non performing loans

2nd edition

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non performing loans

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foreword

Throughout the CEE/SEE region, the percentage of non-performing loans (NPLs) to total loan receivables has increased dramatically during the current economic cycle.

In many areas, lenders appear to have reacted to this by pursuing a strategy occasionally called "extend and pretend." But in light of European Asset Quality Review (AQR), of ever-increasing regulatory (capital) pressures concerning flawed banking assets and limited access by certain banks to equity capital, we believe that many regulated lenders may be left with little choice other than more actively managing distressed borrowers/portfolios.

On the other hand, there is increased buy-side demand for distressed credits in a variety of industries and across asset classes and jurisdictions, which in turn should allow current creditors to consider disposals of credit exposures (single names and portfolios) as part of the strategic management of distressed exposures.

We therefore take great pleasure in presenting to you our thoughts on some key legal issues that should be considered carefully by sell- and buy-side industry participants when looking into the viability of NPL transactions (single names and portfolios) in the region.

If you wish to discuss any of these issues in greater detail, please feel free to contact the authors of this guide, any of the members of Schoenherr's distressed assets team or any of your usual contacts in our firm.

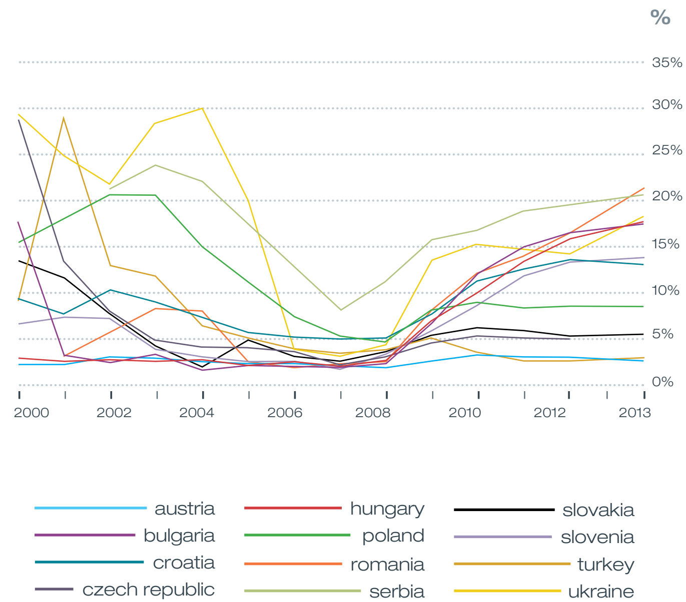
martin ebner

content

a brief look at the factors driving NPL transactions in the region

a brief look
some considerations
guide by jurisdiction
team
disclaimer

In the last decade, in particular the current economic cycle, there has been a dramatic increase of non-performing loans (NPLs) throughout the CEE/SEE region peaking to a total NPL exposure of approximately EUR 155 billion in 2012 equalling to an annual increase of 7% (CAGR) since 2010 (estimate excl. Bulgaria; Source: IMF - World Economic Outlook; PWC). Expressed as relation to total gross bank loans (in %), the region's asset quality shows an even more drastic development, especially in comparison to the euro zone average (see chart below; Source: IMF, Global Financial Stability Report).

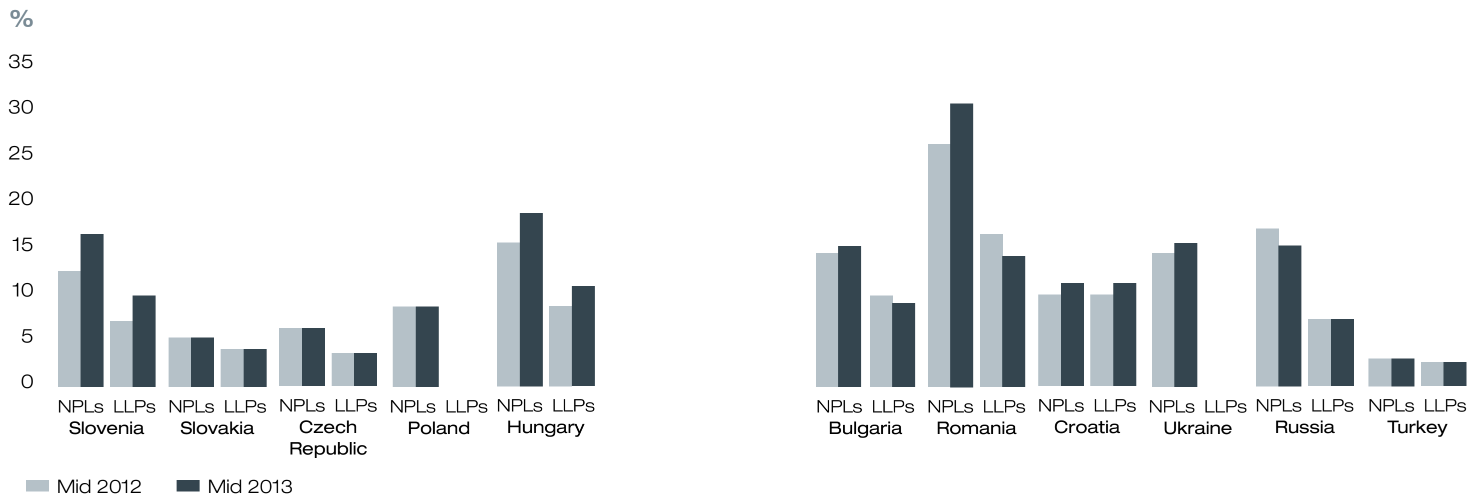


Whereas the December 2013 financial market stability report (*Finanzmarktstabilitätsbericht*) by the Austrian National Bank (*Oesterreichische Nationalbank* (OeNB)) confirms overall adequate capitalisation for the CEE/SEE banking sectors, ranging between 13.5% and 20.8% in mid - 2013, the below comparison of NPLs to loan loss provisions (LLPs) outlines a potential backlog in some of the regions books (Source: OeNB, *Finanzmarktstabilitätsbericht 26, December 2013*).

This rapid increase of NPLs combined with ever-increasing banking regulation throughout Europe and the impact of those assets on institutions' risk-weighted assets (RWAs) encourages credit institutions in the CEE/SEE region to reconsider their long-term strategies concerning non-core and distressed assets.

banking sector: credit quality

non-performing loans (NPLs) and loan loss provisions (LLPs) in % of total credit at end of period



Under the new Basel III regulations, large parts of which have been implemented in the EU on 1 January 2014 (subject to transitional provisions), credit institutions have to gradually increase their capital base and to enhance the quality of capital. In addition, as part of EU measures to restore confidence in the banking sector, certain European credit institutions were required to establish a Core Tier 1 buffer of 9% by the end of June 2012. The 9% Core Tier 1 buffer has meanwhile been transformed into a nominal floor of Core Tier 1 to be held on a continous basis in order to support the introduction of fully loaded Basel III Core Equity Tier 1 capital buffers.

Moreover, certain Austrian banking groups are required to apply certain Basel III capital standards earlier than otherwise provided (no phase in). This national sustainability package also introduced a maximum loan to deposit ratio of 110% for the CEE/SEE subsidiaries of these banks.

Also, it is often the case that state-aid decisions by the EU Commission with respect to “bailed-out” banks contain requirements for asset disposals, including specific timeframes.

Following the EU Parliament’s approval, the Single Supervisory Mechanism (SSM) will be introduced with the goal of strengthening the EU banking system. Under the proposed scheme, the European Central Bank (ECB) will regulate almost 85% of all banking assets in the euro zone. However, an Asset Quality Review (AQR) of 128 significant banks will need to be performed before the ECB assumes full regulatory responsibility in 2014 and before the stress testing of 124 banks is carried out in co-operation with the EBA.

Under the AQR, identified portfolios will be reviewed under harmonised definitions (including the definition of non-performing exposures taken from the EBA ITS on FINREP) and may lead to a re-calculation of RWAs, in particular following collateral valuation.

In this context, institutions are looking for options to reduce their balance sheets, thereby improving capital ratios, which should lead to further disposals of distressed assets.

considerations on NPL transactions

As in any other transaction, legal and regulatory issues are only some of the aspects that impact the success or failure of structuring, implementing and executing a buy- or sell-side NPL transaction. Other key driving factors include the economics of the deal, accounting, tax, reputational and general risk management considerations. But in our experience, legal considerations (including in relation to servicing and enforcement) are among the key drivers when it comes to selling or buying a portfolio of distressed credits. This is not only due to the nature of the parties involved (in particular regulated sell-side businesses), but mainly due to the nature of the assets involved in the transaction, whether a single-name loan or a portfolio of consumer credits.

Below we have set out our thoughts on how to strategically approach a sell- or buy-side NPL transaction. Whereas this guide focuses on portfolios of non-performing corporate and consumer loans, many of the issues addressed will also be relevant to single name transactions in large corporate exposures.

This guide is structured according to transaction stages, from pre-transaction decision-making, via structuring aspects and transaction execution to post-execution servicing.

Pre-transaction aspects (decision-making)

A potential sell-side credit institution has many options for managing its clients in distress, ranging from restructuring the debt (which in the region is often confined to extending tenors and granting covenant holidays) to forcing borrowers into liquidation.

When considering whether the disposal of certain assets or asset-classes may be an optimal strategy for actively managing distressed credits, the management of the potential sell-side institution will have to carefully consider whether the perceived negative effects are outweighed by the advantages.

On the down side, there may be negative effects on an institution's financials, because of losses realised on a sale of assets that are not marked-to-market in an institution's books, in combination with the threat of foregoing the up-side that may potentially come from a successful recovery or even from enforcement. In addition, many institutions may be concerned about managing reputational aspects. For example, they may fear media reports about selling claims against widows and orphans to aggressive investors.

On the other hand, the most obvious benefit of a successfully completed sale of NPLs is the effect on risk-weighted assets (RWAs) and the resultant freeing up of equity. Selling institutions have also received positive market and shareholder feedback (including rising stock prices once a transaction or series of transactions has been announced and completed) as well as positive ratings response to the improvement/enhancement of on-balance sheet assets that continue to be held by the institution and to the more focussed approach to core activities, such as originating new business while "outsourcing" certain aspects of problem loan management.

» **Challenge yourself (sell-side)**

- Do I have the organisational and managerial capacities to manage and service distressed exposures in a value-preserving manner and at least in the same quality as experienced third-party special servicers?
- What will be the likely effect on my financials of selling non-performing loans (substantially) below par?
- Will my investor relations/public relations unit be able to manage reputational aspects?
- Am I able to define a portfolio that suits expectations on credit quality, maturity and pricing?

Structuring aspects

Once an institution concludes that disposals of single names or portfolios of non-performing loans form an important pillar of its overall strategy of actively managing its problematic exposures, it is time to decide on the overall transaction structure (auction process, negotiated sales, etc.) and to start the vendor due diligence process that precedes most successful sale transactions.

Accurate, reliable and complete data about the non-performing loans are the key to maximising sales proceeds. It is often at this stage of preparing information for potential investors when institutions learn more than they ever wanted to know about their own customers/borrowers and in particular the quality and consistency of documentation and data available in relation to the distressed credits. In addition to practical aspects in relation to the completeness of documentation and data quality, one has to consider that any sell-side (credit) institution will normally be bound by data protection and banking secrecy laws that limit or even prevent the full disclosure of data to potential buy-side institutions and their advisors. However, that dilemma can usually be overcome in a manner that satisfies compliance considerations as well as investor due diligence requests. The available options range from disclosure of anonymised and aggregated data only, to full disclosure of the credit documentation to due diligence advisors formally appointed/endorsed by the selling institution, who in turn produce a report to the potential investor on an aggregated and no-names basis only (i.e., without referencing specific loans and customers).

Since a fully-fledged buy-side due diligence of each and every credit file will often not only run afoul of limitations on information disclosure and data transfer, but also will be very costly, management of the selling institution should consider what it takes for the selling institution to become comfortable that a sample of, say, 5% to 10% of all loan contracts relative to transactions included in the portfolio constitutes a representative sample of documentation used. Once this level of comfort is achieved (i.e. once the sell-side institution has established that there are no significant deviations in documentation standard), buy-side due diligence could be limited to the loan contracts included in this sample and representations to this effect in the sale/purchase documentation could be offered to investors.

During this pre-sale vendor due diligence process, any sell-side institution will also be well advised to scrutinise the credit files relating to the portfolio to be sold to determine whether they contain only the information and data required by a potential buyer for enforcement purposes (since data disclosure would often be limited to data on a strictly need-to-know basis; see below).

To achieve a bankruptcy remote transfer of the NPLs (a true sale), structuring considerations will come into play during this phase of a transaction. In addition to tax (particularly VAT and withholding tax considerations), the structure will largely be driven by the legal aspects of the transferability of loans and related security interests and the resulting structure proposal (trust, true sale, spin-off or demerger; see below) will have to be reflected in the transaction documentation proposed to potential investors by the seller.

» Challenge yourself (sell-side)

- Have I used consistent documentation when originating the loans subject to the transaction?
- Are all required customer consents to data processing and information disclosure available?

- How else can I transfer/disclose data and information during due diligence stages and afterwards?

- Am I in a position to strip-off non-core information from the credit files so that disclosure can be limited to data and information on a need-to-know basis?

- Are the loan receivables and related security interests transferable (under the terms of the contracts and governing law) or do I need to explore a corporate transaction, such as a spin-off/demerger of the portfolio?

Buy-side institutions, on the other hand, when gearing up to participate in a sales/auction process, will be keen to validate their pricing and valuation models against the local legal environment (e.g., their assumptions in terms of collection and enforcement proceedings). Moreover, they will be looking into setting up a legally compliant and tax efficient acquisition structure, where their focus will be on compliance with local banking and servicing regulation. Not least, they will be looking into how the acquisition will be financed.

» Challenge yourself (buy-side)

- Do I have the requisite local experience to adequately price the NPL portfolio or is additional due diligence on the local legal and tax regimes required?

- Will the structure I usually use be feasible in the local environment? In particular, will the acquisition vehicle or the servicing vehicle (if different) have to be licensed?

- Is professional servicing expertise available locally or do I have to build this and at what cost?

Transaction execution

Sell-side institutions will usually be looking at a two-stage sales process, which would commence by asking interested bidders for indicative bids based on a standard information package or fact book made available by the seller.

After this pre-selection process, short-listed bidders would normally be granted access to additional information so as to allow them to complete their due diligence and to submit binding bids. The contents and level of detail of the data room/data tape and relating access rights will be driven by competition considerations as well as banking secrecy and data protection laws (see above).

In a well-structured process, at this stage the proposed transfer and servicing documentation would be made available by the sell-side institution to shortlisted bidders. Documentation will largely be driven by issues relating to the transferability of loan receivables and related security, where parties aim at achieving a transfer without debtor involvement while avoiding excessive costs, such as the costs of security re-registrations. Transferability aspects, for example, will be decisive in establishing whether a true sale of the assets can be implemented or whether the portfolio will have to be hived-off from the selling institution's balance sheet into an SPV by means of a corporate transaction with a subsequent sale of that SPV's shares to the investor.

Irrespective of whether the parties pursue an asset or share deal transaction, any buyer will be well advised to not only focus on the desired receivables and security interests transfer, but to also verify whether the structure chosen may have undesirable effects in terms of liability and/or employee transfers (such as being treated under local laws as a transfer of a business unit) and, if so, how these risks can best be mitigated.

In addition to the receivables transfer documentation, agreements governing the servicing and enforcement of the receivables sold and purchased will normally have to be put in place. Whether the servicing will be performed by third-party servicers or by the selling institution on behalf and for the account of the purchaser will, in addition to banking secrecy and data protection considerations, be determined on the one hand by the servicing capabilities of local special servicers and the selling institution, and on the other hand by reputational considerations of the selling institution in relation to servicing on behalf of, and at the instruction of, the investor.

Other ancillary documents may include a data trust agreement if the involvement of a data trustee is required from a banking secrecy and data protection perspective, also in regards to non-performing loans, and financing documentation at the buyer's end.

» Challenge yourself (buy-side)

- Does the transfer documentation result in a bankruptcy remote transfer of the loan receivables, related security and other ancillary rights to the purchaser?
- Will the proposed transfer mechanism require the involvement of debtors or trigger costly and/or cumbersome notifications or re-registrations?
- Is there a risk that the transfer will also trigger the assumption of liabilities and/or employees attached to the loan portfolio by the buyer? How can this be avoided/mitigated?
- Does local law allow a timely transfer of sufficient data to the servicer to allow a seamless continuance of servicing/enforcement?

Post-execution servicing

Once the data needed by the servicer to perform its duties are available to it, the transaction will enter into the key-value driving stage. The buyer's return will depend primarily on the results yielded by the servicer when servicing the portfolio and when enforcing the loan receivables and related security as well as on the time needed to recover the non-performing loan receivables.

At this stage debtors will attempt to raise various types of defences, both in relation to the underlying credit and security documentation as well as in relation to the validity of the transfer to the buyer. The buyer will therefore have to concern itself to provide local law compliant evidence of transfer to local courts and enforcement authorities.

» Challenge yourself (buy-side)

- Does the servicer hold all licences required under local laws to perform its duties?
- Has the buyer (or a data trustee)/servicer obtained all documentation required to service the loan portfolio (credit files)?
- Has the buyer obtained all means of evidence required under local laws to prove the validity of the transfer of receivables, related security and other ancillary rights to local courts?

jurisdiction

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a brief look
some considerations
guide by jurisdiction
team
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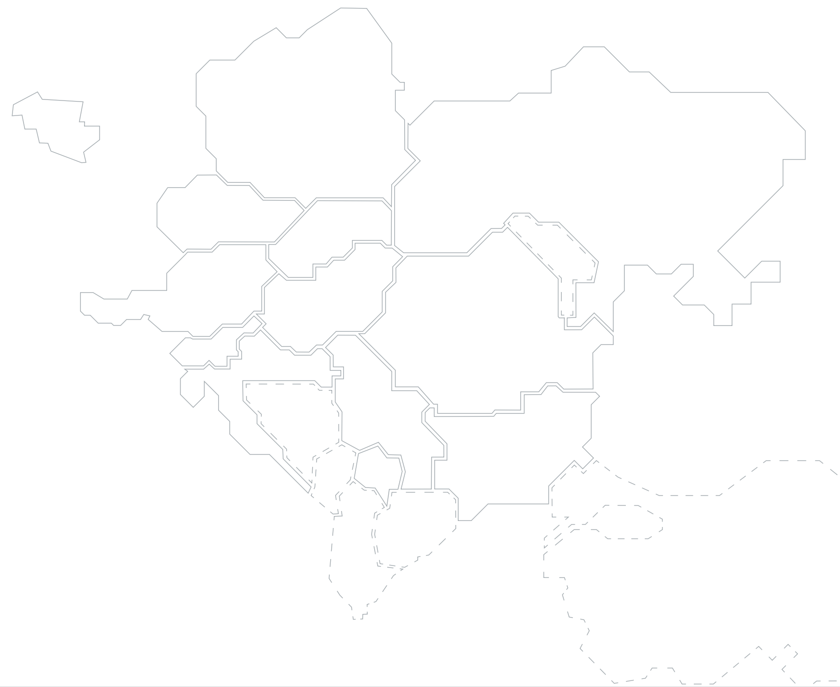
The solutions that we think may be available for some of the key structuring considerations identified in the general sections of this guide are set out below for each jurisdiction.

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austria

The limitations resulting from secrecy obligations (data protection and banking secrecy, the latter of which is enshrined in Austrian constitutional law) at due diligence stages are usually addressed by appropriate precautions to avoid customer-specific disclosure to investors.

Until late 2012 the general view, which was also confirmed by the Supreme Court with respect to a subrogation structure, was that secrecy obligations should not bar a credit institution from selling and assigning loans, since in particular in respect of non-performing loans, the interests of the bank outweigh the customers' legitimate interests to keep their data secret.

Against this background, a Supreme Court judgment of 26 November 2012 took some industry participants by surprise. In this judgment the Supreme Court held that an assignment of receivables in violation of Austrian banking secrecy is null and void. Future practice will have to look at structures where either the purchaser itself is subject to banking secrecy (as is the case for qualifying securitization SPVs) or structures based on the extension of banking secrecy.

In any event, data and information disclosure should only occur on a need-to-know basis.

Despite factoring being a regulated banking business in Austria, the purchaser's potential licensing requirements are usually overcome by structuring the transaction in a manner that the purchaser qualifies as securitisation SPV. This will also be beneficial from a banking secrecy perspective. Alternatively, the buyer could use a foreign acquisition company, thus arguing that no regulated business is performed in Austria.

The assignment of receivables and related security can normally be accomplished in a manner that qualifies as a true sale. With respect to the maximum amount mortgages frequently used by Austrian credit institutions, however, certain pre-transfer steps will have to be implemented in order to convert the mortgage and to allow for a legal assignment by way of subrogation *(Einlösung)*. Subrogation generally leads to a transfer of all rights by operation of law and may be a preferred structure with respect to many types of secured loans. If conversion and subrogation is not an option, it may be worth exploring a transfer of the portfolio to a newly set up SPV by means of a demerger *(Spaltung)*, which would require the consent of the banking regulator and bring about new regulatory challenges. For receivables where an enforceable court judgment already has been obtained, additional form requirements apply to the transfer.

Enforcement of secured claims involves Austrian courts and enforcement officers, unless the transaction relates to corporate loans, where the originating bank and the borrower often will have agreed on out-of-court enforcement. Contrary to some other jurisdictions, however, the SPV holder of the loan receivables would be treated akin to an Austrian credit institution, since banks do not enjoy special privileges on enforcement, with few exceptions if security in the form of financial collateral was granted.

When using a foreign acquisition company for non-performing loans, tax considerations will be decisive in determining the acquisition company's jurisdiction. Recently, the Austrian legislator extended the application of the Austrian withholding regime on interest income derived from Austrian sources. Therefore, the acquisition company's jurisdiction will even be more relevant in order to ensure that tax treaty relief is available for Austrian withholding tax on interest income.

austria

Finally, the assignment of receivables and other rights may be subject to Austrian Stamp Duty, if a deed is set up evidencing the transaction. However, certain transactions are exempt, including the assignment of receivables between credit institutions, assignments to securitisation SPVs, and assignments under a factoring contract. In addition, certain strategies are used in order not to trigger Austrian Stamp Duty (e.g. by avoiding an Austrian nexus).

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Under Bulgarian law assignors are under a statutory obligation to provide assignees with all documents concerning the assigned receivables. Since these might include documents containing personal data or facts and circumstances subject to banking secrecy, the interaction between this statutory disclosure requirement on the one hand and data protection and banking secrecy limitations on the other merits particular attention. As far as data protection is concerned, the originating and selling bank's legitimate interest (e.g. to achieve regulatory capital relief by assigning loan receivables) should prevail over the interests of the debtor, especially with respect to non-performing loan receivables.

However, the Bulgarian Supreme Court of Cassation recently upheld a huge administrative penalty on a bank for transferring personal data to a collection agency (only for dunning purposes), in a scenario where there was no actual assignment of the respective loan receivables. In that case the initial consent of the bank's customers for transfers of personal data was quite narrowly worded (not covering expressly transfers to collection agencies for dunning purposes) so arguably, if the consent was phrased in a broader manner, the result might have been different.

In situations involving actual assignment of receivables, the Bulgarian Personal Data Protection Commission has already held in a number of rulings that it is permissible to transfer personal data by mobile operators that had assigned claims for unpaid bills to third parties and in performance of the assignments transferred personal data about the respective debtors, holding it forms a part of the "legitimate interests" of the creditors. While not yet tested before Bulgarian courts, we believe that the "legitimate interest" exception from personal data protection rules could be applied *mutatis mutandis* to bank secrecy restrictions where a bank has assigned non-performing loans to a third party. It seems a reasonable solution with respect to non-performing loans from a banking secrecy perspective to uphold the bank's interest to assign receivables under such loans, thereby enabling it to clean its balance sheet and to generate some liquidity instead of attempting to collect its claims in lengthy and cumbersome enforcement proceedings. Bank secrecy should therefore not be an obstacle to disclose information about the debtor, but disclosure should be made only on an as needed basis.

bulgaria

From a financial services regulatory perspective, the general rule is that the acquisition of receivables arising from credit agreements may be performed locally as a "main activity" (bringing 50% or more of the net revenues or corresponding to 50% or more of the balance sheet total) only by credit institutions (local or EU/EEA under EU passporting rules) or by financial institutions registered with the Bulgarian National Bank. While this registration does not imply fully fledged supervision (compared to a credit institution), the acquirer will be able to operate under an unregulated regime only if the acquisition of receivables is performed outside Bulgaria. There is no express statutory rule or practice in Bulgaria shedding light on the issue of when a particular banking activity (including acquisition of receivables) is to be regarded as being performed in Bulgaria or outside of Bulgaria. The implementation of a transaction that avoids being caught by the local regulatory regime will therefore require careful structuring. Once regulatory constraints on the purchaser are avoided, however, the transaction may be implemented in an unregulated environment, since the activities of collection agencies are not subject to licensing/registration requirements in Bulgaria.

Loan receivables (whether performing or not) and related security interests can be transferred either by assignment or, likely, by contractual subrogation. Depending on the asset/portfolio in question, the parties may opt to implement either structure. This is because assignments need to be registered to be effective with respect to certain types of security interests (notably real estate mortgages and non-possessory pledges). Depending on the size of the portfolio, such registration may be a time-consuming and costly venture. Contractual subrogation, a structure which is not tested before Bulgarian courts, but is supported by the predominant doctrinal opinions in Bulgaria, would on the other hand achieve a transfer of the loan receivables and all ancillary rights (including related security) without any registration, thus bringing cost-effectiveness.

If none of these structures is feasible, the demerger of part of the originating bank in order to transfer the non-performing portion of the loan book might also be an option, provided that permission by the Bulgarian National Bank can be obtained.

guide by jurisdiction

croatia

Becoming a member state of the EU in July 2013, Croatia's legal system has been substantially streamlined with EU standards, while further harmonisation is an ongoing process. Already a few past hurdles have been mitigated, such as liberalisation of FX, cross-border payment and national payment systems. Also, the harmonisation of local laws with EU law now permits EU-domiciled companies, including regulated entities in the banking and non-banking financial sector, to provide services in Croatia either directly or via a branch (passporting).

The Croatian parliament is expected to pass the first Croatian law on factoring in 2014, thus affecting some of the players on the Croatian NPL market, including factoring companies. At the moment factoring is a regulated business if conducted by credit institutions (supervised by the Croatian National Bank *(Hrvatska narodna banka; HNB)* but not if conducted by other entities (while still supervised to some extent by the Croatian Financial Services Supervisor Agency *[Hrvatska agencija za nadzor fi-nancijskih usluga])*. While the final features of the future factoring act re-main to be seen, it is expected that the act will comply with the respective EU Directives allowing, inter alia, passporting of EU-domiciled financial institutions to do factoring business on the local market.

True NPL transactions (i.e. those resulting in hive-off of the loan portfolio from the banks' balance sheet) so far are mostly structured as an assignment (asset deal), while corporate NPL transactions (share deal) are still to be tested/seen (those not only requiring HNB approval but also likely to have undesirable effects in terms of liability and/or employee transfers and alike).

Making an assignment agreement may be costly due to notarial fees, stamp duties and required translation costs. But these costs may be reduced by assignment of loans in bulk. To the extent the transaction (if not a synthetic transaction) involves secured loan receivables, the transfer of related security (mortgages, pledges, fiduciary assignments, etc.) will be, in general, perfected only upon re-registration with the competent public registers. However, the necessity to re-register does not affect the priority of the security interest.

As to banking secrecy, banks are by law relieved from confidentiality to the extent necessary to conclude and perform transfers of receivables (to a regulated or non-regulated entity). The secrecy exemption does not yet apply at the due diligence stage, but that is usually overcome by performing the due diligence through disclosure of loan documents to advisors formally appointed/endorsed by the selling institution, who in turn produce a report to the potential investor on an aggregated and no-names basis only (i.e. without referencing specific loans and customers).

While the above exemption is available between banks and the transfer-ees of their receivables, it may not be available to the transferees (e.g. securitisation SPV) if will-ing to outsource debt collection to local collection agen-cies. From a deal structuring perspective, this likely means that a se-curitisation SPV must either rely on the selling bank as the future servicer of the receivables or must ser-vice the portfolio itself. Also, the selling bank will likely have to continue pending litigation for the foreclosure proceed-ings relating to the sold claims since the defendant has solid grounds un-der law to object to the securitisation SPV taking over the process.

Following an average increase of the monthly instalments on loans indexed to CHF by some 50% since the begin-ning of the financial crisis, a consumer protection asso-ciation filed an action on behalf of about 100,000 citizens against eight banks. In the first instance the verdict in favour of the claimant ordered banks to convert the re-spective loans' original principle amount indexed to CHF into Kuna (HRK) according to its exchange rate on the day of the use of the loans, with fixed interest rates (as set out in the initial loan agreements). As a final decision is still pending with the High Commercial Court following the ap-peal by the defendant banks, it remains to be seen what effects this verdict may have on the banking system.

croatia

Most loans in Croatia are now indexed to EUR while those indexed to CHF are no longer offered.

In addition, and against the recommendations of the HNB and the Croa-tian Banking Association *(Hrvatska udruga banaka),* the Croatian govern-ment has being pushing amendments to the Con-sumer Lending Act to re-strict variable interest rates on foreign-currency indexed consumer loans, in particular those linked to CHF.

The amendments (which entered into force on 1 January 2014) will impact future lending business as well as existing loans, in particular because the law sets criteria for and imposes maximum inter-est rates on consumer loans, stipulates additional information requirements on banks and author-ises the Ministry of Finance to determine the fees charged by banks in connection with consumer loans.


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czech republic

NPL transactions in the Czech Republic date back to the late 1990s. At that time, *Česka konsolidační agentura* purchased NPLs from state-owned banks so that they could be privatised. Czech banks have since adopted a more conservative approach to lending. Accordingly, and thanks to the stability of the Czech economy, the volume of NPLs in the Czech Republic is currently lower than in most CEE jurisdictions.

NPL transactions usually take the form of an assignment of receivables (an asset deal). Such assignment agreement needs to identify the transferred receivables in a sufficiently specific manner. The New Czech Civil Code, effective as of 1 January 2014, introduces a concept of a global assignment by which "all" receivables, whether present or future, may be transferred if such group of receivables is sufficiently specified, that is, if the receivables are of a certain type, arising in a specific period of time, under the same legal title or another sufficient specification of the receivables.

According to the recent practice of the Czech Supreme Court, requirements for specification tend to become less formal.

The assignment of receivables must be notified to the debtor by the assignor; the assignee is also entitled to prove the assignment to the debtor. The notification is not a requirement for the validity of the assignment, however, until the debtor is notified, it may successfully discharge the assigned receivables to the assignor. Moreover, in case of multiple assignments, the assignment of which the debtor obtains knowledge first shall be effective. This may have practical consequences for silent assignments. The change of creditor must be notified also to the parties granting the security (until notified, no effects of the assignment towards them arise) and if the security is registered in the public registers, also to the respective registry. Such notification however does not constitute a re-registration.

In addition to the relaxed regulatory regime, NPL transactions in the Czech Republic offer a facilitated transfer process for all security interests, including mortgages, pledges and other accessory rights such as default and contractual interests, transfer automatically by operation of law. Security interests can therefore be enforced by the assignee based on an assignment agreement governed by foreign law that needs to be translated into Czech when seeking enforcement before Czech courts. Re-registration of security interests in the purchaser's name is not required, which saves not only time, but also notarisation and translation costs.

On the other hand, parties need to specifically agree for contractual penalties or damage claims to transfer, as they are most likely not deemed accessory rights.

Another clear advantage is that the acquisition of NPL portfolios is not regarded as a banking activity. A purchaser of an NPL portfolio does not therefore require a banking licence. If a Czech subsidiary or a Czech branch of the purchaser acquires the portfolio, it will need a local trade licence to administer and collect receivables, including factoring, which is relatively easy to obtain. No trade licence is needed if a foreign investor makes a cross-border purchase of the NPL portfolio and then services it via a local collection agency.

Before 2000, bank secrecy was not an issue, as full documentation was disclosed during due diligence in the sale process to *Česka konsolidační agentura*. While this approach has since changed, recent Supreme Court decisions support the view that bank secrecy obligations do not prevent a credit institution from assigning its receivables. Similarly, data protection legislation limiting disclosure of data has to be considered, in particular if consumer credit portfolios are concerned. As the Czech Data Protection Office is known for its strict enforcement practice, anonymising customer information for any due diligence purposes is highly recommended.

Unlike in other jurisdictions, regulated entities do not enjoy special enforcement privileges. If the assignee wants to collect receivables in relation to which insolvency or enforcement proceedings are pending, a certified translation of the assignment agreement with notarised and, if applicable, apostilled or superlegalised signatures must be in most cases presented to the court.


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hungary

The most important market players in the Hungarian NPL market are factoring companies closely connected to banking groups and principally charged with deleveraging banks' balance sheets to comply with increasingly stringent capital adequacy rules. Thanks to relatively easy transaction execution, unsecured consumer loans are the most commonly sold loans, generally at huge discounts.

According to our information, international NPL investors are only slowly getting on the Hungarian market. This may be attributed in part to local licensing as well as banking secrecy and data protection rules, which are the major hurdles to be overcome in transaction structuring. With factoring being a regulated banking business, arguments that a foreign SPV would not be performing licensed activities in Hungary will likely not be accepted by Hungarian authorities, because the receivables purchased relate to loans of Hungarian borrowers. The most practical way of structuring a transaction would therefore be a scenario in which the purchaser qualifies as a securitisation SPV. In that case an exemption from licensing requirements may be available, although regulation appears somewhat ambiguous.

While the exemption has not yet been tested and there is no solid market practice on securitisations generally, we believe that the law may be construed in a way to support the securitisation SPV exemption. Nevertheless, preliminary discussions with the Hungarian regulator prior to implementing securitisation SPV structures should be considered.

Aside from licensing and regulation, banking secrecy and data protection rules are a further challenge for NPL transactions. As a principle, banking secrecy and data protection rules should not prevent a credit institution from selling or enforcing its loans if this is in the best interest of the credit institution. Although this can certainly be argued in an NPL context, the "overriding interest" argument is only available to credit institutions, but not to securitisation SPVs. This creates a significant burden, as the securitisation SPV could be prevented from outsourcing debt collection to a local collection agency, because transferring data to, and processing data by, such a collection agency would be critical from a banking secrecy and data protection perspective. From a deal structuring perspective, this likely means that a securitisation SPV must either rely on the selling bank as the future servicer of the receivables or must service the portfolio itself (unless the collection agency was still appointed by the selling credit institution). Also, the "overriding interest" qualification arguably limits data and information disclosures in the course of NPL transactions (including during due diligence) to strict "need-to-know" disclosures.

Assignments of receivables and related security can usually be accomplished in a manner that qualifies as a true sale without having to undergo cumbersome and/or costly security re-registrations. With the exception of maximum amount mortgages created before 15 March 2014, collateral, as a rule, transfers together with the assigned receivable. Re-registration of security interests in the purchaser's name is therefore not required to validly transfer the security interest to the purchaser. This is different with maximum amount mortgages, which were frequently used so far by Hungarian credit institutions to secure revolving facilities, for example. Here, transfer of the maximum amount mortgage with the underlying (secured) obligation (the NPL) is far from straightforward. Long-standing Hungarian court practice is of the firm view that a maximum amount mortgage secures, and is therefore connected to, the entire legal relationship (the entire banking relationship), but not to individual claims (the NPL).

Since maximum amount mortgages can only transfer with the entire legal relationship secured by the mortgage, but not with an individual claim, one precedent concluded that upon termination of the entire relationship and acceleration of the loan, the maximum amount mortgage is converted into a fixed amount mortgage and automatically transfers as an accessory right to

hungary

the loan receivables to the purchaser. But this practice is not universally accepted and there are also contradictory rulings. This hurdle is defeated by the new Hungarian Civil Code that entered into force on 15 March 2014. The New Civil Code foresees that secured claims may not become unsecured following such transfer, thus mandating the transfer of the mortgage.

Enforcement of secured claims involves Hungarian courts and enforcement officers, unless the parties have agreed on out-of-court enforcement. However, only credit institutions are entitled to certain out-of-court sales privileges if contractually agreed with the debtor. These privileges would not pass to an unregulated purchaser.


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poland

NPL transactions are facilitated in Poland by enabling banks to freely trade in distressed receivables without the debtor's consent and relieving them from banking secrecy obligations, along with a favourable regulatory regime that does not subject purchasers to financial services licence requirements.

In terms of structuring, sales to a special type of closed end investment funds called "securitisation funds" are the most popular and advantageous structure for NPL portfolio transactions on the Polish market. Fund managers usually entrust servicing of receivables purchased, including debt collection, to special servicing companies, which require a local authorisation of the Polish Financial Supervision Authority.

Polish law further allows trades in receivables without the debtor's consent in case of so called "lost receivables" (i.e. mainly receivables overdue for more than 12 months or receivables where the bank has initiated enforcement proceedings) as well as in a procedure referred to as "public sale of bank receivables". These two possibilities may have less practical significance, though, because of the tax benefits available to banks when selling portfolios to securitisation funds.

Banking secrecy regulations follow the above transaction mechanisms. Banks are relieved from confidentiality to the extent necessary for concluding and performing transfers of receivables to a securitisation fund. Similar exemptions are available for the other two alternatives referred to above (i.e. sale of "lost" receivables and public sale of bank receivables). The exemption also extends to servicing of receivables by a special servicing company. While the secrecy exemption does not yet apply at the due diligence stage, this could be structured in a way that the bank mandates/endorses advisors who would then themselves be bound by banking secrecy and would produce due diligence reports containing aggregated and thus not sensitive information only.

Transfer of receivables secured by a mortgage results in a transfer of the mortgage; however, the transfer of such receivables requires registration of the purchaser in the respective land and mortgage register. The necessity to register the change does not affect priority of the security interest though. The transfer of a registered pledge takes effect upon entry of the purchaser poland

in the register of pledges only. Rights under sureties are generally considered accessory and will thus transfer by operation of law together with the receivable.

The time-consuming and costly transfer of receivables secured by mortgages or registered pledges is clearly the main difficulty for true sale transactions in secured NPLs. As an alternative, banks may enter into sub-participation agreements with securitisation funds. Under such sub-participation agreement a bank undertakes to transfer all proceeds realised from its receivables to the securitisation fund. Sub-participation does therefore not involve a transfer of receivables as such but a transfer of proceeds only and would accordingly not require re-registration of security interests. More importantly, claims against the bank under a sub-participation are bankruptcy remote, meaning that the receiver will continue paying out proceeds to the fund. In practice, the lack of detailed rules for such payments may cause some concerns when structuring transactions.

Secured claims are usually enforced in court unless the loan is secured collateral that may be enforced out of court, for example, by taking ownership, private sale, etc. Polish banks enjoy special enforcement privileges which do not pass to the SPV or fund purchasing such receivables. Purchasers of receivables would therefore need to resort to rather time consuming regular court enforcement procedures, a further reason for considering a sub-participation rather than a true sale deal structure.

guide by jurisdiction

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romania

NPL transactions show a strong increasing trend in the Romanian market. With the exception of a few attempted transactions concerning larger portfolios of secured NPLs, in 2010 – 2012 the Romanian market seemed limited to smaller deals concerning unsecured retail loans. Starting mid-year 2013, boosted also by a more general consolidation trend in the Romanian market, we have witnessed one large NPL sale successfully closed, and several even larger sale processes are currently ongoing. We believe this is a reflection of both the increasing ratio of NPLs in the Romanian market and the increasing interest recently shown by international investors for Romanian NPLs. While the legislator has facilitated the regulatory regime concerning certain categories of NPLs, other aspects, in particular concerning regulatory, disclosure and true sale considerations, still warrant particular attention.

From a regulatory perspective, the acquisition of loan receivables is viewed as a form of crediting activity, as is factoring, and therefore in principle is reserved to regulated entities, either licensed locally or passported. Licensing requirements are more relaxed, however, with respect to loans that qualify as "loss" and related receivables, which may be assigned to unregulated entities, and assignments to securitisation vehicles, which are only subject to limited supervision by the Romanian Financial Supervisory Authority. Loans qualify as a "loss" if the borrower has outstanding payments overdue for more than 91 days and/or if the borrower undergoes bankruptcy and/or if enforcement has commenced against the borrower. However, certain mortgage loans, even if they qualify as "loss", may only be acquired by licensed credit institutions. Practice has also shown that loans that qualified as "loss" at signing of the transaction may be re-qualified as performing loans in the run-up to closing the respective transaction; this is a moving target and should be factored accordingly into the transaction structuring. Another aspect to consider is that in several instances the portfolios offered in the market bundled together both NPLs and sub-performing or even performing (non-core) assets.

In any event, an acquirer of loan receivables may service and collect the acquired receivables itself or via an appointed agent, as servicing and collection do not carry licensing requirements in Romania.

romania

Although assignments to non-regulated entities are permissible in certain circumstances, Romanian law does not contain an express exemption from banking secrecy and data protection in relation to assignments to such entities. In respect of professional (banking) secrecy limitations incumbent on credit institutions and financial institutions, specific information in relation to loan receivables and debtors may be disclosed in certain limited scenarios only, including for "legitimate interest" of the disclosing party. In the absence of any specific guidance or interpretation by Romanian authorities on what constitutes a "legitimate interest", we take the view that disclosure of specific information subject to secrecy rules should be avoided during due diligence stages. Furthermore, such disclosure should be made to an assignee/transferee under NPLs only after putting in place appropriate confidentiality undertakings. Notification or even approval requirements may apply to the processing of personal data, depending on the data concerned and the domicile of the data recipient.

For true sale, the acquisition of non-performing loan portfolios is traditionally structured as an assignment of receivables. This results in an automatic transfer from the assignor to the assignee of all the assignor's rights concerning the assigned receivables together with all the related securities and ancillary rights. In practice sellers have limited their representations to the receivables and the material guarantees and/or security documents expressly identified by the transaction documents, while in relation to secondary collateral, insurances and other elements of the underlying loan file, sellers have significantly limited their liability.

There are no available court decisions confirming that given features of the assigned receivables (e.g. enforcement privileges of credit institutions and financial institutions) or the right to accelerate repayment constitute ancillary rights subject to automatic transfer. It can be argued that this uncertainty may be clarified in part by an express provision in the assignment documentation, specifying that ancillary rights, including the right to accelerate payments, are transferred to the assignee of the non-performing receivables.

Whereas the new Civil Code which entered into force on 1 October 2011 clarifies and simplifies the rules applicable to assignments of receivables, including the rules concerning the effectiveness of assignments towards the assigned debtors, for opposability purposes towards other third parties, the assignment of a portfolio of receivables must still be registered in the Electronic Archive for Movable Securities. Furthermore, to the extent that the assigned receivables are secured and the security over moveable assets has been properly entered into the Electronic Archive for Movables Securities or, in case of receivables backed by security over immovable assets, in the Land Book, respective entries should be amended to reflect the assignment.

While amendments in the Electronic Archive for Movable Securities are not very costly and in general should not represent a hurdle for the acquirers of receivables, amendments in the Land Book registrations require that the assignment agreement concerning the underlying receivables be concluded in the form of an authentic deed in front of a Romanian public notary, subject to payment of certain *ad valorem* fees. Signing such an authentic deed will also require that land book excerpts for each of the mortgaged real properties be obtained, which is also a logistics and cost burden.


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serbia

While the increasing percentage of non-performing loans to total gross bank loans (mainly due to the slow recovery from the 2008 crisis and RSD depreciation, which contributed to overleveraged corporate balance sheets) and the high equity requirements (Core Tier 1 ratio of 12%) imposed on local banks by the National Bank of Serbia (NBS) are expected to drive the Serbian NPL market, a few hurdles need to be overcome for such transactions to materialise.

Potential obstacles that need to be carefully addressed in deal structuring relate mainly to the stringent and inflexible foreign exchange regulations that prohibit a cross-border sale and assignment of loan receivables. This means that a foreign purchaser can acquire receivables deriving from foreign credit transactions with local borrowers only from a non-resident seller, a scenario that would seem to be relevant for single name (corporate) loans only. On the other hand, only a resident purchaser may acquire local receivables and receivables from a resident lender that are deriving from foreign credit transactions. Accordingly, a local acquisition company needs to be set up in order to acquire local customer receivables.

While FX regulations would seem at first sight to be cumbersome, what is certainly beneficial is the absence of supervision/regulation for Serbian NPL acquisition vehicles, because under Serbian law, neither the purchase nor the servicing and collection of loan receivables is subject to bank licensing requirements.

For true sale, receivables and ancillary rights are usually transferred by assignment. Under the general provisions, the seller (originator) can assign its receivables by means of an agreement with a third party (e.g. SPV purchaser) and the assigned receivables become the property of the purchaser on execution of the assignment agreement. To the extent that the transaction involves secured loan receivables, however, the transfer of related security (mortgages, pledges, etc) will be perfected only upon re-registration with the competent registers. In practice this can result in a cumbersome and time-consuming process. In addition, to the extent that the transaction relates to receivables deriving from foreign (cross-border) credit transactions, Serbian FX rules set out that the respective assignment agreement has to be concluded either as a tri-partite agreement involving not only the originating lender and purchaser but also the debtor of the underlying receivable, or to obtain a specific debtor's consent to the assignment, who in practice will have little to no incentive to become a party to such a transaction or to provide its consent.

Finally, in transaction structuring, the parties will have to consider limitations in relation to banking secrecy and data protection, which are either novel or not tested before the Serbian courts and which, if not addressed adequately during structuring stages, could result in a true impediment to the effective transfer and assignment of receivables, ancillary rights and related security. With respect to defaulting receivables, the NBS' Decision on Risk Management by Banks, which sets out the transfer (along with the appropriate *ex-ante* notification of the NBS) of defaulted receivables to a local entity as a means of credit risk mitigation, could in our view be used as a supporting argument to permit a transfer (banking secrecy rules notwithstanding).

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slovakia

A need for restructuring of state-controlled banks and their preparation for upcoming privatisation at the end of the 1990s triggered the first extensive NPL transactions in Slovakia. A company, Slovenská konsolidačná, a.s., had been established by the state in order to take over classified (NPL) portfolios from such banks. The process had been quite successful and subsequent legislative changes and adoption of a rather conservative approach to lending by the banks caused a decrease of the NPL ratio in Slovakia (at about 5% in December 2013 pursuant to a statistics of the National Bank of Slovakia).

The most important market players in Slovakia are, besides factoring and forfeiting subsidiaries of local banks, the debt collection companies that are members of worldwide groups.

In general, NPL transactions take the form of an assignment of receivables. Consent of the debtor with the assignment is not required, unless it was explicitly agreed otherwise between the originator and the debtor. When assigning the receivables, accessory rights (such as interest or default interest) as well as security instruments (such as pledge or a guarantee) are automatically transferred by operation of law. Transfer of other related rights, if any, must be explicitly agreed.

Notification of the debtor is only a formal requirement not influencing the validity of the assignment. This fact is also supported by a court ruling which states that an assignment does not have to be necessarily notified to the debtor and therefore the assignment as such may be kept confidential between the parties to the assignment agreement. However, until the debtor is notified of the assignment, he may discharge the assigned receivable to the assignor as its (former) creditor. The change of the creditor should be notified also to the parties granting security and if the receivable is secured by a pledge, also to the respective registry.

Global assignments - that is, transferring "all" receivables of the originator of a certain kind or against a specific debtor - are possible, although this might cause practical difficulties (e.g. how to determine what was actually assigned). All documents concerning assigned receivables must be provided to the assignee in order to allow him enforcement.

From a regulatory perspective NPL transactions are not considered a banking activity. If a purchase of NPLs is carried out on a regular basis as an entrepreneurial activity, only a free trade licence is required.

Corporate-law-type transactions (demergers) are also possible, but given the relaxed regulatory regime for assignments (asset deals), such transfer would usually be too cumbersome.

Pursuant to the Slovak Act on Banks a bank may assign its receivable against and provide the assignee with the necessary documentation without the client's consent (bank secrecy exemption), but only if the debtor is, despite a written warning, in default for more than 90 calendar days. However, the law does not provide any exemption with respect to a potential due diligence by the buyer before the actual purchase, which therefore requires careful structuring. Due to similar concerns, data protection laws must be considered.

Enforcement of claims involves Slovak courts and enforcement officers, except for a specific case like enforcement of pledges, where also a direct out-of-court sale or auction is possible. Banks do not enjoy any enforcement privileges compared to other non-regulated private entities.

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slovenia

Slovenian law offers banks a variety of alternatives when managing non-performing loans. Depending on the debtor's financial condition, these range from usual debt restructuring tools, such as enforcement holidays, to forcing borrowers into liquidation. Recently there is also a tendency to stimulate assignments or subrogation of non-performing loans receivables, for example, to the Bank Asset Management Company DUTB (the "bad bank") that became operative in Q4/2013 and is in charge of working out/selling off acquired bank loans until 2017.

Unlike other jurisdictions, prospective purchasers (other than Slovenian banks) do not need to be concerned about financial services licensing requirements, as factoring is not a licensed activity in Slovenia.

If receivables are assigned, in principle accessory rights such as security interests (mortgages, pledges or sureties) or the right to preferential satisfaction transfer to the recipient together with the secured claim by operation of law. Registered security rights such as mortgages and pledges over certain movables, however, will need to be re-registered in the name of the purchaser for the transfer to become legally effective. The necessity to register the change does not affect the priority of the security interest. Further, certain types of security such as, promissory notes, require additional legal acts for a transfer to be legally effective. Depending on the portfolio's size, this time-consuming and costly venture is clearly one of the challenges for NPL transactions in Slovenia, as documents will need to be translated, notarised and appostilled, and court and notary fees will be charged.

In Slovenia, as in many other jurisdictions, an assignment of receivables does not require the debtor's consent. If the assignment of claims is prohibited in non-commercial loan agreements (e.g. consumer loans), debtor consent is required. Debtor's consent is further needed in case of assumption of the loan contract (a structure that would be uncommon in a portfolio transaction).

With regard to banking secrecy and data protection rules, credit institutions are permitted to collect, process and exchange certain information on the credit standing of their customers in an interbank system. However, such information may be collected and processed exclusively for managing the credit risk of these institutions.

If such data is disclosed to a third party, customer's secrecy interests should be respected, all the more since no legal literature or court decisions are available confirming that in case of NPL transactions the bank's interest to disclosure outweighs a customer's confidentiality interests. Careful structuring of the transaction will therefore be required to balance compliance with banking secrecy and data protection rules and a prospective purchaser's interest of receiving full disclosure. Customer data may therefore need to be provided in an anonymised manner or on an aggregated basis so that not sensitive information is revealed.

Finally, banks do not enjoy special enforcement privileges. If no out-of-court enforcement has been agreed upon (which is subject to specific statutory requirements), secured claims will need to be enforced under regular enforcement procedures before Slovenian courts and enforcement offices.

slovenia

guide by jurisdiction

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turkey

Turkey, in the aftermath of its most severe banking and financial crisis in 2000-2001, has initiated an ambitious structural reform programme aimed at sanitising its banking and financial sector. As part of such structural renovation efforts, transactions in non-performing loan portfolios have been introduced. Asset management companies (AMC), defined in the Banking Law in 2005, are authorised entities that are permitted to engage in non-performing loans transactions. AMCs (not to be confused with portfolio management companies, which are licensed by the Capital Markets Authority) are required to be established in compliance with the Banking Law and the relevant regulation issued by the Banking Regulatory and Supervisory Authority (BRSA). AMCs, as a pre-condition to become operative, need to obtain a specific license from BRSA. Currently, there are nine AMCs who are licence by the Banking sector regulator.

AMCs must comply with a minimum share capital requirement of Turkish Lira equivalent of approximately EUR 3,400,000. In addition, certain corporate governance rules need to be observed by AMCs, such as having at least five board members.

Share transfers for more than 50% of the share capital of an AMC require pre-approval of BRSA. AMCs are entitled, exhaustively, to be engaged in the following activities as determined by the Banking Law:

- purchase of non-performing loans from financial institutions (banks, participation banks, other financial institutions);
- management and improvement of transferred assets;
- restructuring of receivables of financial institutions, delivering advisory and intermediation services during the sale of such assets to third parties;
- advising of companies in their corporate and financial restructuring processes.

Banks and financial institutions are regularly announcing tenders in relation to the sale of their non-performing loan portfolios, to which AMCs are invited to bid. Transfers of non-performing loan portfolios are performed in the form of assignment of receivables (asset transfer) and, within such framework, the consent of the debtor is not required. Blanket assignments are not recognised, and and the agreement providing for the assignment of receivables needs to set forth the specifics of each transferred receivable in the form prescribed by applicable legislation.

By the end of 2012, the nominal amount of the non-performing loans transferred by financial institutions to AMCs reached EUR 5 billion. AMCs have paid approximately EUR 600 million to financial institutions for the transfers of such portfolios. In relation to 2013, it is estimated that a further amount (notional) of receivables of EUR 1.5 billion has been transferred to AMCs.

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ukraine

The Ukrainian NPL market is dominated by local factoring companies buying loans from Ukrainian banks, where the servicing of the portfolio is sometimes retained by the originating bank. Some Ukrainian banks, however, have started moving portfolios cross border into unregulated SPVs.

It is therefore worth exploring local and cross-border structures. The issue of whether the purchase of receivables by a local company should or should not be qualified as factoring is currently broadly disputed in Ukraine. The National Commission for Regulation of Financial Services Markets of Ukraine and the tax authorities favour an opinion that all acquisitions of loan receivables qualify as factoring. At the same time, market players often favour an opinion that the acquisition of loan receivables does not necessarily qualify as factoring. Court practice on this issue is diverse and risks are minimised if the acquirer is a licensed factoring company.

If acquisition of loan receivables qualifies as factoring, a licensing requirement is triggered for the local purchaser, because factoring is a financial service, which may generally only be rendered by financial institutions. Aside from having to hold a minimum share capital of UAH 3 million (approx. EUR 270,000) for factoring companies providing only factoring services or UAH 5 million (approx. EUR 450,000) for factoring companies providing other permitted types of financial services, Ukrainian factoring companies must also comply with other requirements, in particular concerning qualified and experienced staff and sufficient technical equipment.

Another mechanism in the Ukrainian market is the acquisition of NPLs by a Ukrainian venture investment fund, as a pool of assets managed by a Ukrainian asset management company. The minimum share capital of an asset management company is UAH 7 million (approx. EUR 640,000). An asset management company is licensed by the National Commission for Regulation of Financial Services Markets of Ukraine. The asset management company issues the fund's securities and invests the proceeds from such issuance into NPLs.

Foreign SPVs can also be used for the acquisition of NPLs. Careful structuring, which will also involve a local debt collection agency or the originating bank as a servicer, and documentation will be required in order to avoid Ukrainian licensing requirements. The purchase price paid by a foreign SPV to the Ukrainian originating bank has to be registered as a foreign investment in Ukraine. Registration will allow the foreign SPV to exchange any receivables collected in UAH into a convertible currency and to withdraw money from Ukraine.

When deciding whether to use a local or foreign purchasing vehicle, the parties should not only focus on regulatory aspects but also be aware that a cross-border assignment may trigger the maximum interest rate limitations for cross-border loans, as set by the National Bank of Ukraine (NBU). While the prevailing opinion among practicing lawyers is that these limitations should not be triggered by a cross-border assignment, there is no uniform position of the NBU on this point.

Irrespective of whether a local or a foreign purchaser is involved, banking secrecy must be considered. Up until very recently, Ukrainian banks had to rely to a greater extent on borrowers' consent to transfer/disclose information constituting banking secrecy. The industry concerns were addressed in an amendment to Ukrainian banking legislation (in force since 16 October 2011) that expressly permits the disclosure of information constituting banking secrecy to the purchaser of the relevant loan receivable as well as to persons and entities providing services to the bank. At pre-execution/due diligence stages, this allows a structure under which advisors (including legal advisors) are formally appointed by the originating bank, thereby obtaining access to banking secrecy relevant information, and produce reports to an interested party that contain aggregated information only, that is, without containing sensitive information.

An assignment of receivables and related security can usually be structured as a true sale. Registered security interests can also be validly assigned together with the loan receivables. The form requirements applicable to the assigned security interests have to be followed in the receivables purchase agreement. For example, mortgages are usually notarised; hence, the receivables purchase agreement must be notarised too. The transfer of the security interest will only be opposable against third parties upon completion of re-registration of registered security interests. The resultant cost and timing issues are not deal breakers, but will have to be considered when pricing the transaction and when considering deal closing mechanics.

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disclaimer

The general overview set out in this guide has been prepared for information purposes only and does not purport to constitute (nor may it be interpreted as substituting) transaction-specific legal advice. It does not purport to be exhaustive in any respect.

This guide is based on the relevant laws and regulations as of 28 February 2014 and may therefore not present an accurate picture of the legal situation in the future.

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