GUEST OPINION

EMERGING OPPORTUNITIES

In its overview of the common features of true sale securitisation in Central and Eastern Europe, Mayer Brown Rowe & Maw concludes that the technique is achievable under the general legal frameworks currently in place in all CEE jurisdictions.

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This article is intended to provide a brief overview of the common features of true sale securitisation transactions in Central and Eastern Europe (CEE). In a true sale securitisation, an originator generally transfers a pool of its assets to a special purpose vehicle (SPV) and the SPV finances the purchase by issuing debt instruments into the capital markets. A true sale is only achieved if the transfer legally isolates the assets from the insolvency risk of the originator.

Market review

As all CEE countries are civil law jurisdictions, their approach to securitisation transactions differs from that in common law jurisdictions. Civil law jurisdictions, with the formality of their civil codes, the inability to rely on equitable principles and the scarcity or uncertainty of case law applicable to the finance sector, pose special challenges to securitisation.

In addition to these challenges, several potential impediments have traditionally hindered the growth of securitisation transactions in the region, such as a lack of familiarity with securitisation concepts and structures; the overall cost of doing a transaction for the first time; the sufficiency of liquidity available to commercial banks through classic funding channels (parent funding, corporate and consumer deposits, and through the capital markets); the fact that plain vanilla products have historically generated profits comparable to those in mature markets; the fact that typical securitisable and homogenous banking portfolios of assets (eg car leases, mortgages and credit card portfolios) have only recently been built up to a significant volume; and the tax issues arising in various jurisdictions.

However, a confluence of factors, including a growing need to diversify funding sources, increased familiarity with securitisation structures, a desire to raise off-balance sheet financing and to transfer specified portfolio-associated risks to the capital markets, have been and will continue to drive the market forward.

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Legal considerations

The following summary is premised on the assumption that there is no special securitisation law in place in the CEE jurisdictions and that any potential transaction is based on general principals of local substantive law. Accordingly, we have examined and summarised the common features relating to choice of law, true sale, transfer of collateral, insolvency, data protection, licensing and

regulatory requirements, and the taxation regimes that apply to the CEE region.

Choice of law

The CEE countries recognise free choice of law as a general principle of their international private law systems, and provided that there is a foreign element in the contractual relationship, the parties can choose a foreign law to govern the assignment agreement. Pursuant to the provisions of the Treaty of Rome, which is implemented in the relevant jurisdictions, foreign law will, however, be set aside if its application would, in effect, be contrary to public policy or mandatory rules of local substantive law (eg conflicts with consumer protection laws).

True sale

In all CEE jurisdictions a true sale can be achieved by way of assignment. In the absence of special securitisation laws, the assignment is governed by the provisions of the relevant country's civil code.

An assignment agreement is valid upon the consent of the originator (the seller) and the SPV (the purchaser), and – unless the underlying contract prohibits such an assignment or expressly requires the consent of the debtor – debtor consent is not required. If the underlying contract contains a general prohibition on assignment, some jurisdictions, such as Bulgaria, treat the assignment as null and void; other jurisdictions, such as Romania or Serbia, require the consent of the debtor to override any prohibition.

Notification of underlying debtors is not usually a condition of a valid assignment. However, notice to debtors cuts off the debtor's right to discharge, set off or counterclaim its obligation against the originator, and also perfects the assignment against third parties (eg subsequent purchasers).

The assignment agreement does not need to comply with special formalities under general legal principles, other than in cases when the underlying contract expressly stipulates formalities to be followed in order to conclude a valid assignment or the assigned receivables are secured by a mortgage or pledge. In such cases any associated security may require re-registration in favour of the SPV, resulting in incremental costs and formalities.

The assignment of future receivables is generally possible, to the extent that the receivables are capable of being sufficiently identified at the time of the transfer. Czech and Serbian laws do not, however, recognise the assignment of future receivables.

As in any CEE securitisation, transaction care must be taken to incorporate features to the structure minimising the risk that the true sale will be recharacterised as a secured financing. The parties should consider incorporating limited recourse provisions in the assignment, ensuring that full legal title in the receivables is transferred and should pay particular attention to segregation of cashflows if the originator is to continue servicing the receivables.

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Collateral

In most jurisdictions ancillary rights, such as security interests and guarantees, are automatically transferred to the SPV by operation of law together with the assignment of the underlying receivables, provided that such rights are attached to the assigned receivables. If the ancillary right is registered in a public registry, such as a mortgage or pledge, the transfer of such mortgage or pledge will only become effective upon re-registration in the land registry or the public registry for pledges. Re-registration in favour of the SPV will obviously prove crucial in the event of any enforcement scenario.

Insolvency

On the assumption that the true sale is valid, binding and enforceable, the assigned receivables are isolated from the estate of the originator, subject to distribution upon liquidation, and cannot be collected by an insolvency administrator in the event of an insolvency of the originator. However, the insolvency laws of the examined jurisdictions entitle the insolvency administrator, the creditors of the originator under insolvency, or both, to challenge the validity of the following transactions concluded by the originator: those diminishing the assets of the originator or defrauding its creditors; those concluded without consideration or at an undervalue; and those concluded for the purpose of giving unfair preference to the claim of a particular creditor or creditors.

The clawback periods vary throughout the region, from one month to five years prior to commencement of insolvency proceedings – although Croatia is an exception, with a suspect period of 10 years applicable only to challenging fraudulent transactions. In some jurisdictions, such as Bulgaria, insolvency rules applicable to originator banks provide slightly different provisions and clawback periods in comparison to corporate insolvency rules.

Data protection and bank secrecy

In a true sale transaction, the assignment and transfer of receivables owing from individuals must comply with data protection laws. In Europe, the Data Protection legislation limits the circumstances in which personal data can be passed from the data controller to another person and care must be taken to ensure that any transfer of personal data falls within one of the permitted grounds.

The transfer of personal data from a European Economic Area (EEA) country to a country outside the EEA must be on a basis that ensures that the personal data, when held in the non-EEA country, is subject to an adequate level of data

EMEA NEW MARKET STRUCTURED TRANSACTIONS (VOLUME & NUMBER)

Source: Moody's

protection. There are a limited number of countries which are recognised by the European Commission as having an adequate data protection regime, and where the recipient country is not one of these recognised countries it is common to put in place a contractual arrangement on model terms proposed by the Commission.

Importantly, the restrictions on transferring personal data do not apply to transfers within the borders of the European Economic Area. Personal data and data constituting business or bank secrets are subject to further special relevant data protection regimes in all CEE jurisdictions.

The severity of banking secrecy laws depends on the provisions of the relevant jurisdictions, though the strict requirements may be waived provided that certain legal requirements and conditions are satisfied and complied with. It should be noted that breaching bank secrecy rules is a criminal offence in all CEE jurisdictions.

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Licensing and regulatory

Licensing and regulatory requirements vary throughout the region. The purchasing and servicing of receivables does not, however, require a licence, provided that the purchasing of receivables is not deemed to be providing financial services under the provisions of the relevant legislation. Thus financial services provided by the originator or SPV are regulated activities and require a special licence issued by the local financial supervisory authority or the national bank.

Passporting of banking services by a purchaser in a cross-border transaction is generally available with certain restrictions applicable in cases of transfer of services to "third countries" (ie outside the EU and transfers to a country which is not an OECD member). Local exchange laws usually place no restrictions on money transfer and currency exchange, subject to the "third countries" exceptions referred to above.

In addition to the licensing and passporting restrictions, if the debtors of the assigned receivables are consumers, special consumer protection laws may be applicable, and derogation from such to the detriment of the consumer may render the assignment null and void. The future implementation of Basel II also imposes further capital adequacy requirements on originator banks.

Taxation

Other than in Poland, no stamp or transfer taxes are payable on the sale and purchase of receivables. If, however, the assignment requires certain formalities or the receivables are secured by registered charges, notarisation and statutory re-registration fees may be payable.

The VAT treatment of any transaction varies throughout the region. In some jurisdictions, such as Hungary, Serbia, Slovenia or Slovakia, the transfer of receivables does not attract VAT liability. The servicing of receivables, should it constitute a financial or financial intermediary service, is VAT-exempt in Poland, Hungary and Croatia.

With respect to withholding tax liabilities, as a general principle, payments will depend on the tax residency and the legal status of the investor (institutional or individual), the presence of double tax treaties in the relevant jurisdictions and whether the income originates from instruments traded on regulated markets. Inevitably, withholding tax risks exist in cross-border transactions where cash is passed from the originator resident in a CEE jurisdiction to an offshore SPV, in respect of certain payments under a swap or other derivative agreement entered into by the issuer for hedging purposes, or any form of external credit enhancement.

Withholding tax may also arise on payments derived from a pool of underlying assets and receivables that secure the SPV's rated obligations. The parties to any transaction should consider whether it is necessary or advisable to seek a tax ruling from the relevant authorities.

Future prospects

In order to alleviate current legal and commercial obstacles, new securitisation legislation is either in place, intended to be enacted or in the process of being prepared in most CEE countries. The purpose of special laws on securitisation is to achieve inter alia: legal certainty for the assignment of receivables; higher levels of efficiency and transparency in the transactions; bankruptcy remoteness for the onshore purchasing SPVs; and favourable taxation treatment.

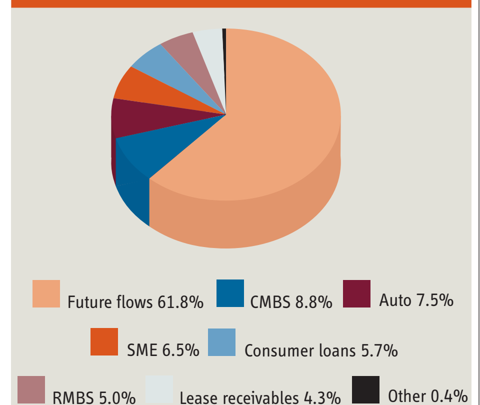
The aim is to enable different types of transactions, involving different types of originators and different forms of SPVs (including SPVs structured as funds) purchasing different types of assets (including future receivables). Securitisations are likely to be used by local banks (with, in some cases, the support of their Western parents), leasing and mortgage companies, and other originators. Possible support could come from experienced market participants, such as the World Bank, IFC or the European Investment Bank and European Investment Fund, as well as the provision of credit enhancement and higher ratings through guarantees for the senior classes of notes issued.

Recent deals, such as the Polish/Czech small business loans (ROOF CEE 2006-1), the LBBW/Balda Hungarian/German ABS trade receivables and the loan portfolio true sale securitisation transaction in Bulgaria (ProCredit Bank) are a healthy sign for the securitisation market, indicating that CEE investors and issuers are becoming more comfortable with securitisation as an efficient form of funding. Rating agencies expect to see securitisation in the CEE region increase, both in volume and in diversity.

Conclusion

In summary, true sale securitisation is achievable under the general legal frameworks currently in place in all CEE jurisdictions, and will be facilitated by future legislation.

EMEA NEW MARKET 2006 SECURITISATION BY ASSET TYPE



Source: Moody's