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Securitisation

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1. Structurally Embedded Laws of General Application

1.1 Insolvency Laws

Although the term "legal true sale" is used in German market practice by the parties to financial transactions, it cannot be defined by reference to a specific provision of German law. A German "legal true sale" as the term is used in the following document, and in German market practice, means:

- the insolvency-proof assignment/transfer of a financial asset from a seller (the originator) to a purchaser, with the effect that the sold and assigned/transferred assets cease to form part of the seller's insolvency estate in the event that the seller becomes insolvent subsequent to the assignment/transfer of the respective asset; and
- that the assigned/transferred asset is not exposed to the risk that the seller's insolvency administrator may successfully challenge the assignment/transfer of the asset, or that the seller's insolvency administrator may successfully raise claw-back rights with respect to the sold and assigned/transferred asset.

This requires that the seller is subject to German law insolvency proceedings. If there is a risk that a seller of the receivables/assets shall not be subject to German law insolvency proceedings, then it is advisable to examine whether or not a perfection of the sale and assignment/transfer of the receivables/assets under the receivables purchase agreement will be acknowledged under the non-German insolvency proceedings applying to the seller.

For the German legal true sale analysis, the most important aspect to consider in connection with the sale and assignment of a receivable is whether or not the seller has also transferred the credit risk (ie, the risk that the obligor would have to pay – on condition of its solvency – the receivables on the agreed date) to the purchaser. In contrast with a retained seller participation in the credit risk of a sold and assigned receivable, any retained seller risk in the verity or dilution risk will not be taken into account for German true sale analysis purposes.

If the seller is subject to insolvency proceedings under German law, there are no additional requirements for a legal true sale if the sale and assignment is non-recourse with respect to the credit risk of the receivables that have been sold. The transfer of the credit risk should not be questioned or re-characterised as an assignment of receivables for security purposes (*Sicherungszession*) with respect to receivables that will be purchased on a non-recourse basis, provided that the terms of the receivables purchase do not have the economic effect that the credit risk (*Delkredererisiko*) of the receivables has (despite the sale and assignment of them) in fact been retained by the seller. This would be the case if the seller's retained credit risk participation (due to retained purchase price provisions, default risk reserves, etc) were not at arm's length for a non-recourse receivables sale. It is notable in this context that retained dilution reserves or yield reserves or deemed collections due to broken representations and warranties will not impact the German legal true sale analysis.

The transfer of a sold and assigned receivable under a receivables purchase agreement could be questioned and re-characterised as an assignment of receivables for security purposes (*Sicherungszession*) – ie, as a secured lending transaction, with respect to receivables that will be purchased on a recourse basis. In the latter case, the acquirer of receivables for security purposes will, in the case of the commencement of German law insolvency proceedings against the seller, be treated as a preferred creditor and will have a right to separate satisfaction (*Absonderungsrecht*). If the transaction contemplates a secured loan facility (as opposed to a receivables purchase agreement) secured by the receivables, then the assignment of the receivables would be deemed a security assignment rather than a true sale.

Under German law, it is not possible to combine both principles: there is no "true sale for security purposes". In the case of a re-characterisation of a sale of receivables as a secured lending transaction, and in the case of the commencement of German insolvency proceedings against the transferor, German insolvency law provides that the insolvency administrator of the German transferor will mandatorily enforce and collect receivables that had been transferred for security purposes (unless such security qualifies as financial collateral in the sense of Directive 2002/47/EC), meaning that the acquirer would be barred from enforcing the receivables assigned to it itself or through an agent. The insolvency administrator is, however, obliged to transfer the proceeds from such an enforcement of receivables for security purposes to the acquirer. The German insolvency administrator will, however, deduct fees from such enforcement proceeds, as provided for under German insolvency law. These fees amount to 4% of the enforcement proceeds for the determination of the receivables, plus up to a further 5% for the enforcement process (or, under certain conditions, more or less than 5%) plus applicable VAT.

A true sale should be structured as a so-called "cash transaction", which means that the receivables are sold for immediate and equivalent consideration. If the sale is characterised as a cash transaction, then most of the reasons to challenge the sale and transfer under German insolvency law are excluded. Qualification as financial collateral has the effect of excluding some of the reasons to challenge the transaction, but not as many as would be excluded in a cash transaction.

1.2 Special Purpose Entities

Issuers of German asset-backed securities are typically organised as bankruptcy remote special purpose entities (SPEs). Depending on the type of the securitised asset, SPEs are either located in Germany (eg, in the case of a bank loan, auto loan or consumer loan securitisations) or outside of Germany (eg, in the case of auto leases or trade receivables) – mostly Luxembourg, Ireland and The Netherlands. The choice of appropriate SPE jurisdiction is driven mainly by tax considerations, set-up and maintenance costs and confidence in the legal system's ability to ensure a ring-fencing of the assets.

An SPE is typically established as an "orphan" by corporate service providers. Its share capital is held by charitable trusts or charitable foundations.

The corporate structure and organisation of an SPE follows (for public term transactions) the requirements of the applicable rating criteria or securitisation platform provider – eg, True Sale International GmbH (TSI as brand for German quality securitisations) or Prime Collateralised Securities (PCS) UK Limited (True Sale PCS Label).

An SPE's activities will be restricted by negative covenants in the transaction documentation as required by the rating agencies or the respective securitisation platform (TSI/PCS) in order to ensure that the activities of the SPE are limited to those required in connection with the acquisition of the securitised assets and the issued asset-backed securities. An SPE will, in particular, refrain from having its own employees, incurring indebtedness or granting security other than in connection with the securitisation. All transaction parties contracting with the SPE need to agree on non-petition clauses not to commence insolvency proceedings against the SPE, and limited recourse provisions limiting each party's claims against the SPE on the assets acquired by it and the enforcement of such claims in accordance with the provisions of the transaction documents and the agreed priority of payments ("waterfall payments").

Under German insolvency legislation each legal entity will be treated as an independent insolvency subject, with the consequence that an independent SPE will not be consolidated with the originator for insolvency purposes.

Legal opinions obtained in connection with securitisation transactions will typically include statements that the SPE has been validly established in the relevant jurisdiction, as well as statements relating to the corporate capacity of the SPE. In the case of a German SPE, a German legal opinion will not usually contain non-consolidation opinions regarding the consolidation of the SPE's assets and liabilities with the originator for insolvency purposes. German legal opinions issued for securitisation transactions will, however, address the legal, valid and binding transfer of the assets by the originator to the SPE that grants a right for segregation in the case of the originator's subsequent insolvency, as well as the legal, valid and binding granting of security by the SPE to the transaction trustee that can be segregated from the transaction trustee's insolvency estate should the transaction trustee become insolvent. German legal opinions issued for securitisation transactions will also address the validity of limited-recourse and non-petition provisions.

1.3 Transfer of Financial Assets

Usually, the seller and purchaser of financial assets (ie, receivables) will enter into a receivables purchase agreement (RPA).

German law distinguishes between the sale and purchase at the contractual level and the actual in rem transfer of title to the receivables, which is achieved by an assignment. The RPA usually deals with both aspects: the contractual relationship (ie, the sale and purchase) between the seller and the purchaser, and the assignment of the receivables, by means of which the actual title to the receivables is transferred to the purchaser.

The sale and assignment of receivables is perfected by entering into the RPA, which provides for the assignment of the sold receivables. No further registration or notification steps are required.

German law does not recognise any bona fide acquisition (*gutgläubiger Erwerb*) of claims and receivables. As a consequence, pledges over claims and receivables governed by German law cannot be validly granted on a bona fide basis. Hence, receivables need to exist at the time of assignment to the purchaser, and need to be owned by the seller. Once title to a receivable has been transferred to another person, the seller cannot validly transfer or encumber title to the receivable to any third party.

The legal true sale of a German law-governed receivable is perfected under the terms of the RPA between the seller and the purchaser. Notification to the obligor is not required under German law for the perfection of the German law receivables assignment. However, from a practical perspective, obligor notification is required if the purchaser wants to enforce the collection of due receivables directly.

1.4 Construction of Bankruptcy-Remote Transactions

As outlined in **1.1 Insolvency Laws**, for ensuring a bankruptcy remote transaction structure it is essential that in addition to the insolvency proof sale and assignment of the financial asset from the seller to the purchaser or SPE it is crucial that the sale and assignment must not re-characterised due to the retention of credit risk participation to a secured lending transaction and is structured to meet for German insolvency proceeding purposes the requirements as a so-called "cash transaction", which significantly reduces the risk that the sale and assignment of the financial asset is exposed to challenge and claw-back rights of seller's insolvency administrator.

2. Tax Laws and Issues

2.1 Taxes and Tax Avoidance

Payments on receivables (eg, trade receivables), including interest payments, are not generally subject to withholding taxes in Germany. Exceptions may apply, for example, to receivables qualifying as hybrid debt instruments, receivables the obligor of which is a bank or financial services institution in Germany, securitised receivables, and – in limited circumstances – receivables secured by German real estate.

Germany does not impose any stamp duty or other documentary taxes on the sale of receivables.

2.2 Taxes on SPEs

The purchase of receivables would not generally result in German tax liability for a non-German purchaser if the purchaser did not conduct any other business in Germany and the receivables did not give rise to income from German sources (where receivables may generate German-source income, see the exceptions in **2.1 Taxes and Tax Avoidance**).

German tax liability could arise for the purchaser if the receivables were collected, monitored and/or administrated by a German originator or servicer, and the services provided resulted in a permanent representative, a permanent establishment or an effective place of management of the purchaser situated in Germany. To limit the risk of this, a non-German purchaser should display a substantial presence outside Germany and not maintain a fixed place of business inside Germany. Moreover, all relevant business decisions of the purchaser, especially in relation to the acquisition of receivables and its financing, should be made abroad. Further, the purchaser should not provide instructions in respect of the collection services performed by the originator or servicer, and such entities should not have the power to represent or legally bind the purchaser.

2.3 Taxes on Transfers Crossing Borders

In general, the sale of receivables is exempt from German VAT. An exception might apply if not only receivables but entire contractual relations were transferred. However, this is not usually the case in a true sale securitisation.

VAT may be imposed on factoring services – eg, on collection services provided by the purchaser. However, no factoring services are generally provided if, following a sale, the seller continues to collect the receivables (as is frequently the case in a true sale securitisation).

2.4 Other Taxes

In respect of a sale of trade receivables that originate from the sale of goods and services being subject to VAT, a purchaser may become secondarily liable for any VAT not duly paid by the seller. A secondary liability does not generally exist if and to the extent that the purchaser pays a consideration for the receivables to the free disposition of the seller.

2.5 Obtaining Legal Opinions

From a tax perspective, legal opinions in relation to securitisations usually cover:

- potential stamp taxes and withholding taxes;
- the tax treatment of the SPE;
- potential VAT on the transfer of the receivables and the services provided to the SPE; and
- secondary tax liabilities.

3. Accounting Rules and Issues

3.1 Legal Issues with Securitisation Accounting Rules

The Institute of Auditors (*Institut der Wirtschaftsprüfer*) summarised the requirements for a true sale for German commercial balance sheet purposes in its statement dated 1 October 2003 (IDW RS HFA 8, as amended on 9 December 2003 – the IDW statement). Pursuant to this statement, a true sale of receivables for accounting purposes can be assumed if the economic ownership of the receivables is passed to the purchaser of the receivables. This is the case if, among other things, the following criteria are fulfilled:

- from an economic perspective, the credit risk (ie, the risk that the debtor of the receivables does not meet its payment obligations) is assumed by the purchaser;
- the sale of the receivables is final (which would not be the case, for example, if the reassignment/resale of the receivables had already been agreed at the time of the sale);
- there are no default guarantees from the seller and no total return swap is entered into between the seller and the purchaser, nor an agreement pursuant to which the purchase price will be adjusted in accordance with the losses of the sold receivables;

- the seller of the receivables does not hold equity in the purchaser and does not acquire debt securities issued by the purchaser (either in full or in a significant amount); and
- any purchase price discount agreed between the parties is either non-adjustable or, if adjustable, qualifies as appropriate and customary in the market (eg, because it is determined in accordance with the quota of actual past losses plus a reasonable risk surcharge).

3.2 Dealing with Legal Issues

Accounting analysis in relation to a securitisation is generally undertaken separately from the legal analysis.

In order to provide an opinion that the asset has been assigned on a true-sale basis for accounting purposes, legal practitioners ordinarily ensure through the documentation that the assignor bears no risk for the due realisation of the assigned assets and that representations and warranties are limited to title. To the extent that the assignor provides any undertaking to ensure realisation of any of the assets, or part thereof, the opinion is qualified to state that the true sale has not occurred to that extent. Hence, the receivables/assets which have not been subject to a true sale will continue to be accounted in the books of the assignor as a receivable.

4. Laws and Regulations Specifically Relating to Securitisation

4.1 Specific Disclosure Laws or Regulations

There is no specific German disclosure law applying to securitisations.

However, relevant regulations pursuant to applicable European law include, in particular, Regulation (EU) 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 (the Securitisation Regulation or SR), and any regulatory technical standards authorised thereunder.

The SR is applicable since 1 January 2019 to all securitisations (as defined therein) other than securitisations existing prior to that date to the extent that they are grandfathered.

Prior to holding a securitisation position, an institutional investor, other than the originator, sponsor or original lender, shall verify that (if established in the European Union) the originator, sponsor or original lender retains on an ongoing basis a material net economic interest and the risk retention is disclosed to the institutional investor each in accordance with the SR.

The originator, sponsor and SPE of a securitisation shall make at least the following information available to holders of a securitisation position, to the competent authorities and, upon request, to potential investors:

- information on the underlying exposures on a quarterly basis;
- all underlying documentation that is essential for the understanding of the transaction;
- where a prospectus has not been drawn up, a transaction summary or overview of the main features of the securitisation;
- in the case of simple, transparent and standardised (STS) securitisations, the STS notification;
- quarterly investor reports;
- any inside information relating to the securitisation that the originator, sponsor or SPE is obliged to make public in accordance with Article 17 of Regulation (EU) No 596/2014 of the European Parliament and of the Council (2) on insider dealing and market manipulation, or where this does not apply;
- any significant event such as:
  - (a) a material breach of the obligations provided for in the documents made available in accordance with the second bullet point above, including any remedy, waiver or consent subsequently provided in relation to such a breach;
  - (b) a change in the structural features that can materially impact the performance of the securitisation;
  - (c) a change in the risk characteristics of the securitisation or of the underlying exposures that can materially impact the performance of the securitisation;
  - (d) in the case of STS securitisations, where the securitisation ceases to meet the STS requirements or where competent authorities have taken remedial or administrative actions;
  - (e) any material amendment to transaction documents.

Certain specific disclosure requirements will also apply if the notes are intended to be admitted to trading on the regulated market at a stock exchange, or admitted as eligible collateral with the European Central Bank.

Regulation (EC) 1060/2009 of the European Parliament and of the Council of 16 September 2009 on credit rating agencies, as amended pursuant to Regulation (EU) 513/2011 of the European Parliament and the Council of 11 May 2011 and Regulation (EU) 462/2013 of the European Parliament and of the Council of 21 May 2013, also stipulates certain disclosure requirements.

4.2 General Disclosure Laws or Regulations

In practice, asset-backed securities are not offered to the public or retail investors (as defined under Directive 2014/65/EU (MIFID II)), but only to qualified investors (as defined in Regulation (EU) 2017/1129 of the European Parliament and the Council – the Prospectus Regulation). Therefore, no key information document pursuant to Regulation (EU) 1286/2014 or the PRIIPs Regulation is required.

Public German asset-backed securities issuances are mostly structured as "wholesale transactions" – ie, with a denomination of at least EUR100,000 and listed on the regulated market of Luxembourg or the Irish Stock Exchange. Such listing prospectus needs to comply with the requirements of the Prospectus Regulation for "wholesale" transactions.

Asset-backed securities that are intended to be placed with institutional investors (as defined in the SR) – eg, credit institutes, insurance enterprises, reinsurers, AIFMs or UCITs, need to comply with the transparency requirements of Article 7 of the SR. This provision requires that the originator, sponsor or SPEs of a securitisation transaction make the following information available:

- information on the underlying exposures on a quarterly basis, or in the case of ABCP, information on the underlying receivables or credit claims on a monthly basis;
- all underlying documentation (including the prospectus or, where a prospectus has not been drawn up in compliance with Directive 2003/71/EC of the European Parliament and the Council, a transaction summary or overview of the main features of the securitisation) that is essential for the understanding of the transaction;
- in the case of an STS securitisation, the STS notification pursuant to Article 27 of the SR;
- quarterly investor reports, or, in the case of ABCP, monthly investor reports; and
- any insider information relating to securitisations that the originator, sponsor or the SPE is obliged to make public in accordance with Article 17 of Regulation (EU) 596/2014 of the European Parliament and of the Council.

4.3 Credit Risk Retention

Asset-backed securities that are intended to be placed with institutional investors (as defined in the SR) – ie, credit institutes, insurance enterprises, reinsurers, AIFMs or UCITs, must comply with the risk retention requirements pursuant to Article 6 of the SR. The originator, sponsor or original lender of a securitisation shall retain, on an ongoing basis, a material net economic interest in the securitisation of not less than 5%. This retention of the material net economic interest in the securitisation can only be achieved by:

- the retention of not less than 5% of the nominal value of each tranche sold or transferred to investors ("vertical slice");
- the retention of the originator's interest of not less than 5% of the nominal value of each securitised exposures (in the case of revolving securitisations);
- the retention of randomly selected exposures, equivalent to not less than 5% of the nominal value of the securitised exposures;
- the retention of the first loss tranche; or
- the retention of a first loss exposure of not less than 5% of every securitised exposure in the securitisation.

The material net economic interest shall not be split among different types of retainers, or be subject to any credit-risk mitigation or hedging.

4.4 Periodic Reporting

Asset-backed securities that are intended to be placed with institutional investors (as defined in the SR) must publish quarterly investor reports, or, in case of ABCP, monthly investor reports (as per Article 7 or the SR).

4.5 Activities of Rating Agencies (RAs)

Regulation (EU) 462/2013 of the European Parliament and of the Council (the CRA3 Regulation) sets out a compulsory process of registration with the European Securities and Markets Authority (ESMA) for rating agencies (RA). German public asset-backed securities that shall serve as collateral for Eurosystem purposes (ECB collateral) are typically rated by two rating agencies and are structured to comply with ECB collateral eligibility criteria.

For more information on ECB collateral eligibility requirements, please visit www.ecb.europa.eu/paym/coll/loanlevel/implementation/html/index.en.html.

4.6 Treatment of Securitisation in Financial Entities

Credit institutions and investment firms have to calculate their regulatory capital as provided for under the CRR.

The regulatory capital risk weight of a securitisation position will depend, in particular, on the question of whether a securitisation position results from a traditional securitisation or meets the requirements of a simple, transparent and standardised securitisation (an STS securitisation) as defined by the SR.

Articles 20 to 22 of the SR define the STS criteria for non-ABCP securitisations as:

- for simple securitisation (Article 20 of the SR):

(a) legal true sale and no severe claw-back risk;
(b) specified perfection triggers;
(c) the seller's rep assets are neither encumbered, nor is transfer of them unenforceable;
(d) clear eligibility criteria, no active portfolio management on a discretionary basis, and any later-transferred assets meet the initial criteria;
(e) the assets are homogenous in terms of asset type, with full recourse to debtors (and guarantors), defined periodic payments (and sale proceeds) and no transferrable securities other than unlisted corporate bonds;
(f) the assets do not include securitisations;
(g) the assets originated in ordinary course of business, there are credit underwriting criteria and no "self-cert" residential loans;
(h) there are no assets in default, or exposures to credit-impaired obligors;
(i) at least one payment has been made (with exceptions); and
(j) repayment does not depend substantially on the refinancing or sale of assets,

- for standardised securitisation (Article 21 of the SR):
  (a) risk retention as per Article 6 of the SR;
  (b) interest rate and currency risks are hedged as per common standards, and there are no other derivatives;
  (c) interest payments match market rates or the "sectoral" cost of funds, and are not complex – ie, there are:
    (i) sequential payments and no cash trapping after enforcement or acceleration notice;
    (ii) specified triggers for sequential payments;
    (iii) specified triggers for early amortisation or termination of revolving periods (if any);
    (iv) provisions for continuity of servicing, replacement of liquidity and derivatives, etc;
    (v) servicer experience and documented policies, procedures and controls;
    (vi) clear and consistent definitions, remedies and actions relating to delinquency, default, etc; and
  (d) provisions for timely resolution of conflicts between classes of investors, clearly defined voting rights allocated to noteholders, etc; and
- for transparent securitisation (Article 22 of the SR):
  (a) at least five years of historical data for similar exposures;
  (b) third-party verification of asset samples before issuance;
  (c) provision of a liability cash flow model to investors before pricing, and on an ongoing basis;
  (d) for residential loans and auto loans or leases, disclosure of environmental performance;
  (e) disclosure by the originator and sponsor as per Article 7 of the SR – ie, of loan level data before pricing, transaction documents, prospectus or transaction summary and STS notification drafts before pricing; and
  (f) provision of final documents within 15 days after closing.

The following provides an overview of the risk weights (in %) for senior tranches under Basel II (RBA), SEC-ERBA (non-STS) and SEC-ERBA-STS:

- RBA (Basel II):
  (a) AAA: 1-year maturity – 7%; 5 years – 7%;
  (b) AA: 1-year maturity – 8%; 5 years – 8%;
  (c) A: 1-year maturity – 12%; 5 years – 12%;
  (d) BBB: 1-year maturity – 60%; 5 years – 60%;
  (e) BB: 1-year maturity – 425%; 5 years – 425%;
  (f) B: 1-year maturity – 1250%; 5 years – 1250%;
  (g) CCC±: 1-year maturity – 1250%; 5 years – 1250%;
  (h) <CCC-: 1-year maturity – 1250%; 5 years – 1250%.
- SEC-ERBA (non-STS):
  (a) AAA: 1-year maturity – 15%; 5 years – 20%;
  (b) AA: 1-year maturity – 25%; 5 years – 40%;
  (c) A: 1-year maturity – 50%; 5 years – 65%;
  (d) BBB: 1-year maturity – 90%; 5 years – 105%;
  (e) BB: 1-year maturity – 160%; 5 years – 180%;
  (f) B: 1-year maturity – 310%; 5 years – 340%;
  (g) CCC±: 1-year maturity – 460%; 5 years – 505%;
  (h) <CCC-: 1-year maturity – 1250%; 5 years – 1250%.
- SEC-ERBA-STS):
  (a) AAA: 1-year maturity – 10%; 5 years – 10%;
  (b) AA: 1-year maturity – 15%; 5 years – 20%;
  (c) A: 1-year maturity – 30%; 5 years – 40%;
  (d) BBB: 1-year maturity – 55%; 5 years – 65%;
  (e) BB: 1-year maturity – 135%; 5 years – 155%;
  (f) B: 1-year maturity – 280%; 5 years – 305%;
  (g) CCC±: 1-year maturity – 415%; 5 years – 455%;
  (h) <CCC-: 1-year maturity – 1250%; 5 years – 1250%.

4.7 Use of Derivatives

Derivatives are used in securitisations by banks for regulatory risk transfer and by SPEs to hedge interest rate risks and to hedge currency exchange risks.

4.8 Specific Accounting Rules

The Institute of Auditors (*Institut der Wirtschaftsprüfer*) summarised the requirements for a true sale for German commercial balance sheet purposes in its statement dated 1 October 2003 (IDW RS HFA 8, as amended on 9 December 2003 – the IDW statement). Pursuant to this statement, a true sale of receivables for accounting purposes can be assumed if the economic ownership of the receivables is passed to the purchaser of the receivables. This is the case if, among other things, the following criteria are fulfilled:

- from an economic perspective, the credit risk (ie, the risk that the debtor of the receivables does not meet its payment obligations) is assumed by the purchaser;
- the sale of the receivables is final (which would not be the case, for example, if the reassignment/resale of the receivables had already been agreed at the time of the sale);
- there are no default guarantees from the seller and no total return swap is entered into between the seller and the purchaser, nor an agreement pursuant to which the purchase price will be adjusted in accordance with the losses of the sold receivables;
- the seller of the receivables does not hold equity in the purchaser and does not acquire debt securities issued by the purchaser (either in full or in a significant amount); and
- any purchase price discount agreed between the parties is either non-adjustable or, if adjustable, qualifies as appropriate and customary in the market (eg, because it is determined in accordance with the quota of actual past losses plus a reasonable risk surcharge).

4.9 Investor Protection
The SR intends to provide investor protection to institutional investors (as defined in the SR) – ie, credit institutes, insurance enterprises, reinsurers, AIFMs or UCITs. Investor protection is achieved in particular by means of:

- pre-investment due diligence requirements for institutional investors (Article 5 of the SR);
- the originator, sponsor and original lender of a securitisation retaining, on an ongoing basis, a material net economic interest in the securitisation of not less than 5% (Article 6 of the SR);
- transparency requirements for the underlying exposures (loan-level information, documentation, investor reporting) (Article 7 of the SR);
- the ban on re-securitisations (Article 8 of the SR);
- the obligation to disclose the originator's criteria for the granting of credit (Article 9 of the SR); and
- the obligation to hold data in a securitisation repository (Article 17 of the SR).

4.10 Banks Securitising Financial Assets
The legal environment for securitisations of German regulated institutions is governed by the provisions of the CRR and the Securitisation Regulation. When German financial institutions securitise financial assets, they often use the German securitisation platform provider True Sale International and often structure securitisation transactions in line with the collateral requirements of the European Central Bank.

4.11 SPEs or Other Entities
German law does not provide for specific legislation relating to SPEs as securitisation companies. For further details, see **1.2 Special Purpose Entities**.

4.12 Activities Avoided by SPEs or Other Securitisation Entities
There is no legislation available in Germany that defines activities to be avoided by SPEs or other securitisation entities. Restrictions on SPEs or other securitisation entities result from rating criteria or the requirements defined by securitisation platform providers like TSI or PCS. For further details, see **1.2 Special Purpose Entities**.

4.13 Material Forms of Credit Enhancement
German securitisations can benefit from various forms of credit enhancement. However, if the issuer retains a significant interest in the credit risk attached to a sold and transferred financial asset, there is a risk that the transfer of a sold and assigned receivable under a receivables purchase agreement could be questioned and re-characterised as an assignment of receivables for security purposes (*Sicherungszession*) – ie, as a secured lending transaction – with respect to receivables that will be purchased on a recourse basis.

This risk should be mitigated if the terms of the receivables purchase do not have the economic effect that the credit risk (*Delkredererisiko*) of the receivables has been factually retained by the seller, despite the sale and assignment of them. This would be the case if the credit risk participation retained by the seller (due to, for example, retained purchase price provisions, default risk reserves, etc) were not at arm's length for a non-recourse receivables sale. It should be noted in this context that retained dilution reserves or yield reserves or deemed collections due to broken representations and warranties will not impact the German legal true sale analysis.

Credit enhancement means a contractual arrangement whereby the credit quality of a position in a securitisation is improved in relation to what it would have been if the enhancement had not been provided, including the enhancement provided by more junior tranches in the securitisation and other types of credit protection (Article 4 (1) 65 of the CRR).

Credit enhancement can be provided to a securitisation transaction in various forms, for example:

- the subordination of junior notes or the granting of subordinated loans to the issuer;
- deferred purchase price provisions;

- over-collateralisation (sale and transfer of financial assets to the issuer at a value greater than that of the consideration paid for them);
- excess spread (interest-bearing financial assets generating a greater interest cash flow than the coupon of the issued asset-backed security, or, in the case of non-interest-bearing assets, the discount being greater than the coupon); and/or
- cash reserves.

In particular, deferred purchase price provisions, excessive discounts or the transfer of receivables on a recourse basis could result in the risk (due to the participation in the sold and transferred receivable retained by the originator) that the sale and assignment of a receivable could be re-characterised as an assignment for security purposes (*Sicherungsabtretung*).

It is the prevailing view among legal practitioners that re-characterisation is dependent on the degree of default risk retained by the seller. If the credit risk retained by the seller were to be seen to be considerably higher than the historic default ratio relating to the portfolio of receivables sold to the purchaser, it could be argued that the originator has not transferred the credit risk in relation to the receivables to the issuer, and that the alleged sale effectively constitutes a secured loan on the basis that the seller of the receivables remains substantially exposed to the collection and credit risk attaching to the receivables.

Furthermore, although not necessarily in itself determining the insolvency treatment of a transaction which is intended as an assignment in the context of a sale (rather than a security assignment in the context of a secured loan), in the context of insolvency, the German accounting treatment of a securitisation transaction may be a strong indication of the relevance of the re-characterisation risk.

Where a transaction which is intended to constitute a sale results in the sold receivables no longer being entered in the originator's balance sheet under generally applicable German accounting rules, it is less likely to be treated as a secured loan, because the analysis of whether a sale constitutes a secured loan or a sale must follow a commercial approach.

Where a transaction is treated as a secured loan for accounting and/or tax purposes, the risk of it also being treated as a secured loan for legal purposes (including for the purposes of an analysis in the context of Section 166 of the *Insolvenzordnung* or Insolvency Statute) increases (see the final paragraph of **1.1 Insolvency Laws**).

4.14 Participation of Government-Sponsored Entities

There are currently no German government-sponsored entities active in German securitisations.

4.15 Entities Investing in Securitisation

According to True Sale International in 2018, UK investors (41%) followed by Benelux investors (11%) and US investors (10%) invested in European ABS. In 2018, European ABS was placed predominantly to funds (52%), pension funds (15%) and banks (29%).

5. Documentation

5.1 Bankruptcy-Remote Transfers

Under German law-governed true sale securitisations, the bankruptcy remote transfer of the assets to be securitised is typically achieved by three core transaction documents, consisting of:

- a receivables purchase agreement (RPA), entered into between the originator and the issuer;
- a servicing agreement entered into between the originator in its capacity as servicer, the security trustee as trustee and the issuer;
- a security trust agreement entered into between, among others, the issuer and the transaction security trustee; and
- in the case of sensitive personal obligor data or aspects which are covered by the principle of banking secrecy (*Bankgeheimnis*), the originator, the issuer, the security trustee and a data trustee enter into a data trust agreement.

Core Provisions of the RPA

The RPA defines in detail the receivables to be sold to the issuer (eg, by reference to an asset list), the purchase price to be paid by the issuer to the originator as equivalent for the transfer, as well as any collateral transferred by the originator to the issuer that secures the performance of the sold receivables. Collateral that secures the performance of the sold receivables is, in auto loan securitisations, typically the transfer of the originator's security title (*Sicherungseigentum*) to the financed vehicles, or in auto lease securitisations the transfer of the originator's title to the leased vehicles for security purposes to the issuer. The originator typically warrants that the sold receivables legally exist and will not be impaired or reduced by obligor defences or set-off rights, that the originator holds good and unencumbered title to the sold receivables, that the sold receivables comply with the eligibility criteria, that the originator will not amend its credit and collection policy without the issuer's consent, and that the credit and collection policy applied by the originator to the sold receivables is consistent with the credit and collection policy applied by the originator to its own (not securitised) receivables.

The RPA further stipulates that the originator must be deemed to have received deemed collections or benefits from indemnities if collections on the sold receivables will be reduced by non-credit risk or non-default risk related shortfalls (ie, sold receivables did not exist or became disputed receivables or are otherwise exposed to obligor defences and set-off rights). Under German law, notification of the obligor on the sale of a securitised receivable is not a requirement for the perfection of the issuer's title in the acquired receivables.

German RPAs typically provide that the obligor of the sold receivables is not notified on the sale of the securitised receivables by the originator to the issuer as long as the originator is in compliance with its contractual obligations under the RPA and the servicing agreement and in good financial standing. However, the issuer reserves the right to inform the obligor of the acquisition of the securitised receivables upon occurrence of an obligor notification event, which is typically combined with a servicer replacement event. Upon occurrence of an obligor notification event, the obligor will be informed of the acquisition of the securitised receivables by the issuer and will be asked to pay to the issuer directly.

Core Provisions of the Servicing Agreement

Under a tripartite servicing agreement entered into between the originator in its capacity as servicer, the issuer and the security trustee as trustee, the issuer appoints the originator as its servicer to service, administer, collect and enforce the securitised receivables and available receivables collateral (eg, financed or leased vehicles) in accordance with the originator's credit and collection policy and to transfer collections on securitised receivables to the issuer. The servicing agreement typically provides for indemnifications for any losses or damages arising from the issuer's reliance on information, representations, warranties and reports derived from or included in servicer reports or any claims which arise from the servicer's collection activities. Servicing agreements typically provide for the replacement of the originator/servicer by a third-party replacement servicer if a servicer replacement event is triggered (including, but not limited to, the originator's/servicer's insolvency).

Core Provisions of the Trust Agreement

The security trustee, originator/servicer, the issuer and all other transaction parties enter into a trust agreement. Pursuant to the terms of this trust agreement, the security trustee will on-transfer all assets and the related collateral acquired from the originator, and all claims against the servicer and other transaction parties, as note collateral to the security trustee. The security trustee will hold the collateral in trust for the beneficiaries, which include the noteholders. The key element of the trust agreement are the definition of the priority of payments (waterfall provisions), as well as the acceptance of the limited recourse and non-petition clauses by all transaction parties. The trust agreement contains issuer undertakings to the security trustee not to sell or charge the collateral, to refrain from all actions and omissions to act which may result in a significant decrease in the value or loss of the collateral, to have independent directors and not to enter into any other agreements unless such agreements contain limited recourse, non-petition and limitation on payments provisions, as defined in detail in the trust agreement.

Core Provisions of the Data Trust Agreement

In order not to disclose sensitive obligor data to the issuer which are subject to restrictions resulting from data privacy and are subject to disclosure restrictions resulting from the principle of banking secrecy (*Bankgeheimnis*), the RPA will contain (in order to ensure compliance with disclosure limitations required by the German regulator for German institutes, BaFin) provisions that the originator will disclose the identity (ie, name and address) of the obligor of bank loan receivables to the issuer only in encrypted form and that the decryption key will be safe kept by a data trustee. BaFin proposes to use as data trustee a credit institution licensed to do banking business in the EU or the EEA. However, in practice, data trustees are not always credit institutions. The data trust agreement provides that the identity of the respective obligors will not be disclosed to the issuer as long as the originator/servicer services the securitised receivables on behalf of the issuer. Upon replacement of the originator/servicer by a third-party replacement servicer (eg, in the case of servicer's insolvency or of a significant default of its obligations), the data trustee will provide the replacement servicer with the decryption key, enabling the replacement servicer to collect the securitised receivables on behalf of the issuer.

Corporate Administration Agreement

The issuer and a corporate service provider (as administrator) enter into a corporate administration agreement to provide corporate services to the issuer (ie, to provide the registered address, office services and accounting services for the issuer, to provide independent directors and arrange for the issuer's tax filings). The independent directors provided by the corporate service provider to the issuer have the obligation to ensure that the issuer does not carry out any activities, and in particular does not incur any financial indebtedness, other than as required for the specific securitisation transaction.

5.2 Principal Warranties

Please see **5.1 Bankruptcy-Remote Transfers**.

5.3 Principal Perfection Provisions

Please see **5.1 Bankruptcy-Remote Transfers**.

5.4 Principal Covenants

Please see **5.1 Bankruptcy-Remote Transfers**.

5.5 Principal Servicing Provisions
Please see **5.1 Bankruptcy-Remote Transfers**.

5.6 Principal Defaults
Please see **5.1 Bankruptcy-Remote Transfers**.

5.7 Principal Indemnities
Please see **5.1 Bankruptcy-Remote Transfers**.

5.8 Other Principal Matters
Please see **5.1 Bankruptcy-Remote Transfers**.

6. Enforcement

6.1 Other Enforcements
A key element of any legal, valid and binding transfer of a securitised financial asset is that there should be no assignment restrictions hindering the transfer of the asset, under the RPA, from the seller to the SPE. Section 399 of the German Civil Code (BGB) provides that a receivable cannot be transferred if assignment of it has been explicitly excluded by agreement with the obligor. It should be noted that the German principle of banking secrecy (*Bankgeheimnis*) does not hinder the assignment of bank loan receivables unless the bank and its customer have explicitly agreed on assignment restrictions.

As an exception to the general rule of Section 399 of the BGB, even an explicit contractual assignment restriction will not hinder the assignment of receivables if the receivable in question has been originated under a commercial contract between merchants to which Section 354a of the German Commercial Code (HGB) applies. Section 354a of the HGB provides that the assignment of monetary claims (ie, claims for the payment of money) governed by German law cannot effectively be contractually excluded if the underlying agreement between the contracting parties constitutes a commercial transaction (*Handelsgeschäft*), provided that such restriction on assignment was agreed on or after Section 354a of the HGB came into force on 30 July 1994.

In such circumstances, monetary claims to which such a restriction applies can be validly assigned notwithstanding a contractual restriction on assignment in the underlying contract, provided that the obligor under such a claim is a merchant (*Kaufmann*). Notwithstanding the fact that, to the extent to which Section 354a of the HGB provides that they are not enforceable, German courts would not enforce restrictions on the assignment of monetary claims, since the same section allows the obligor of an assigned claim to pay and discharge its obligations to the original creditor, even if the obligor had been notified of the assignment of its debt obligation. In the event that some of the obligors would not be merchants but instead consumers, sole traders or professionals, contractually stipulated restrictions on assignment would render any assignment in violation of such restrictions to be invalid.

It should be noted that German law does not allow for the securitisation of lease receivables under operating leases, since even in the case of a legal, valid and binding assignment of operating lease receivables, the SPE (as acquirer of the receivables) would be exposed to the risk of the originator becoming insolvent subsequent to the sale and transfer, and the originator's insolvency administrator discontinuing the originator's business operations and the relevant obligor stopping or withholding payments on the assigned operating lease receivables.

A legal true sale of lease receivables that have been originated by a German originator (seller) under a financial lease contract (eg, auto leases) can only be achieved if the requirements of Section 108, paragraph 1, sentence 2 of the German Insolvency Code (InsO) (henceforth, 108.1.2 InsO) are met. Pursuant to 108.1.2 InsO, leasing and rental agreements in respect of movable assets principally survive the institution of insolvency proceedings against the lessor if the acquisition of the leased assets are financed by a third party to whom the movable assets (eg, leased vehicles) have been transferred as collateral for such financing. This means that an assignment of claims from the leasing agreement which becomes due after the institution of insolvency proceedings against the lessor remains valid.

To date there is no case law or legal precedent available on this matter, but in accordance with the interpretation of the law by German legal scholars and securitisation practitioners, the applicability of 108.1.2 InsO is conditional on the acquisition of the leased assets having been financed by a third party, and the assets having been transferred to this third party for security purposes. Legal literature discusses whether these conditions are also met with regard to leasing assets financed for an interim period by a seller's own means or by means of third parties. Considering that it was the explicit aim of the legislator to maintain the validity of agreements on the assignment of future lease receivables in the event of the lessor's insolvency, and thereby to facilitate the refinancing of leases, it should not make a difference to the applicability of 108.1.2 InsO if the seller refinances the assets subsequent to a short interim period in compliance with 108.1.2 InsO.

What constitutes a "short interim period" depends on the circumstances of the interim financing and, in particular, whether or not the leasing enterprise has intended from the outset to refinance the acquisition of the leased assets in compliance with 108.1.2 InsO.

6.2 Effectiveness of Overall Enforcement Regime

Since German law does not provide for special securitisation legislation, the effectiveness and enforceability of securitisation transactions depends on the perfection of the transfer of the securitised financial asset by means of a legal true sale. For details on this, see **1.1 Insolvency Laws**.

As a further element to ensure the enforcement of the securitisation of financial assets, German securitisation transactions provide for the on-transfer of the securitised financial assets pursuant to the terms of a trust agreement between, among others, the SPE and the security trustee of the securitisation in question (see 'Core Provisions of the Trust Agreement' under **5.1 Bankruptcy-Remote Transfers**).

7. Roles and Responsibilities of the Parties

7.1 Issuers

Issuers are insolvency remote special-purpose vehicles. For further details, see **1.2 Special Purpose Entities**.

7.2 Sponsors

The sponsor is the party that usually initiates the securitisation transaction. The sponsor can be the originator of the receivables to be securitised or an affiliate, often being the parent company of the originator.

7.3 Underwriters and Placement Agents

Underwriters are usually also referred to as managers and/or arrangers, and are typically banks. Underwriters are responsible for arranging the securitisation transactions and for the marketing thereof. Together with the originator – which may also act as arranger – the underwriters underwrite the notes issued by the issuer.

7.4 Servicers

Servicing is usually undertaken by the seller (also referred to as originator) of the receivables.

7.5 Investors

Investors are typically banks or other financial institutions. The investors fund the issuer by subscribing the notes and paying the respective purchase price.

7.6 Trustees

Trustees are usually also referred to as "security trustees" or "collateral agents". Their function is to hold and administer (and in an enforcement scenario, also to enforce) the security granted over the assets of the issuer. The security is to be held in favour of the secured parties, in particular the noteholders.

8. Synthetic Securitisations

8.1 Synthetic Securitisation

Institutions in Germany primarily use synthetic securitisations for the purpose of regulatory risk transfer. The regulatory regime of synthetic securitisations is governed by the CRR. The current SR provides that the criteria for simple, transparent and standardised securitisations (STS securitisations) do not apply to synthetic securitisations. On 2 July 2019, the EBA published, together with a legislative proposal, a report on the feasibility of a specific framework for STS securitisations limited to balance-sheet synthetic securitisation.

A synthetic securitisation is a securitisation where the transfer of risk is achieved by the use of a credit derivative or a financial guarantee, and the exposures being securitised remain exposures of the originator institution (Article 242, paragraph 11 of the CRR). The credit derivative and financial guarantee is granted by a securitisation SPV to the originator with respect to a specific loan portfolio. By setting the relevant attachment point and detachment point for losses of interest and capital under the loan portfolio, the synthetic securitisation and first loss piece will be tranched.

If an interest or capital loss is determined under the loan portfolio due to a failure to pay, a bankruptcy or, under certain conditions, a restructuring, and is verified under the credit derivative or the financial guarantee within the relevant attachment and detachment points, then the securitisation SPV will be required to make a relevant payment to the originator under the credit derivative or financial guarantee. These payment obligations are funded by way of the proceeds from the issuance of a credit-linked note to investors. The cash proceeds from such an issuance serve as collateral and funding basis for the potential loss payments under the credit derivative or the financial guarantee.

A synthetic securitisation will be recognised for regulatory risk transfer purposes if the requirements of Article 244 of the CRR have been satisfied. This requires, inter alia, that an originator institution:

- had transferred significant risk to third parties, either through funded or unfunded credit protection; and
- the originator institution applies a 1.250% risk weight to all securitisation positions it holds in the securitisation or deducts these securitisation positions from its common equity tier 1 items in accordance with Article 36, paragraph 1 (k) of the CRR.

A regulatory risk transfer can also be achieved by an unfunded credit protection – ie, without raising debt from capital markets investors. In this case, the originator will enter into a credit default swap structure in accordance with the aforementioned CRR requirements.

Many other regulatory and legal questions arise in the context of synthetic securitisations and must be taken into account when structuring a transaction, including whether or not the derivatives regulation applies and whether or not the granting of financial guarantee is subject to a licence requirement. There are also limitations with respect to investors; most recently the German regulatory BaFin required the market to have investor protection criteria in place for credit-linked notes offered to retail investors.

8.2 Engagement of Issuers/Originators

No response provided.

8.3 Regulation

The legal environment for synthetic securitisations in Germany – and, in particular, for regulatory risk transfer – is governed by the CRR. Synthetic securitisations are currently not eligible for STS securitisations. However, in September 2019, the European Banking Authority EBA started the consultation process for synthetic STS securitisations.

8.4 Principal Laws and Regulations

See **8.1 Synthetic Securitisation for more information.**

8.5 Principal Structures

See **8.1 Synthetic Securitisation for more information.**

8.6 Regulatory Capital Effect

See **8.1 Synthetic Securitisation for more information.**

9. Specific Asset Types

9.1 Common Financial Assets

German securitisations refer to a wide range of financial assets, most commonly bank loan receivables, consumer loan receivables, auto loan receivables, auto lease receivables, SME loans or trade receivables. Due to the strong standing of German covered bonds (*Pfandbriefe*), true sale CMBS or RMBS securitisations are less common in the German market. However, synthetic CMBS, RMBS or ship portfolio securitisations have been seen in the German market with a focus on regulatory risk transfer. In contrast to other jurisdictions, credit card or student loan securitisations are of no relevance in Germany. Due to legal implications, whole-business securitisations or the securitisation of operating lease receivables are also difficult to implement.

9.2 Common Structures

The basic structure of a German securitisation transaction does not generally change based solely on the underlying securitised financial asset.

In line with European Central Bank's (ECB) collateral eligibility criteria securitisations of German credit institutions comply with ECB's loan level templates which are available for RMBS, CMBS, SME, consumer finance, leasing ABS, Auto ABS, credit card, ABS and public sector loans, whereby credit card ABS and public sector loan ABS is quite unusual for the German market. Since master trust structures, re-securitisations and residual value lease securitisations will not be accepted as ECB collateral, also the latter type of securitisations are not typical for a German securitisation structure.

Mayer Brown LLP has more than 100 structured finance lawyers in offices across the Americas, Asia and Europe, advising on all aspects of securitisation and structured finance transactions. The firm carried out the first CLO transaction in 1988, the first partially enhanced multi-seller commercial paper conduit in 1989 and the first TSI-certified securitisation in Germany (Driver One) in 2004. It has experience in the conduit, CDO and synthetic markets, and expertise in the areas of securitisation of intellectual property and non-performing loans, securitisation as an acquisition financing tool, large rescue structures for distressed assets or structured credit products and other hybrids or derivatives. Globally, Mayer Brown advises intensively on auto-related securitisations, helping leasing companies, banks and other auto lessors create like-kind exchange programmes on their own account and co-ordinating such programmes with titling trusts and securitisation structures. Its German securitisation practice advises on all aspects of securitisation and structured finance transactions, including factoring and asset-based lending transactions.

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