisite standing can avoid a transaction that took place within two years before the commencement of the insolvency proceeding, if the transaction was a fraudulent transfer pursuant to section 548 of the Bankruptcy Code. The look-back period for fraudulent transfers is two years both for transactions between unrelated parties and for transactions between related parties and, as discussed below, the look-back period for "preferences" is generally 90 days for unrelated parties and one year where the recipient of the alleged preference is an affiliate of the debtor-transferor. Under section 548, a transaction constitutes a fraudulent transfer if the debtor (a) made a transfer or incurred an obligation with an actual intent to hinder, delay or defraud any entity to which the debtor was or became indebted, or (b) received less than a reasonably equivalent value in exchange for the transfer or obligation, and the debtor (i) was insolvent when the transfer was made or the obligation was incurred, or became insolvent as a result thereof, (ii) was engaged (or was about to engage) in a business or transaction for which any property remaining with the debtor was an unreasonably small capital, or (iii) intended to incur (or believed that it would incur) debts beyond its ability to pay as such debts matured. If a transaction is avoided as a fraudulent transfer, then a transferee that takes for value and in good faith would have a lien on, or may retain, any property the debtor transferred to it, but only to the extent that the transferee gave value to the debtor in exchange for the transfer.

Pursuant to section 544 of the Bankruptcy Code, the debtor-in-possession, bankruptcy trustee or other party with requisite standing can avoid a transaction under applicable non-bankruptcy law. For example, a transaction could be avoided under state fraudulent transfer law. Most state fraudulent transfer statutes are based on the Uniform Fraudulent Transfer Act, and others are based on the older Uniform Fraudulent Conveyance Act. These statutes contain elements that are similar to those set forth in section 548 of the Bankruptcy Code, though the look-back period under state fraudulent transfer statutes generally is longer than that under section 548. For example, the statute of limitations under the Uniform Fraudulent Transfer Act is four years after the transfer was made.

If the transaction is deemed to be a secured loan by the special purpose vehicle to the originator, then the debtor-in-possession, bankruptcy trustee or other party with requisite standing can avoid transfers made by the debtor-originator in connection with the transaction as preferential transfers, pursuant to section 547 of the Bankruptcy Code. Preferential transfers are those made (a) to a creditor, (b) on account of an antecedent debt owed by the debtor before the transfer was made, (c) while the debtor was insolvent, and (d) that enable the creditor to receive more than it would have received in a chapter 7 (liquidation) case. Given the requirement that the payment be on account of antecedent debt (as opposed to the purchase price of property paid at the time of sale), the concept of a preference is usually not applicable to true sales (unless there is a portion of the purchase price that is deferred and paid after the sale has closed).

Generally, only transfers made within 90 days before the commencement of the insolvency proceeding are subject to avoidance as preferential transfers. However, transfers made to a special purpose vehicle within one year before the commencement of the insolvency proceeding may be subject to avoidance, because such transfers may be deemed to have been made to an "insider" (*i.e.*, a related party). Courts typically recognize payments to fully-secured creditors as not being preferential. Even if the plaintiff can establish all of the elements of a preference claim, there are a number of statutory affirmative defences available to creditors, including defences for transfers made in the ordinary course of business and transfers in which the creditors provided contemporaneous or subsequent new value to the debtor.

6.4 Substantive Consolidation. Under what facts or circumstances, if any, could the insolvency official consolidate the assets and liabilities of the purchaser with those of the seller or its affiliates in the insolvency proceeding? If the purchaser is owned by the seller or by an affiliate of the seller, does that affect the consolidation analysis?

Courts have the equitable power to order substantive consolidation under section 105(a) of the Bankruptcy Code. Substantive consolidation has the effect of consolidating the assets and liabilities of multiple legal entities and treating them as if the liabilities were owed by, and the assets held by, a single legal entity. Inter-company claims and guarantees by consolidated entities are disregarded. Substantive consolidation may be ordered with respect to related entities that are all the subject of an insolvency proceeding, and also may be ordered with respect to related entities where some are the subject of an insolvency proceeding and the others are not.

Courts in the U.S. do not apply a uniform standard in determining whether to order substantive consolidation. However, a number of

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influential courts have stated that substantive consolidation is an extraordinary remedy that typically is reserved for circumstances in which (a) creditors had dealt with the various legal entities as a single economic unit and did not rely on their separate identity in extending credit, or (b) the affairs of the entities were so entangled that substantive consolidation would benefit creditors. Courts are more likely to order substantive consolidation when principal parties consent.

In the past, courts have relied on a consideration of the following factors (among others) to guide their analysis of whether the relationships between multiple legal entities are so obscured that they could not be disentangled:

(1) the presence or absence of consolidated financial statements;
(2) the unity of interests and ownership between various corporate entities;
(3) the existence of parent and inter-corporate guarantees on loans;
(4) the degree of difficulty in segregating and ascertaining individual assets and liabilities;
(5) the transfer of assets without observance of corporate formalities;
(6) the commingling of assets and business functions; and
(7) the profitability of consolidation at a single physical location.

Recent court decisions have adopted an open-ended, equitable inquiry to determine whether to substantively consolidate multiple legal entities. These courts have focused on the need in insolvency proceedings to protect the pre-petition expectations of creditors. Both case law and policy considerations indicate that a court primarily should base its determination on whether or not substantive consolidation would be equitable to the respective creditors of the entities for which substantive consolidation is sought.

When a special purpose vehicle is used as part of a securitization transaction, parties rely on the separate corporate existence of that special purpose vehicle. The special purpose vehicle should be monitored to ensure that (a) corporate formalities are observed, (b) the assets and liabilities of the special purpose vehicle can be readily distinguished from those of the originator, (c) the separate legal existence of the special purpose vehicle and the originator are disclosed to third parties, and (d) the special purpose vehicle is appropriately limited in its investments, indebtedness, business and ownership. If this is the case and the originator were to become a debtor in an insolvency proceeding, then it is unlikely that a court would order substantive consolidation of the originator and the special purpose vehicle if a party objects.

Under the foregoing substantive consolidation analysis, it is extremely unlikely that two companies that are not closely affiliated would satisfy the requirements for substantive consolidation. For two unaffiliated companies to be consolidated, active fraud by those in control of the entities would almost certainly have to be involved.

6.5 Effect of Insolvency on Receivables Sales. If insolvency proceedings are commenced against the seller in your jurisdiction, what effect do those proceedings have on (a) sales of receivables that would otherwise occur after the commencement of such proceedings, or (b) on sales of receivables that only come into existence after the commencement of such proceedings?

The commencement of an insolvency proceeding of the originator would create uncertainties as to sales of receivables that have not yet occurred and sales of receivables that have not yet come into existence.

First, many future flow securitizations are structured such that there is recourse back to the originator (which may take the form of a guarantee from the originator). The existence of such recourse could cause a court to conclude that the future flow securitization was not a true sale, but rather, was a secured loan.

Second, the receivables generated after the commencement of the originator's insolvency proceeding could be deemed to be included in the originator's bankruptcy estate, thus triggering the automatic stay as to those receivables. In addition, receivables generated after the commencement of the originator's insolvency proceeding generally would not be subject to a lien resulting from the security agreement entered into by the originator and the special purpose vehicle before the bankruptcy filing (unless such receivables are the proceeds, products, offspring or profits of assets acquired prior to the bankruptcy filing and subject to a security agreement).

Third, if the assets securitized are receivables that arise under executory contracts, there is a risk that in an insolvency proceeding involving a party to the contract, that party would "reject" the executory contract and no further receivables would be generated. The term "executory contract" is not defined in the Bankruptcy Code, but numerous courts have described it as a contract under which the obligations of both the debtor and the non-debtor are so far unperformed that the failure of either party to complete performance would constitute a material breach that excuses the performance of the other party. A debtor's decision to reject an executory contract is subject to bankruptcy court approval, and parties have an opportunity to object to a proposed rejection. However, bankruptcy courts generally will approve the rejection of executory contracts so long as the debtor demonstrates a valid business justification for its decision to reject. The rejection of an executory contract is treated as a court-authorized breach by the debtor, and gives rise only to an unsecured claim by the non-debtor party for damages.

6.6 Effect of Limited Recourse Provisions. If a debtor's contract contains a limited recourse provision (see question 7.3 below), can the debtor nevertheless be declared insolvent on the grounds that it cannot pay its debts as they become due?

Generally, no. However, some courts in certain U.S. jurisdictions may find that a debtor is insolvent on the grounds that it cannot pay its debts as they come due notwithstanding limited recourse provisions in the debtor's contracts. Such a finding of insolvency may be used to trigger springing recourse liability, which may allow lenders to pursue the assets of the debtor and/or certain guarantors pursuant to applicable "bad boy" provisions in the underlying loan documents.

7 Special Rules

7.1 Securitisation Law. Is there a special securitisation law (and/or special provisions in other laws) in your jurisdiction establishing a legal framework for securitisation transactions? If so, what are the basics? Is there a regulatory authority responsible for regulating securitisation transactions in your jurisdiction?

Although there is no federal statue on securitization, as noted in our answer to question 4.9 nine states have statutes that seek to facilitate securitizations by bolstering the true sale analysis.

To implement the credit risk retention requirements described in the answer to question 8.6 below, in October 2014 the Federal Deposit

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Insurance Corporation, the Federal Housing Finance Agency, the Office of the Comptroller of the Currency of the Department of the Treasury, the Securities and Exchange Commission, the Board of Governors of the Federal Reserve System and the U.S. Department of Housing and Urban Development jointly adopted final rules requiring a "sponsor" of a securitization (or a "majority-owned affiliate") to retain a portion of the credit risk of the securitized assets as more fully described below. In addition to establishing the requirements regarding credit risk retention, the rules also require the sponsor of a securitization to satisfy certain disclosure requirements both prior to and after giving effect to a securitization transaction.

7.2 Securitisation Entities. Does your jurisdiction have laws specifically providing for establishment of special purpose entities for securitisation? If so, what does the law provide as to: (a) requirements for establishment and management of such an entity; (b) legal attributes and benefits of the entity; and (c) any specific requirements as to the status of directors or shareholders?

Not as such. Certain U.S. federal tax laws, investment company regulations and securities laws have some provisions that facilitate securitization by providing special rules for special purpose entities that satisfy certain requirements. Most domestic securitizations in the U.S. use entities organized as corporations, limited liability companies or statutory trusts under the laws of Delaware. Trusts created under the laws of New York are also common. Some types of U.S. securitizations, such as CDOs, use entities domiciled in offshore jurisdictions such as the Cayman Islands.

7.3 Location and form of Securitisation Entities. Is it typical to establish the special purpose entity in your jurisdiction or offshore? If in your jurisdiction, what are the advantages to locating the special purpose entity in your jurisdiction? If offshore, where are special purpose entities typically located for securitisations in your jurisdiction? What are the forms that the special purpose entity would normally take in your jurisdiction and how would such entity usually be owned?

The answer to this question will generally be the same as the answer to question 7.2 above.

7.4 Limited-Recourse Clause. Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) limiting the recourse of parties to that agreement to the available assets of the relevant debtor, and providing that to the extent of any shortfall the debt of the relevant debtor is extinguished?

Courts in New York, if New York law is validly selected, typically will enforce limited-recourse clauses and any carve-outs thereto. These courts will determine, based on the facts of each case, whether any of the carve-outs to the limited-recourse clause apply in a particular situation. In interpreting the limited-recourse provision and its carve-outs, courts will analyse their language in an attempt to determine the intent of the parties. Courts will enforce the agreement of the parties, giving the contract language its normal and usual meaning. If a court determines that a carve-out to the limited-recourse clause applies in a particular case, then recourse may not be limited. Courts generally will give effect to a limited-recourse provision in a contract where the governing law is that of another country, unless the enforcement of that provision would offend the public policy of the state in which the court convenes as set forth in question 2.3.

Under section 1111(b) of the Bankruptcy Code, however, the general rule is that a secured claim in a Chapter 11 case is treated as a recourse claim, whether or not it is limited-recourse by agreement or applicable law. This section of the Bankruptcy Code converts limited-recourse claims to recourse claims, but also permits classes of undersecured creditors to elect to waive their deficiency claims and have their entire allowed claims treated as secured claims. This provision does not apply if the property is to be sold.

7.5 Non-Petition Clause. Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) prohibiting the parties from: (a) taking legal action against the purchaser or another person; or (b) commencing an insolvency proceeding against the purchaser or another person?

"Covenants not to sue" typically are governed by state law, and courts will interpret them in accordance with the rules governing the construction of contracts. To be enforceable, a covenant not to sue should be supported by adequate consideration by the beneficiary of the covenant. Courts very rarely refuse to enforce covenants not to sue that are negotiated in business transactions. However, they will not enforce covenants not to sue that violate applicable law or public policy.

Courts typically will also enforce contractual provisions prohibiting parties from commencing an involuntary insolvency proceeding against a purchaser or another person. Like covenants not to sue, courts will interpret these provisions in accordance with the rules governing the construction of contracts, and they should be supported by adequate consideration. However, covenants preventing entities from filing voluntary bankruptcy petitions probably are unenforceable.

7.6 Priority of Payments "Waterfall". Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) distributing payments to parties in a certain order specified in the contract?

In general, sophisticated parties may allocate proceeds of collateral and other payments among themselves by contract. Whether a U.S. court would apply a foreign choice of law depends on a wide range of factors, but in general such choice of law is likely to be upheld if the jurisdiction chosen has a substantial relationship to the transaction, and the application of such foreign law is not contrary to any fundamental policy of the applicable U.S. jurisdiction.

7.7 Independent Director. Will a court in your jurisdiction give effect to a contractual provision in an agreement (even if that agreement's governing law is the law of another country) or a provision in a party's organisational documents prohibiting the directors from taking specified actions (including commencing an insolvency proceeding) without the affirmative vote of an independent director?

Independent directors are often found in U.S. securitization transactions in order to limit the ability of the SPE to commence voluntary bankruptcy proceedings. However, an agreement by an entity not to file a voluntary bankruptcy petition may be

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unenforceable as against public policy. In fact, failure of a director to commence bankruptcy proceedings when he/she properly concludes that it would be in the best interest of the SPE to do so may constitute a breach of fiduciary duty.

7.8 Location of Purchaser. Is it typical to establish the purchaser in your jurisdiction or offshore? If in your jurisdiction, what are the advantages to locating the purchaser in your jurisdiction? If offshore, where are purchasers typically located for securitisations in your jurisdiction?

The location of purchaser generally depends on the transaction structure and the location of the underlying obligor(s). As noted in question 7.2, domestic purchasers typically use entities organized as corporations, limited liability companies or statutory trusts under the laws of Delaware. When a purchaser is located offshore, typical jurisdictions include the Cayman Islands among others based on the location of the underlying obligors and other relevant tax considerations.

8 Regulatory Issues

8.1 Required Authorisations, etc. Assuming that the purchaser does no other business in your jurisdiction, will its purchase and ownership or its collection and enforcement of receivables result in its being required to qualify to do business or to obtain any licence or its being subject to regulation as a financial institution in your jurisdiction? Does the answer to the preceding question change if the purchaser does business with more than one seller in your jurisdiction?

Receivables purchases generally do not subject a purchaser to licensing or other qualification requirements to do business in the U.S., although there may be exceptions to this rule from state to state depending upon the type of receivable. Collection and enforcement activities are more likely to require an entity to obtain a licence and qualify to do business within a state especially in the case of consumer receivables.

8.2 Servicing. Does the seller require any licences, etc., in order to continue to enforce and collect receivables following their sale to the purchaser, including to appear before a court? Does a third-party replacement servicer require any licences, etc., in order to enforce and collect sold receivables?

No general servicing licence is required. However, a servicer or replacement servicer may require the same licences possessed by the originator operating company depending upon the type of receivables and the jurisdiction involved. In addition, a servicer may need to meet certain licensing and other requirements with respect to collection and enforcement activities in limited instances.

8.3 Data Protection. Does your jurisdiction have laws restricting the use or dissemination of data about or provided by obligors? If so, do these laws apply only to consumer obligors or also to enterprises?

Confidential consumer information cannot generally be disclosed to third parties and can only be used for the purposes for which such information was provided. Entities possessing consumer information are generally obligated to safeguard such information from unauthorized access and disclosure.

8.4 Consumer Protection. If the obligors are consumers, will the purchaser (including a bank acting as purchaser) be required to comply with any consumer protection law of your jurisdiction? Briefly, what is required?

Consumer protection laws exist at both the federal and state levels in the U.S. A purchaser may be liable for the acts of the seller originating the receivable, as these liabilities are considered to pass to the holder of the receivable. In addition, a purchaser could be subject to debt collection laws, reporting laws and confidentiality laws, among other laws.

8.5 Currency Restrictions. Does your jurisdiction have laws restricting the exchange of your jurisdiction's currency for other currencies or the making of payments in your jurisdiction's currency to persons outside the country?

Federal anti-money laundering laws require financial institutions to implement due diligence procedures with respect to their customers in order to prevent the transfer of cash to certain prohibited persons.

8.6 Risk Retention. Does your jurisdiction have laws or regulations relating to "risk retention"? How are securitisation transactions in your jurisdiction usually structured to satisfy those risk retention requirements?

Yes, pursuant to the credit risk retention rules, 17 C.F.R. Part 246 ("U.S. Risk Retention Rules"), the sponsor of a securitization transaction is generally required to retain at least a 5 percent interest in the credit risk of the securitization, either directly or, in some cases, through a majority-owned affiliate. Such retention obligations are typically satisfied by retaining an "eligible horizontal residual interest", an "eligible vertical interest" or a combination of the foregoing. However, there are other alternatives for certain asset classes. For example, sponsors of revolving pool structures, such as credit card master trusts, can satisfy risk retention by holding a seller interest. Sponsors of RMBS pools comprised entirely of qualified mortgages do not have to hold risk retention at all. And a recent federal court ruling has made the risk retention rules inapplicable to the sponsors of "open market CLOs". Special provisions also apply to ABCP conduits, CMBS, and tender option bonds.

In structures involving an "eligible horizontal residual interest", the sponsor (or a majority-owned affiliate) typically retains an interest in a single class or multiple classes of subordinated or equity securities in the issuing entity. On any payment date or allocation date on which the issuing entity has insufficient funds to satisfy its obligation to pay all contractual interest or principal due, any resulting shortfall would then reduce amounts payable to the eligible horizontal residual interest prior to any reduction in the amounts payable to any other ABS interest, whether through loss allocation, operation of the priority of payments, or any other governing contractual provision (until the amount of such ABS interest is reduced to zero). In structures involving an "eligible vertical interest," the sponsor (or a majority-owned affiliate) typically would retain an interest in each class of ABS interests in the issuing entity issued as part of such securitization transaction that constitutes the same proportion (and at least five percent) of each such class. The sponsor (or majority-owned affiliate) is required to hold such retained interest for so long as required under the U.S. Risk Retention Rules, which vary by type of asset being securitized.

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In addition, the U.S. Risk Retention Rules prohibit the assignment, transfer or hedging of the portion of the retained economic interest that is intended to satisfy the requirements of the U.S. Risk Retention Rules, and the sponsor (or its applicable affiliate) may not pledge the retained credit risk as collateral for any financing unless such financing is full recourse to the sponsor (or such affiliate).

8.7 Regulatory Developments. Have there been any regulatory developments in your jurisdiction which are likely to have a material impact on securitisation transactions in your jurisdiction?

In addition to the same considerations discussed in the answer to question 8.6, the Dodd Frank Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act") created several new regulatory bodies. The Dodd-Frank Act required hundreds of new regulations, many of them focused on the financial services industry, and the agencies regulating the financial services industry also periodically adopt changes to their regulations and supervisory guidance and practices. The Dodd-Frank Act also requires regulations related to asset-backed securities (which included the U.S. Risk Retention Rules discussed in the answer to question 8.6). Proposals for legislation further regulating the financial services industry are continually being introduced in the U.S. Congress and in state legislatures. Congress continues to consider extensive changes to the laws regulating financial services firms, including bills that address risks to the economy. Regulations relating to the foregoing have been proposed, some of which have been adopted as final rules while others remain pending. Such regulations, including those that have been adopted to implement the more recent Basel internal ratings based and advanced measures approaches, may result in greater capital charges to financial institutions that own asset-backed securities or otherwise adversely affect the attractiveness of investments in asset-backed securities for regulatory capital purposes.

In addition, the Dodd-Frank Act required the SEC to, among other things, adopt new requirements for issuers, underwriters and third-party due diligence service providers to promote the transparency of the findings and conclusions of third-party due diligence as it relates to asset-backed securities. Among other things, these rules require an issuer or underwriter of an ABS that is to be rated by a nationally recognized statistical rating organization (NRSRO) to furnish a Form ABS-15G with the SEC containing the findings and conclusions of any third-party due diligence report obtained by the issuer or underwriter at least five business days prior to the first sale in the related offering.

Furthermore, the Financial Accounting Standards Board has adopted changes to the accounting standards for structured products. These changes, or any future changes, may affect the accounting for entities, and could under certain circumstances require an investor or its owner generally to consolidate the assets of an ABS issuer in their financial statements, and record third parties' investments in the Issuers as liabilities of that investor or owner, or could otherwise adversely affect the manner in which the investor or its owner must report an investment in asset-backed securities for financial reporting purposes.

9 Taxation

9.1 Withholding Taxes. Will any part of payments on receivables by the obligors to the seller or the purchaser be subject to withholding taxes in your jurisdiction? Does the answer depend on the nature of the receivables, whether they bear interest, their term to maturity, or where the seller or the purchaser is located? In the case of a sale of trade receivables at a discount, is there a risk that the discount will be recharacterised in whole or in part as interest? In the case of a sale of trade receivables where a portion of the purchase price is payable upon collection of the receivable, is there a risk that the deferred purchase price will be recharacterised in whole or in part as interest? If withholding taxes might apply, what are the typical methods for eliminating or reducing withholding taxes?

The following summary assumes that the sale of the receivables by the seller to the purchaser will be respected as a true sale for U.S. federal income tax purposes whereby the seller will not retain any interest in the receivables. Payments of interest on any interest-bearing receivables with maturities in excess of 183 days to the seller or the purchaser by obligors who are U.S. persons (hereinafter, "U.S. source interest") generally are subject to U.S. federal withholding tax if the seller or the purchaser is a non-resident of the U.S. The statutory rate of U.S. federal withholding tax generally is 30 percent, but this rate can be reduced to 0 percent (or other lower rate) by an applicable income tax convention between the U.S. and the seller's or purchaser's country of residence. In addition, certain payments of U.S. source interest are exempt from U.S. federal withholding tax under the "portfolio interest" exception to withholding but most receivables are not in the registered form necessary to meet this exception. In addition, for receivables that arise (or are deemed to arise) on or after 1 July 2014, such U.S. source interest payments generally will be subject to a 30 percent withholding tax under FATCA if paid to a "foreign financial institution" or a "non-financial foreign entity", unless (i) the foreign financial institution undertakes certain diligence and reporting obligations, (ii) the non-financial foreign entity either certifies it does not have any "substantial United States owners" or furnishes identifying information regarding each substantial U.S. owner, or (iii) the foreign financial institution or non-financial foreign entity otherwise qualifies for an exemption from these rules. Entities located in jurisdictions that have an intergovernmental agreement with the U.S. governing FATCA may be subject to different rules. The proceeds from dispositions of such receivables on or after January 1 2019 are also potentially subject to a 30 percent FATCA withholding tax. Furthermore, payments of U.S. source interest to the seller or the purchaser may also be subject to "backup withholding" if the seller or the purchaser does not provide the payer with the appropriate certification that it is exempt from backup withholding. Backup withholding currently is imposed at a rate of 24 percent. It is not an additional tax but rather an advance payment of tax which may later be credited or refunded. Payments of interest to the seller or the purchaser by an obligor who is not a U.S. person generally are not subject to U.S. federal withholding tax unless such interest arises from a branch in the U.S. maintained by such obligor. Depending on the particular facts, a purchase of a trade receivable at a discount could cause the discount to be treated as market discount to the purchaser for U.S. federal income tax purposes. Market discount accrued on a receivable held by a purchaser that is a non-resident of the U.S. will generally not be subject to U.S. federal withholding tax. Depending on the particular facts, a sale of a trade receivable where a portion

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of the purchase price is payable upon collection of the receivable could cause a portion of the purchase price to be re-characterized as interest income to the seller for U.S. federal income tax purposes. If so, U.S. federal withholding tax may apply to such interest if the buyer is a resident of the U.S. and the seller is not, in the absence of an applicable exemption.

If receivables with maturities in excess of 183 days are unregistered, one common method of causing such receivables to be treated as registered is by placing such receivables in grantor trusts whose ownership interest are in registered form.

9.2 Seller Tax Accounting. Does your jurisdiction require that a specific accounting policy is adopted for tax purposes by the seller or purchaser in the context of a securitisation?

Most taxpayers are required to use the accrual method of accounting. In certain limited cases, some securitization vehicles may elect to mark their assets to market.

9.3 Stamp Duty, etc. Does your jurisdiction impose stamp duty or other transfer or documentary taxes on sales of receivables?

There are no federal stamp duties or documentary taxes on sales of receivables, and these types of charges are unusual at the state level; however, Tennessee and Florida are states that have material taxes that need to be considered.

9.4 Value Added Taxes. Does your jurisdiction impose value added tax, sales tax or other similar taxes on sales of goods or services, on sales of receivables or on fees for collection agent services?

There are no federal value added taxes or sales taxes on sales of goods or services, on sales of receivables or on fees for collection agent services. Virtually all of the 50 states of the U.S. have some form of state sales tax on sales of goods or services. In general, no value added, sales or similar taxes will apply to sales of receivables or to fees for collection agent services.

9.5 Purchaser Liability. If the seller is required to pay value-added tax, stamp duty or other taxes upon the sale of receivables (or on the sale of goods or services that give rise to the receivables) and the seller does not pay, then will the taxing authority be able to make claims for the unpaid tax against the purchaser or against the sold receivables or collections?

As discussed above, there are no federal stamp duties or documentary taxes on sales of receivables. The ability of state taxing authorities to collect any value added tax, stamp duty or other taxes, if imposed, may vary.

9.6 Doing Business. Assuming that the purchaser conducts no other business in your jurisdiction, would the purchaser's purchase of the receivables, its appointment of the seller as its servicer and collection agent, or its enforcement of the receivables against the obligors, make it liable to tax in your jurisdiction?

If a non-resident purchaser is considered to be carrying on a trade or business in the U.S., it will be required to file a U.S. federal income tax return and, absent an applicable income tax convention between the U.S. and the country where the non-resident purchaser is resident, will be required to pay U.S. federal income tax on any income that is effectively connected with its carrying on of a trade or business in the U.S. (ECT). Typically, a purchaser resident in a country with which the U.S. has an income tax convention will only be subject to U.S. federal income tax on its ECT from a trade or business carried on through a permanent establishment in the U.S.

Whether or not the purchaser is carrying on a business in the U.S., or has a permanent establishment in the U.S., is a question of fact to be considered on a case-by-case basis. Particular attention must be given to the appointment of a seller resident in the U.S. as servicer and collection agent for a non-resident purchaser, in order that such appointment does not cause the purchaser to be considered to be carrying on a trade or business through a permanent establishment in the U.S. (thus giving rise to ECT).

9.7 Taxable Income. If a purchaser located in your jurisdiction receives debt relief as the result of a limited recourse clause (see question 7.3 above), is that debt relief liable to tax in your jurisdiction?

If a purchaser is relieved of limited recourse debt by using the assets securing such debt, a purchaser generally has taxable gain or loss. The amount of gain or loss is generally the difference between the amount of the debt satisfied and the purchaser's tax basis in such assets.

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