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The International Comparative Legal Guide to:

Securitisation 2019

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PREFACE

On behalf of Latham & Watkins, I would like to thank Global Legal Group for their efforts in publishing the 12th edition of *The International Comparative Legal Guide to: Securitisation*.

Maintaining an accurate and up-to-date guide regarding relevant practices and legislation in a variety of jurisdictions is critical, and the 2019 edition of this *Guide* accomplishes that objective by providing global businesses, in-house counsel, and international legal practitioners with ready access to important information regarding the legislative frameworks for securitisation in 26 individual jurisdictions.

The invitation to participate in this publication was well received by the world's leading law firms, thereby validating the continued growth and interest in securitisation around the world. We thank the authors for so generously sharing their knowledge and expertise, and for making this publication so valuable a contribution to our profession. The *Guide's* first 11 editions established it as one of the most comprehensive guides in the practice of securitisation. On behalf of Latham & Watkins, I am delighted to serve as the *Guide's* contributing editor and hope that you find this edition both useful and enlightening.

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Unlocking Value in Private Equity Transactions

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Introduction

Securitisation markets have been off to a cautious but steady start in 2019, despite lingering uncertainty over transparency requirements under the new EU Securitisation Regulation, risk retention in Japan, and political headwinds such as Brexit and the end of net asset purchases by the European Central Bank. By the end of March 2019, over €12 billion of new issuance priced in Europe, across a variety of asset classes. A number of transactions are in the pipeline, even in the midst of regulatory uncertainty. One of the asset classes that has attracted increased attention in recent times is private equity.

We discuss below how securitisation can be a valuable tool as a means of:

- financing or refinancing all or part of acquisitions of portfolio companies by private equity houses; and
- realising value in, or providing leveraged exposure to, private equity investments and illiquid assets.

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 limited partners’ investment commitments, 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. Of course, funding that 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, including:

- initial bridge financing;
- more permanent take-out financing;
- incremental financing, which permits private equity sponsors to extract some value after a period of initial success with an acquisition;

- refinancing all or any of that debt; and
- 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. Typically, the more homogenous and predictable the cash flows from the receivables, and the more impenetrable the ring-fencing, the lower the cost of the financing.

Securitisation financing can help lower the average cost of debt in an acquisition, therefore it permits private equity sponsors to bid more for target groups and can help private equity sponsors increase returns on equity – potentially both.

While securitisations can play an important role in each stage of financing, the complexity of structuring and documenting securitisation transactions means that these transactions 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, Latham lawyers have completed so-called “bridge” securitisation financings that 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. 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 applied to repay the loans to the issuer and to repay the rated securities to investors. Operating and financial covenants for a whole-business securitisation tend to be largely similar to those for leveraged loans. Whole-business securitisations generally require target groups with 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. This enhanced structure will likely enable the target group to achieve higher levels of borrowing and longer maturities than what is available in the leveraged loan or high-yield bond markets.

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 these 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), as well as 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 that lenders in the acquisitions originally provided. In fact, collateralised loan obligations (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, immediately 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 to 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 subsequent brief ramp-up period. 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 U.S.) 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 that 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 that the underlying assets generate 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 to acquire such equity interests. These 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 such vehicles offer to private equity sponsors are manifold, including the benefits 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 M&A or capital markets might otherwise allow. If pricing for an IPO is not attractive, securitisation can be a beneficial (even if temporary) way to raise funds at competitive pricing from investors who want a leveraged exposure to the investment.

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. The portfolio should have an expected realisation profile that, to the greatest extent possible, smooths out the cash flows to be received by the vehicle. Even then, a liquidity facility to pay interest in a timely manner on the most senior tranche of debt securities, as well as perhaps a funding reserve or other credit or liquidity enhancement, may well be needed. Over-collateralisation requirements for CFOs 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 of the LP will be required to consent to such transfer, and to consent 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 and interest cover tests similar to those used in CLOs and, sometimes, additional leverage ratios that need to be satisfied to permit distributions to the equity holder.

A New Regulatory Landscape

The EU Securitisation Regulation defines “securitisation” broadly and refers to a transaction or scheme whereby the credit risk associated with an exposure or a pool of exposures is tranching and has certain characteristics, including that: (a) payments in the transaction or scheme are dependent upon the performance of the exposure or of the pool of exposures; and (b) the subordination of tranches determines the distribution of losses during the ongoing life of the transaction or scheme.

While there is typically a transfer of risk in a whole-business securitisation, the risk is based on the value of a group of operating companies, reflected by the residual cash flows of the business. Whole-business securitisations could be structured in such a way as to conclude that the transfer of operational equity type risk falls out of scope of the EU Securitisation Regulation's risk retention, due diligence, and transparency requirements.

Market participants (and arguably regulators) have historically accepted this approach. However, such an equity-focused approach raises an equally important question – does the investment constitute an alternative investment fund (AIF) under the EU Alternative Investment Fund Managers Directive (AIFMD), or equivalent in other jurisdictions? For example, while CFO structures may look like CLOs, the notes are backed by funds rather than loan obligations. Falling within the AIFMD's scope comes with its own host of disclosure, authorisation, and conduct of business requirements (among others). In any event, the analysis will be fact-specific and individual transactions should be structured carefully to ensure the best result, whether by way of a securitisation, CFO, fund, or other structure.

Under the new EU Securitisation Regulation, originators, sponsors and issuers must comply with a direct obligation to make significant amounts of information and documentation relating to securitisations available to regulators, investors, and, upon request, potential investors. Such information includes underlying documentation, monthly or quarterly investor reports, data on the credit quality, cash flows and performance of the underlying assets, any material non-public information that the originator, sponsor, or issuer must disclose under market abuse legislation and any other "significant events" such as changes to the transaction's structure, risk profile, or documentation.

EU-regulated institutional investors already required much of this information as part of their own due diligence requirements under the previous rules. However, the new direct disclosure requirements come with administrative sanctions for non-compliance, even though the Commission has not yet finalised the reporting

templates. The extent to which wider disclosure and transparency requirements apply to originators and sponsors established outside the EU remains uncertain, even where the only EU nexus is European investors.

At the same time, CFO structures may avoid some costs normally associated with securitisations. For example, hedging for FX exposure may be avoided because of the significant equity cushion used for over-collateralisation. CFOs also should be structured to fall outside of the new EU Securitisation Regulation risk retention, credit granting and disclosure requirements, as they are more akin to a leveraged acquisition. The risk being tranching in relation to private equity funds that invest in leveraged buyouts is more equity in nature. The performance risk being taken by investors is effectively equity price risk and dividend risk on equity, rather than credit risk. This risk can be contrasted with classic securitisations such as residential mortgage loan securitisations and CLOs, in which case the risk shared by the different classes of notes would be the credit risk in relation to those loans.

In light of these developments, well-established private equity-related transaction structures may carry added appeal. Historically, such structures fell outside of EU risk retention and reporting obligations because they are structured to extract the residual cash flows of an operating group of companies, rather than to repackage the credit risk of debt obligations.

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. In light of recent developments, securitisation transactions can be a challenge to structure and complete relative to other forms of financing. However, they potentially offer a unique set of benefits and therefore are worth considering for private equity assets.

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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.

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 6 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. 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.

- 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

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

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 statutes 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.

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 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 depository 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 receive 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. 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 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 7.4 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? Does your jurisdiction define what type of transaction constitutes a securitisation?**

Although there is no federal statute 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 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 generally 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 relating to the form, holder and fair value of retained interests both prior to and after giving effect to a securitization transaction.

More generally, the Securities and Exchange Commission (the “SEC”) is the primary regulatory authority with respect to the administration and regulation of the U.S. Securities Act of 1933, as amended (the “Securities Act”), the U.S. Securities Exchange Act of 1934, as amended (the “Securities Exchange Act”), and other federal securities laws. As noted in the answers to questions 8.6 and 8.7, the Dodd Frank Wall Street Reform and Consumer Protection Act (the “Dodd-Frank Act”) adopted several regulations related to asset-backed securities (which included the U.S. Risk Retention Rules discussed in the answer to question 8.6), which 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.

While neither the Securities Act or the Exchange Act specifically define securitization, an “asset-backed security” is defined in Section 3(a)(79) of the Exchange Act, as amended by the Dodd-Frank Act, as a fixed-income or other security collateralized by any type of self-liquidating financial asset (including a loan, a lease, a mortgage, or a secured or unsecured receivable) that allows the holder of the security to receive payments that depend primarily on cash flow from the asset, including: a collateralized mortgage obligation; a collateralized debt obligation; a collateralized bond obligation; a collateralized debt obligation of asset-backed securities; a collateralized debt obligation of collateralized debt obligations; and a security that the SEC, by rule, determines to be an asset-backed security for such purposes; and does not include a security issued by a finance subsidiary held by the parent company or a company controlled by the parent company, if none of the securities issued by the finance subsidiary are held by an entity that is not controlled by the parent company. Similar definitions of asset-backed securities are used to determine whether a registered offering of securities falls into a special registration regime for asset-backed securities.

The SEC has also established a set of line-item disclosures for SEC-registered offering of asset-backed securities, known as Regulation AB, that differ significantly from disclosures for operating companies. The Regulation AB requirements include the provision of loan-level data for certain specified asset classes, including RMBS and auto loans. Issuers and underwriters tend to consider such disclosure requirements even in the context of unregistered deals, as a baseline of what would be considered to be material.

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 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 adopted under Section 15G of the Securities Exchange Act of 1934, as such may be amended from time to time ("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 (and, in the case of CMBS, the B-piece buyer may hold the risk retention in certain securitizations). 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 5 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.

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). A foreign safer harbour may also be available for securitizations that do not involve a US sponsor and that limit the initial issuance of the securities so that not more than 10 percent by value may be held by US investors (as defined under the U.S. Risk Retention Rules).

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 questions 7.1 and 8.6, 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. The time of first sale is generally considered to be the pricing of the offering of the securities, rather than the closing date.

In addition, the Dodd-Frank Act included the Volcker Rule, which restricts the ability of "banking entities" to acquire or hold ownership interests in "covered funds." A significant portion of U.S.-based securitizations involve an issuing entity that may be considered a "covered fund," and thus the offering documents for securitizations typically provide information as to the characterization of the issuing entity for purposes of the Volcker Rule. Other regulatory requirements that may also affect securitizations include: rules relating to the registration of investment companies; rules requiring an operator of a commodity

pool to become a registered entity (and that cause certain entities that own swaps to be treated as commodity pools); and rules that may impose margin or clearing requirements on issuing entities that enter into certain types of swaps.

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 July 1, 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. While the proceeds from dispositions of such receivables would have been subject to FATCA withholding on or after January 1, 2019, proposed U.S. Treasury regulations (on which taxpayers are entitled to rely) eliminate such withholding entirely. 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 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. (ECI). 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 ECI 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 ECI).

9.7 Taxable Income. If a purchaser located in your jurisdiction receives debt relief as the result of a limited recourse clause (see question 7.4 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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Mr. Safran has advised clients on commercial law and personal property transfer issues in connection with credit facilities, secured bond transactions, project financings, real estate securitizations, collateralized debt obligations, credit card and other receivables financings and other structured financing arrangements.

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