

## Increasing activity in the Belgian market **Stibbe**



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# Increasing activity in the Belgian market

Jan Peeters & Wouter Ghijsels

Stibbe

Belgium has seen increasing activity in its relatively small securitisation market especially in the fourth quarter of last year. In September 2004, an Antwerp based diamond trader, Rosy Blue Carat SA, closed a tap issue of US \$50,000,000 Class A2 Floating Rate Notes due in 2009 based on a securitisation of present and future stock of diamonds. The particular nature of the underlying asset raised specific issues with respect to for example insolvency events.

Two months later, the 'First Flemish Securitisation NV Compartment SKV2' issued 97,500,000 euros mortgage-backed floating-rate notes. The primary security for the notes was a pool of mortgage loans in the Flemish Region originated by 11 Social Credit Companies.

Around the same time, at the end of November, 'Beheersmaatschappij Antwerpen Mobiel' (BAM), the project company created to finance, manage and operate the transport infrastructure in and around Antwerp, successfully securitised a receivable ('single asset') on 'Tunnel Liefkenshoek NV' issuing notes of €193,000,000, backed by a guarantee from the Flemish Region.

In January 2005, the Belgian Ministry of Finance has started a tendering procedure to appoint a financial and legal advisor to advise on the securitisation for an estimated amount of 300,000,000 euros of a portfolio of tax claims. The Belgian government will thus be duplicating the innovative securitisation structure which had already been implemented successfully in Italy and Portugal in the past. The availability and the quality of the data relating to the historical recovery of 'tax claims' and the collection procedures which are in place to recover the claims, will determine the level of success of such a transaction.

In addition to these disclosed transactions, various Belgian banks have structured undisclosed trade and other receivables securitisations through their conduits for corporate clients, having established this as a financing technique for more sophisticated companies as a replacement for, or in addition to, more traditional means of financing.

What often frustrates participants in this type of transaction in Belgium is the poor quality of the available data with respect to the asset portfolio. Often there is no reliable information about historical performances of the assigned receivables. Originators apply their own internal rules for the origination and collection of receivables and do not have standard credit and collection policies.

The existence of so-called Belgian 'coordination centres', ie companies who are subject to the beneficial fiscal status of a 'coordination centre', is often the rationale behind this kind of structure as such a coordination center can operate as a factoring company for other operational group companies buying intra group all or some trade receivables which can then be sold onwards to a securitisation conduit of the bank on the basis of which the latter can issue debt instruments. The Belgian government is currently adapting new legislation to try to put in place an attractive alternative to the coordination centres whose tax-exempt status is fading out following a decision by the EU Commission.

### Belgian legal framework

As we elaborated on in more detail in our contribution last year, Belgium has a robust legal framework making it possible to implement both basic and more complex securitisation structures. The regulatory framework has also been tested before the courts (Europe Loan Finance case).

The first Belgian legislative initiative in the field of securitisation was the Act of 5 August 1992 (hereinafter the Act), modifying the Act of 4 December 1990 on financial transactions and financial markets, creating a general framework for securitisation transactions under Belgian law. This Act was completed by a Royal Decree of 29 November 1993 on all necessary aspects of securitisation, which was subsequently modified several times, notably in 1996 (hereinafter the Decree).

This has resulted in the possibility of creating a 'receivables investment organisation' (hereinafter the RIO). The RIO has as exclusive corporate purpose: the investment in receivables that are assigned to it by a third party. The assets of a RIO are usually constituted by a portfolio of assigned receivables. Therefore, each securitisation operation covering a set of receivables will in principle entail the creation of a specific bankruptcy remote RIO (or the set up of a compartment thereof), ie both in legal and accounting terms distinct from the originator of the securitisation.

The RIO is of a closed-end type; the shares in the RIO cannot be repurchased by means of its assets upon the request of the bearers, even if the possibility of an early reimbursement or transfer of the receivables held by the RIO is provided for under the applicable regulation. The rationale for this is that normally the receivables are not liquid enough to accommodate early requests for reimbursement by the bearers. For the purpose of financing, the RIO may issue different categories of securities (ie shares or debt instruments) based on the characteristics of the receivables, forming part of the securitised portfolio, on the basis of allocation rules to be provided for under its articles of association.

The RIO can itself be of two categories: a contractual type or a corporate one (then also referred to as a Receivables Investment Company (hereinafter the RIC)), both of which have to be managed, from an administrative and accounting point of view, by a management company in the exclusive interests of the participants. Such a management company needs to obtain a license from the CBFA. Typical requirements to obtain such a licence are fit and proper management, minimum capital requirement, infrastructure and systems, bona fide shareholders, etc.

In the case of an RIC, the capital ties with the originator need to be very limited. An equity link between the assignor and the securitisation vehicle is contrary to the requirement that the transfer must be complete and definitive.

An equity link can only be qualified as securities when sufficient separation exists between the assignor and the vehicle. Sufficient separation is deemed to exist according to the CBFA, and the equity link will therefore be qualified as securities, when the vehicle is of a public character, when the capital link is lower than 20 per cent (the remaining portion being held by one or more effective third parties) and when the assignor is only represented by one person on the board of directors.

The management company may contractually entrust the assignor of the receivables (or another third party) with the task of recovering them, the so-called servicing of the receivables. This has two important advantages: (i) the assignor is very familiar with the receivables, which has its effect on the efficiency and on the operational cost and (ii) this working method allows the RIO not to have to notify the debtors in relation to the assignment of the receivables so that they can continue to deal with the assignor. It is crucial however for the assignee to always ring fence the cash flow and separate it sufficiently from that of the assignor.

In this respect it is useful to stress the importance of the legislative modification in 1994, whereby the Belgian legislator decided to modify, notably with the aim of facilitating securitisation operations, the legal rules surrounding the transfer of receivables, as these rules were set forth in Article 1690 of the Belgian Civil Code. Pursuant to this modified provision, the assignment of a receivable is effective between the assignor and the assignee upon the mere reaching of an agreement between them, and this will then also be effective vis-à-vis third parties, with the exception of the debtor.

A specific protection is put in place for the debtor, as the assignment is only effective towards him if he has been notified of the assignment or if he has acknowledged it. In practice, this has given the securitisation market in Belgium a tremendous boost.

Belgian securitisation legislation was further adapted in 1996, to organize a specific legal regime for RIO's, that do not receive their financial means from the general public (ie private receivables investment companies and private receivable investment funds). The private RIO's are not subject to the control of the CBFA but must be registered with the Ministry of Finance.

Another innovation, introduced in 1996, has been to create legal status for the representatives of the holders of the debt instruments issued by the RIO, whether it is public or private. These representatives must be approved by the CBFA (or resort under other permitted categories, already operating in the regulatory scope, such as the assignor or the management company) and may be dismissed at any time by a general meeting of the holders of the debt instruments. Their powers are determined either in the issuing conditions of the (asset backed) securities or by the general meeting of the holders thereof. These representatives should exercise their powers in the exclusive interest of the holders of the securities.

Furthermore, a public RIO must appoint a rating agency, which is responsible for the delivery of an extended report relating to each securitisation transaction. The report must cover topics such as the sustainability of the underlying receivables, the quality of the financial plan, the fit and proper character of the legal structure, the administrative organisation and the value of the guarantees given to the investors.

Finally, the CBFA is the regulatory authority competent for all securitisation transactions initiated through a RIO in Belgium. In addition thereto, the CBFA is also competent in respect of transactions of Belgian credit

institutions effected through a foreign special purpose vehicle, further to their general supervisory authority over Belgian credit institutions.

#### **New law on collective investment schemes**

On 20 July 2004, the House of Representatives in Belgium, further to the implementation of European Directives numbers 2001/107/EG and 2001/108/EG on collective investment schemes, adopted a new law 'on certain forms of collective management of investment schemes' (hereinafter the Law on Management of Collective Investment Schemes or the Law). This Law was completed by the Royal Decree of 4 March 2005 relating to certain public entities of collective investment. The Law will be implemented in different stages (until 14 February 2007), gradually replacing the old framework.

According to the explanatory memorandum of the House of Representatives, besides the (urgent) need for implementation of the two European directives (which should have been done before 13 February 2004), this proposal is also adapted in order to attempt to modernise the legislative framework with respect to collective investment schemes in Belgium and to maintain the competitiveness of the Belgian market in Europe.

The Law on Management of Collective Investment Schemes is divided into two main parts: (i) the status and the regulatory supervision on collective investment schemes and (ii) the status and the regulatory supervision on the management companies of collective investment schemes.

With respect to the first part on the collective investments schemes themselves, the bits of regulation with respect to the RIO's do not substantially modify previous legislation but rather put all pieces together into the broader picture of the legislation on collective investment schemes.

A modification worth mentioning is the explicit application of the dissolution, liquidation, restructuring and insolvency provisions of Belgian Companies Law on the different individual compartments of a RIO. Each compartment of a RIO will be liquidated or filed in bankruptcy separately, without the liquidation or bankruptcy of one compartment influencing or triggering the liquidation of the other compartments of the RIO. The intention of the legislator is to segregate the different compartments in case one of them is discontinued.

The Law also stresses that an originator can still be appointed as servicer of the transaction, collecting all the receivables on behalf of the RIO. If the originator appoints

in its turn a specialised third party to perform the collection efforts on his behalf, this third party should be subject to regulatory supervision.

The second part on the management companies of collective investment schemes also sums up all existing provisions with respect to their status and supervision.

The main difference in practice will be that all management companies will need to comply with a lot more detailed requirements before they will be able to obtain a licence from the CBFA.

Even though the new requirements to obtain a licence as a management company of a collective investment scheme are substantially along the lines of the existing requirements of the Decree, such as, corporate form, minimum capital requirements, fit and proper management, etc, the new Law on Management of Collective Investment Schemes is much more detailed, provides an update on other recent important legislative initiatives (reference is being made to relatively recent laws such as the Law of 2 August 2002 on the supervision on the financial sector and financial services) and focuses more on current issues such as risk management, analysis systems and valuation methods for, amongst others, (OTC) derivative products.

Also the supervision of these management companies by the CBFA is organised more thoroughly. RIO's now need to provide the CBFA with periodic information, the exact contents of which will need to be further specified by the CBFA. The CBFA also has more investigating powers in order to enforce compliance with these new provisions and to preclude any abuses.

### Conflicts of Law Code

Another legal initiative which will have an important effect on cross border securitisations is the enactment of a New Belgian Conflicts of Law Code (entered into force as of 1 October 2004).

A new Article 87, §3 states that the consequences of a transfer of a receivable or the granting of rights in rem (ie a pledge) conferred upon such receivables are, from a Belgian conflicts of law point of view, governed by the law of the state of the habitual residence of the granting/transferring party (ie for corporations their main establishment) at the moment of the grant/transfer.

This raises the issue that in a cross-border transfer of receivables, a choice of law provision in the contract will not obviate the need. In order to realise a fully effective transfer one will also need to comply with the law of the main establishments of the transferor (in addition to having to comply with the law governing the transfer agreement).

### The EU's consumer credit directive

Recently, a minor amendment of Article 17 of the EU consumer credit directive (COM(2004) 747) endorsed by the European Commission in October 2004, caused a stir amongst securitisation lawyers over Europe. This new Article 17 states that "the consumer must be informed that the contract has been assigned to a third party".

This small sentence has important consequences for consumer finance securitisation in Europe because this could force consumer finance companies to write letters to each obligor when they wish to securitise consumer finance assets (except for residential mortgages, which are specially excluded from the scope of the Directive). So the cost of a mail shot could be very high for a large securitisation. Moreover, the mailing could anger or confuse borrowers not familiar with securitisation, increasing the costs even further.

The European Commission and the European Securitisation Forum are working to modify this article so that it does not apply to a mass assignment or to delete the paragraph altogether. However, a solution is not expected before the end of the year.

At first sight, this also contradicts with the silent assignment of receivables introduced in Belgian law in 1994 (*supra*) in order to facilitate securitisations. However, further to the Belgian consumer (credit) protection laws (Article 26 of the Law of 12 June 1991 on consumer credit as amended from time to time), the assignment of consumer credit contracts will only be effective in principle *vis-à-vis* the relevant consumers in case the consumer is notified of the transfer by registered mail, except in case the assignment itself and the identity of the assignee were already explicitly mentioned in the initial credit documentation. Therefore, in 1994, the Belgian legislator provided for an exemption to facilitate mass assignments of consumer credit agreements towards a (regulated) RIO. Hopefully, the European legislator will not turn back the clock.

## **Stibbe**

**Rue Henri Wafelaertsstraat 47-51  
1060 Brussels, Belgium**

**Tel** +32 2 533 52 11 **Fax** +32 2 533 52 12

**Web** [www.stibbe.com](http://www.stibbe.com)

**Other offices** Amsterdam, London, New York

### **Jan Peeters**

Partner

**Email** [jan.peeters@stibbe.com](mailto:jan.peeters@stibbe.com)

Jan Peeters concentrates on capital market operations (initial public offering, public takeover bids, public to private transactions and privatisations); corporate finance; venture capital; mergers & acquisitions and financial services regulations. In addition, he is active in the regulation of activities of Belgian and foreign credit institutions and investment firms in Belgium. He is the author of various publications in the areas of corporate

law and financial services regulations. Jan Peeters graduated from the University of Antwerp in 1986 and obtained a LLM from the School of Law Boalt Hall, University of California at Berkeley in 1987. He was admitted to the Brussels Bar in 1987 and became a partner at Stibbe in 1996.

### **Wouter Ghijsels**

Associate

**Email** [wouter.ghijsels@stibbe.com](mailto:wouter.ghijsels@stibbe.com)

Wouter Ghijsels is a junior associate specialising in corporate finance and mergers & acquisitions. He is a member of the Brussels Bar and received his law degree from the University of Antwerp in 2001. He obtained a LLM in International Business Law in 2002 from King's College London. He did postgraduate studies in corporate taxation at the Fiscale Hogeschool (Brussels) in 2003.

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**[www.stibbe.com](http://www.stibbe.com)**

**Rue Henri Wafelaertsstraat 47-51, 1060 Brussels, Belgium**

**Tel +32 2 533 52 11 Fax +32 2 533 52 12**