Theodor Baums*

Asset Securitization in Europe

Contents

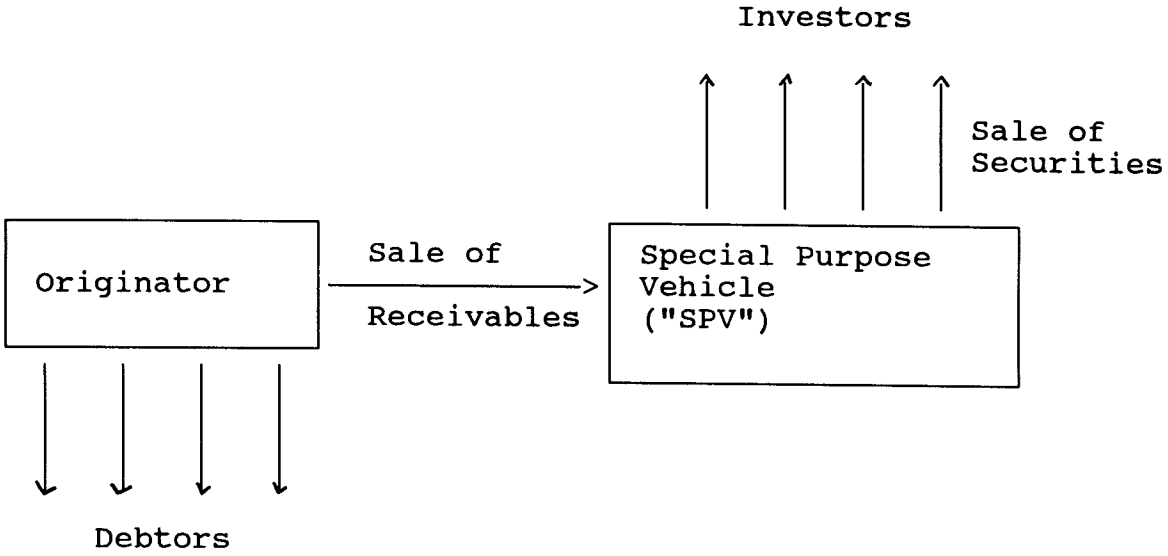
I. Introduction

Until the late 1980s, asset securitisation was an US-American finance technique. Meanwhile this technique has been used also in some European countries, although to a much lesser extent. While some of them have adopted or developed their legal and regulatory framework, others remain on earlier stages. That may be because of the lack of economic incentives, but also because of remaining regulatory or legal impediments.

The following overview deals with the legal and regulatory environment in five selected European countries. It is structured as follows: First, this finance technique will be described in outline to the benefit of the reader who might not be familiar with it. A further part will report the recent development and the underlying economic reasons that drive this development. The main part will then deal with international aspects and give an overview of some legal and regulatory issues in five European legislations. Tax and accounting questions are, however, excluded. Concluding remarks follow.

II. Model of a Securitization Transaction

Asset securitization can be generally defined as the process of transferring certain receivables, such as bank loans, credit card receivables, or trade receivables, from their "orginator" or owner to a separate entity. This entity in turn will issue and sell securities representing interests in such receivables. A special variation are mortgage-backed securities. The following chart shows a simplified structure of an ABS transaction.


Investors
Sale of Securities
Originator
Sale of Receivables
Special Purpose Vehicle ("SPV")
Debtors

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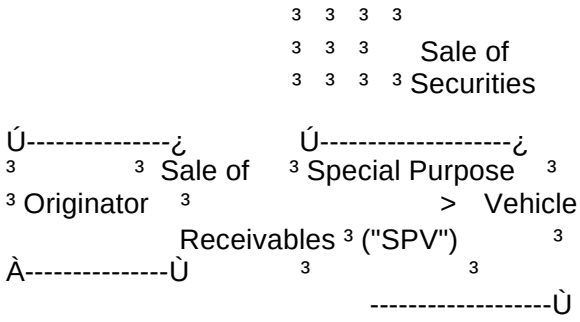

Although there are many methods for securitizing assets, most securitization transactions involve some or all of the following parties: (1) the initial owner of the assets; (2) the issuer of the debt or equity instruments; (3) the investment bankers who assist in structuring the transaction and who underwrite or place the securities; (4) the rating agencies; (5) a credit enhancer who provides credit support through a letter of credit, guarantee, or other assurance; (6) a servicer who collects payments due on the underlying assets and pays them over to the security holders; (7) a trustee, who deals with the credit enhancer, servicer, and issuer on behalf of the security holders; and (8) legal counsel.

The owner of the assets to be securitized is usually a bank, finance company or other holder of income-producing assets such as mortgages, auto loans, credit card receivables or other receivables. These assets are typically pooled together and sold to a special-purpose vehicle so as to separate the assets from other assets of the originating institution. This special purpose vehicle will then issue and sell securities representing interests in the assets. The issued securities may be either debt or equity. In order to ensure that the issued securities receive a high rating from the rating agencies, some type of credit enhancement, such as a letter of credit, is usally used. Some issuers provide for internal credit support by issuing two classes of securities, a "senior" class, which is generally triple-A rated and enjoys certain priorities with respect to collections on the assets, and a "subordinated" class, which is rated in a lower rating category and is subordinated in part to the right of the senior class to receive such collections.
Once assets have been securitized, some party must continue to collect payments on the assets and disburse those proceeds to the securities holders. Typically this party will be the originator (seller) of such assets.

One of the key advantages to securitizing assets is that the securities may often receive a rating significantly higher than that of the originating institution itself. Therefore rating agencies like, for instance, Standard & Poors or Moody's Investors Service, will evaluate the quality of the underlying assets, look at the overall risk profile of the originator, the collection procedures, the selection of the receivables transferred to the issuing entity and so on.

III. Historical Development and Economic Forces behind Securitization

A. Historical Background and Recent Development

A variety of legal and economic factors have combined in recent years to cause a widespread boom in asset or mortgage securitization in the U.S.[1]. In the United States the total outstanding asset (including mortgage) backed securities currently are well in excess

of 2 trillion U.S.-$ with daily trading volumes at the larger investment banks in the tens of billions of dollars[2].

This rapid growth has naturally resulted in numerous attempts to transfer this technique to markets outside the United States, most notably to Europe. However, these projects have met with mixed success.

The largest non-U.S. market has developed in the United Kingdom. The next largest market is France. Other European markets have also begun to develop but are still in the nascent stages. Spain and Belgium have adopted a legislative framework only recently. Isolated transactions have also been completed in Italy and Germany. As to the Netherlands, no public off-balance sheet mortgage or asset-backed transactions have been done to date to my knowledge[3]. However, some securitised transactions in other countries have used Dutch special purpose vehicles as issuing entities, and although no public deals have been brought, the domestic market has seen certain private placements backed by diversified assets.

Asset securitization as it is known today got its start with "the development of the modern mortgage-backed security"[4]. Initially, such development began because of a U.S. federal government desire to develop a secondary mortgage market for residential mortgage loans[5]. Thus the first asset-backed securities issued were backed by pools of mortgages insured or guaranteed by Government agencies such as the Government National Mortgage Association (Ginnie Mae), the Federal Home Loan Mortgage Corporation (Freddie Mac), and the Federal National Mortgage Association (Fannie Mae)[6]. Later on banks responded to pressures on their profitability and legal changes with securitization of their assets. In the 1980s securitization spread to non-mortgage assets, namely loans, credit-card and other receivables. What are the economic forces that drive this development?

B. Economic Forces behind Securitization

In order to truly understand the development of asset securitization, it is important to understand the forces which made, and continue to make, securitization desirable. In particular, what advantages does asset securitization have over more traditional forms of funding?

1. Depositary Institutions

In part, securitization developed as a result of economic and legal pressures on depositary institutions.

Traditionally, banks and thrifts have played the role of financial intermediaries, engaging in what is known as "spread banking", whereby such institutions gather liabilities (typically deposits) to fund assets (typically loans) and retain as profit the spread between the total cost of the liabilities and the total yield on the assets[7]. Asset securitization offers an alternative source of funding, and may therefore be attractive to many of these depositary institutions[8]. Asset securitization allows assets to be removed from the institution's balance sheets, and thus reduces the amount of capital such institution must maintain to comply with regulatory requirements[9]. Securitization also breaks up the traditional role of depositary institutions as financial intermediaries into its component parts, allowing for specialization by institutions with comparative advantages in one or more of these functions[10].

2. In General

Asset securitization has further advantages which apply to all sellers of receivables. First, securitization is often more cost attractive than sales of whole loans because it offers investors a more liquid investment (a tradeable security) with more desirable risk characteristics and thus appeals to a wider pool of potential purchasers[11]. Securitization is particularly cost attractive for sellers whose access to other forms of credit may be limited, since asset-backed securities are rated on the merits of the underlying assets rather than on the financial status of the issuing or selling company[12]. Second, asset securitization reduces the seller's exposure to interest rate risk, prepayment risk, and credit risk[13] by

allocating some or all of such risks to the purchasers of the securities and a credit enhancement vehicle[14]. Finally, asset securitization allows the seller to more efficiently match the terms of its assets with those of its liabilities, since asset-backed securities can be issued for terms which correspond to the term of the assets underlying such securities[15].

IV. International Aspects of Securitisation

Securitization can have international connotations in several ways. Issuers of securities backed by assets from one country may sell such securities in foreign markets. And owners of assets in one country may use a special purpose vehicle based in another country to issue mortgage- or asset-backed securities. At this point we can only point at the regulatory and legal issues that will come up in the future with the further internationalization of the securitization business.

A. Sale of ABS or MBS Internationally

The development of securitization internationally began with the sale of securities backed by U.S. assets in the European and Japanese markets[16].

The first step in securitizing U.S. assets in markets abroad came in the form of Eurodollar deals[17]. In these deals the U.S. issuers sold dollar-denominated asset-backed securities to purchasers in European countries, often listing the securities on the Luxembourg Stock Exchange[18]. The process of tapping the Eurodollar market was fairly simple to achieve from a legal perspective since the Eurobond market is relatively unregulated, and it enabled U.S. issuers to expand their sources of capital[19].

Mortgage-backed securities especially have been sold extensively in Europe, in particular bonds that have been structured to look like the type of instruments European investors are used to buying: products such as Libor floaters, and PAC bonds that look more like corporate bonds and have less prepayment risk than the traditional MBS[20].

The sale of securities backed by U.S. assets to foreign markets is likely to continue in parallel with the general globalization of capital markets[21]. Through this process, issuers are able to optimize the pricing and terms of securities issued, sometimes through the overseas issuance of a security with a particular currency and type of interest rate (floating or fixed), combined with currency or interest rate swaps (or both), to create a synthetic security with the desired characteristics[22].

B. Securitization of Foreign Assets

Securitization of assets from countries outside of the United States has been slower to occur. That has partly to do with the different economic environment and different incentives in those countries. For instance, German banks did not feel a pressure comparable to that for U.S. commercial banks to remove assets from their balance sheets in order to meet the BIS 8 % capital adequacy requirement. Additionally, in many countries legal obstacles to asset securitizations existed or do still exist; I will get back to these legal obstacles in the main part of my article.

Many countries have developed the need to securitize assets prior to developing the legal and technical framework necessary to do so. One such example is Japan, where banks were coming under pressure to reduce their assets to comply with the capital adequacy guidelines imposed by the Basle accord, but where certain legal problems impeded and still impede domestic securitization[23]. Financial institutions in such countries have found and still may find it desirable to securitize their assets using special purpose vehicles in securitization-friendly countries like the United States. For instance, of some 72 asset-backed commercial paper programs established in the United States by commercial banks, 27 were sponsored by Japanese, European or Canadian banks[24]. In particular, nine of these programs were established to purchase non-U.S. receivables[25].
In a variation on this theme, non-U.S. banks have started international asset-backed commercial paper programmes, allowing a number of companies to sell receivables to a single vehicle[26]. The first of these multi-seller vehicles sponsored by European banks

emerged at the end of 1992, with Barclays' SCEPTRE and Morgan Grenfell/Deutsche Bank's TWIN TOWERS programmes[27].

Because a number of sellers with a variety of receivables can share the costs of securitizing, these multi-seller vehicles are particularly cost-effective[28]. Such vehicles should increase the viability of securitization as a financing tool in Europe by lowering transaction costs, reducing administrative time and costs, and improving asset diversification, name recognition and investor appeal[29].

C. Domestic Securitization Programs

The slowest process of all has been the process of establishing the legal framework for securitization in individual countries. Those countries which have been successful in doing so have found themselves home to many special purpose vehicles issuing securities backed by assets from their own and/or foreign countries. Nevertheless for most countries the process has been slow up to now.

The framework for securitization varies significantly from country to country, and the next part will discuss such issues in detail for five selected European countries. Tax and accounting questions will be omitted, however.

V. Selected European Countries

A. United Kingdom

1. Introduction

The United Kingdom has led Europe in securitization transactions, primarily through the issuance of mortgage backed securities[30]. Although the mortgage securitization market in the UK is relatively small in relation to the total mortgage market[31], and the market has developed without the benefit of government support[32], the UK has nevertheless developed a sound framework for mortgage-backed securities[33].

The market for non-mortgage asset-backed securities, however, has been slower to develop in the UK. Nevertheless, as of mid-1993 there had been seven term securitizations involving assets other than first mortgages, totalling œ 1.388 bn[34]. In addition, several UK banks have also been involved in establishing asset-backed commercial paper (CP) programmes[35].

The ABS issuances in the UK to date have involved car loans[36], home equity or second mortgage loans[37], and tax-based vehicle finance leases[38]. As of mid-1993 there had not been a credit-card backed issuance in the UK[39].

2. Securitization Framework

The infrastructure in the UK, unlike many other countries in Europa, is fairly well suited for asset securitization[40]. Although there are no specific laws governing securitization, as, for instance, in France[41], the regulatory authorities have, for the most part, been willing to accommodate the growth of asset securitization.

a) Capital Adequacy

The Bank of England which regulates banks has instituted some fairly strict capital adequacy requirements which ensure that a bank can have a reduced need for capital only if it has no risk from the loans which it has sold[42]. The same is true for the building societies which are regulated by the Building Societies Commission[43]. These building societies may, pursuant to the 1986 Building Societies Act[44], issue mortgage-backed securities. Since most issuances of mortgage-backed securities in the UK have left the originator with some interest rate risk[45], banks and building societies have still had to provide fully in (their) capital for the loans involved[46]. A small number of issuances have attempted to deal with this problem by laying off the interest rate risk to another institution[47].

b) "True Sale"

Since asset securitizations are often undertaken for capital adequacy reasons, the structure of these transactions often relies on the financial institution's ability to treat the transfer of loans as a sale[48]. The two issues here are how to transfer the underlying receivables; and whether the SPV is independent from the seller in the event of the seller's insolvency[49].

In the UK, there are generally three methods of transferring a receivable, novation, assignment and sub-participation[50]. Since *novation* (essentially a re-creation of the obligation) requires the consent and cooperation of all three parties - the SPV, the originator and the account debtor - it's infrequently done[51]. Therefore this method of transfer will not be discussed here any further.

There are two methods of transferring by *assignment*. They are legal and equitable assignmet. Legal assignment seems at first glance ideal for asset securitization, since the consequence of a legal assignment is that the whole and beneficial title is transferred to the SPV, leaving little doubt that the transaction is a "true sale"[52]. Legal assignment, however, includes a statutory requirement to give written notice to the account debtor[53]. This notice requirement can pose problems for a potential asset securitizer because it is administratively cumbersome, and because the securitizing institution may not wish to let their account debtors know that their receivables have been financed, because it gives the wrong impression[54].

Equitable assigment may prove an attractive alternative to legal assignment, since under English law, an equitable assignment would qualify as a "true sale" and would not require notice to the account debtor[55]. There are several disadvantages, however, to using equitable assignment as opposed to legal assignment[56]. First, without notice, the account debtor can discharge the receivable by payment to the originator[57]. Second, the SPV is subject to any set-off which the account debtor might obtain against the originator, both before and after transfer[58]. Third, there remains the possibility that a later sale of the SPV's receivable to a bona-fide purchaser would defeat the SPV's interest in such receivable[59]. Fourth and finally, the SPV procedurally would not be able to sue directly, it must join the originator in any legal proceeding[60].

The final method for transferring receivables in the UK is through a *sub-participation.* Sub-participation, known as a back-to-back loan, is where another bank "purchases" financial assets from their originator by making a loan to the "seller" with recourse limited to the sub-participated assets[61]. In order for such a transfer to be a "true sale", the seller must not have any obligation to fund the repayment of the sub-participation loan[62].

c) Protection of SPV from Originator Insolvency

The bankruptcy-remoteness of the SPV is, of course, a major concern. For SPV's established by banks to be treated as off-balance sheet for capital adequacy purposes, essentially, there should not be any recourse legal, moral or financial from the SPV to the originator of the loans. This is the main reason why, in Common law countries like the United Kingdom, the SPV's are owned by Trusts whose share capital is owned by a third party not linked in any way to the originator.

A further concern in the UK is that where equitable assignment has been used, it is important that there are triggers inserted so that the SPV can perfect its equitable assignment into a legal assignment by notice to the account debtor at any time when it looks as though the originator is getting into financial difficulty[63].

In circumstances where the originator acts as the paying and servicing agent for the SPV and therefore holds money on behalf of the SPV, the protection of the SPV's interest in the collected receivables in the event there is an insolvency of the originator is also of concern[64]. In the UK, the most common way of protecting the SPV's interest is to set up a separate account into which all payments that the originator receives are placed, and to provide that that effectively is a trust account for the SPV[65]. This should protect the SPV's interest in the cash in the event of an insolvency as long as there is no commingling in that

account[66]. Further protection can be achieved by providing that the SPV takes a security interest over the cash in the account[67].

B. The Netherlands

1. Introduction

Domestic securitization of assets from the Netherlands has, to my knowledge, not yet been attempted[68]. There has, however, been significant securitization activity in the Netherlands in the form of securitized transactions originating in other countries for which Dutch special purpose vehicles have been used as issuing entities[69]. I therefore briefly discuss the prospects for domestic securitization programs in the Netherlands, and then focuse on the securitization infrastructure in the Netherlands, in particular as it relates to the establishment of a SPV.

The reason that domestic securitization programs have not developed in the Netherlands seem to be more economic than legal or technical[70]. In particular, a primary reason is simply that the major corporations and other institutions in the Netherlands lack the economic incentive to do so[71]. These institutions are still able to obtain funding at low spreads by using more traditional forms of financing[72]. Further obstacles to privatisation in the Netherlands include the prohibitive costs associated with initial issues of asset-backed securities[73] as well as the conservative approach allegedly taken by the Dutch financial market and investors towards innovative financing techniques[74].

2. Securitization Framework

As mentioned earlier, although the Netherlands has as yet no domestic program in asset securitization, it has been a preferred location for the bankruptcy-remote special purpose vehicles used to issue asset-backed securities. Although the continued use of the Netherlands as a "safe harbour" for SPV's has been cast into doubt by the introduction of the new Dutch Civil Code[75] the Netherlands continue to offer certain tax and legal advantages to SPVs. The major legal issues again are associated with the implications of a transfer of receivables to the SPV, and with the bankruptcy-remoteness of the SPV.

a) Transfer of Receivables

Traditionally, Dutch law allowed for a very easy way of transferring receivables[76]. A contract between the seller and buyer was sufficient, and no notice to the account debtor was required[77]. The new Dutch Civil Code, however, requires that account debtors be notified in order to effect transfer of legal title to receivables[78]. Although the code does not formally specify the type of notice required, in practice written notice will probably be necessary[79].

It is possible that this notice requirement could be avoided by not effecting a legal transfer of the receivables, but instead using a sales contract whereby the originator sells a portfolio of receivables but does not transfer it to the SPV and it is agreed that the SPV will have to write to obtain title to the receivables on first demand[80]. However, there is little or no case law on the implications of such a transfer, so whether or not it would legally achieve the same result as a straight transfer of legal title is a matter of speculation[81].

Additional issues related to the transfer of receivables include: the ability to transfer future receivables, the effect of a transfer on the security attached to the receivables, and the ability to match maturities with an asset securitization[82]. Such issues are highly complex and beyond the scope of this article. It is sufficient to say that while these concerns may make certain types of securitization problematic, they should not in general pose serious problems[83].

The securitized receivables, once transferred to the SPV, must be charged in favour of the investors[84]. In the past this was accomplished through either a fiduciary assignment or a pledge of the receivables in favour of the investors[85]. The new Dutch Civil Code provides only for a pledge of the receivables, and as of 1992 all fiduciary assignments were converted into pledges[86].

b) Bankruptcy-Remoteness

In the situation where an originator wishes to securitize receivables through a Dutch SPV, such SPV would probably be set up with the help of a bank[87]. The originator would then sell its receivables to the Dutch SPV, which would issue securities backed by the receivables in order to fund the purchase price[88]. Credit enhancement may be limited to over-collateralization, or may include insurance such as a letter of credit provided by the bank aiding in the establishment of the SPV[89].

In this context, it is important to reduce as much as practicable the possibility that the bankruptcy of the shareholders of the SPV triggers the bankruptcy of the SPV[90]. A SPV may be insulated to some extent from the insolvency of its shareholders through the creation of a foundation ("stitching") which holds all shares of the SPV[91]. This foundation would most likely be managed by a board of management elected by the bank aiding the foreign corporation in its establishment of a Dutch SPV[92]. It should be specifically provided in the Articles of Association of such foundation that the foundation serves only to hold the shares in the SPV, and that it has neither the right to undertake any other activity than exercising its shareholders' rights, nor the right to incur any liability[93].

To further limit the risks associated with bankruptcy of the originating corporation, it should be ensured that the SPV itself does not enter into transactions other than the securitization transaction in question[94]. In short, a separate SPV ought to be set up for each individual securitization transaction, and the objects and purposes clause of the Articles of Association of the SPV should limit the SPV to such transactions as are necessary to effect the securitization[95].

c) Regulatory Questions

A further cause for concern is the possibility that a SPV located in the Netherlands might be considered a "credit institution" or a "capital market institution", and would thereby have to comply with the Dutch Banking Act and the governance of the Dutch central bank[96]. In principle, a SPV could easily fall within the definition of a "credit institution" or a "capital market institution"[97]. However, the Dutch central bank has laid down special policies for companies engaged in the business of the receipt of funds from non-residents and on paying such funds to non-residents, so-called "finance companies"[98]. A SPV issuing securities backed by foreign receivables would clearly qualify as such a "finance company"[99].

The Dutch central bank policies on finance companies provide that if they adhere to certain ground rules, they will not be regarded to be credit institutions or capital market institutions[100]. These ground rules essentially boil down to a requirement that, in order to avoid becoming subject to central bank supervision, a SPV must only issue debt with a maturity of two years or more and it may issue that debt only to professional investors[101].

C. France

1. Introduction

Securitization was introduced into French law in 1988, as part of a general modernization of the French financial context[102]. The basic legal framework was established with Law no 88-121 (December 25, 1988), and that Act has since been supplemented by numerous implementation decrees and regulations, as well as a recent Law no 93-6 (January 4, 1993)[103].

France chose to promote securitization for a number of reasons. One of the main goals of the introduction of securitization in France was to enable credit institutions to sell their receivables secured by mortgages[104]. This explains why the 1988 Law as implemented only permitted securitization of receivables with at least a two-year final maturity[105]. However, as of early 1993 there had been only one securitization of French mortgages[106].

A second purpose for promoting securitization in France was to aid French credit institutions to abide by the minimum solvency ratio of 8 % set by the BIS for international banks[107].
Beginning on January 1, 1993, this solvency ratio was extended to all credit institutions in the European Community pursuant to the EC Directive no. 89/647 of December 18, 1989[108]. Since French credit institutions had previously only been subject to a minimum ratio of 5 %, the application of the BIS solvency ratio significantly increased the capital requirements of French credit institutions[109]. Accordingly it became crucial for the public authorities to assist French banks in meeting these new requirements, and the introduction into France of the technique of securitization was intended to help French banking institutions to increase their capital in the same conditions as their foreign counterparts[110].

A third and related purpose for permitting asset securitization in France was an effort to strengthen the international competitiveness of French credit institutions[111]. Asset securitization would give French credit institutions access to the same funding options available to American banks, in order to replace traditional funding sources the costs of which are rising, such as retail deposits and commercial paper[112].

As of the end of 1992, there had been a total of 55 non-mortgage asset securitizations in France, and one mortgage securitization[113].

2. Securitization Framework

Although the framework for securitization in France was, as mentioned earlier, established in 1988, providing potential French securitizers with a clear legal accounting and tax road to follow in order to structure an operation, the growth of securitization thus far has been slow[114]. Technical, financial, and legal obstacles have combined to slow the growth of securitization.

a) The "Fonds Commun de Cr,ances" (FCC)

As discussed earlier, the legal framework for securitization was established with Law no 88-121 (December 23, 1988). This law established a new type of special purpose vehicle, called a *Fonds Commun de Cr,ances* (FCC)[115]. In the simplest terms, a FCC owns a pool of *cr,ances* (receivables) and issues *parts* (share certificates) to investors. These shares are not beneficial interests, but instead represent a direct claim on the FCC's assets[116]. A FCC is not subject to corporate or insolvency law; instead it can be characterised as a co-proprietorship among investors. The FCC is initiated by a management company which administers it and represents it against third parties[117]. In addition, there is a depositary which holds the receivables and accounts of the FCC and controls the decisions of the management company[118].

However, the initial statutory regime as established by the 1988 Law was not ideal for general securitization as it included certain restrictions and obstacles[119]. Many of those obstacles have been removed meanwhile, although some still remain.

A major obstacle to the development of securitization in France arising from the 1988 Law was its requirement that receivables eligible for securitization must have a maturity of at least two years[120]. This requirement effectively ruled out the securitization of credit card receivables and other revolving credit assets[121], as well as short term consumer loans[122]. A March 27, 1993 decree implementing the 1993 Law has, however, eliminated the requirement of a minimum maturity for securitized receivables[123]. Securitization of credit card receivables and other short term assets is therefore possible under the current French legal framework.

The 1988 Law further limited the types of receivables which could be securitized in France to "secure" receivables, i.e., receivables which are neither fixed nor doubtful nor subject to judiciary proceedings[124]. This restriction, while strongly criticized[125], remains in place. Thus French institutions may not securitize doubtful receivables or bad debts, such as troubled real estate loans or doubtful receivables from developing countries[126].

The 1988 Law further limited the receivables eligible for securitization to those represented by credit operations of the same nature[127]. The 1993 Law, however, has removed this requirement[128].

Until the 1993 Law, securitization in France was limited to assets held by credit institutions[129]. The 1993 law extended the scope of receivables eligible for securitization to receivables held by insurance companies[130]. At present, however, companies other than credit institutions and insurance companies may not securitize their assets[131], although the extension of securitization to receivables held by commercial companies has been suggested as a further modification to the French legal framework[132].

Pursuant to the 1988 Law, FCCs could not substitute new assets for the original ones, or proceed with further acquisitions of receivables[133]. This limitation impacted the profitability issuance with a maturity longer than the life of the underlying assets[134]. The 1993 Law has removed this limitation and now allows FCCs to acquire securitized receivables after the issuance of the certificates, the effect of which is to contribute to the overall reduction of the total cost of the securitization process[135].

b) Bankruptcy Issues

A major concern for French securitizers is that, in the event that bankruptcy proceedings are initiated against the institution assigning the securitized receivables or the institution responsible for the management of the FCC no mechanism presently exists which would permit the legal isolation of sums or receivables located within one of the above entities and which belong to the FCC[136]. In the event such bankruptcy proceedings did occur, current French law would treat the FCC as a non-privileged creditor[137].

The most recent draft of the French law on trust (hereinafter "draft trust law") would afford the FCC greater protection in the event of a bankruptcy. The draft trust law provides that the trust "is a contract pursuant to which a settlor transfers all or part of its assets to a trustee. ... the latter being in charge of acting for the settlor or the beneficiaries, for a specific purpose"[138]. In a securitization transaction, the entity transferring the receivables would be the settlor, the management company and the depositary would represent the trustees, and the holders of FCC shares would be the beneficiaries[139].

The draft trust law would afford the receivables full protection in the event of a bankruptcy affecting the transferring entity, the management company or the depositary by providing that the assets and rights transferred to the trustee constitute separate assets which may not be attached or pledged by the creditors of the settlor or of the trustee[140]. In addition, it would create a direct contractual relationship between the institution transferring the receivables and the management company[141].

The draft trust law is still subject to a number of uncertainties from a legal and tax standpoint[142]. Further modifications of the law will therefore be required if the improvements described above are to be fully realized[143].

c) Regulatory Framework

The Commission des Op,rations de Bourse (COB) generally regulates French financial institutions, along with the Comit, de la R,glementation Bancaire, the Service de Legislation Fiscale, and the Banque de France[144]. The French regulatory authorities have taken more stringent positions than their counterparts in other European countries on several issues[145].

Some of the more stringent requirements imposed by French regulators are related to investor protection[146]. For example, the creation or liquidation of an FCC used to require the prior consent of the COB, following consultation with the Banque de France[147]. As part of this process the COB had to be provided with a report on the certificates to be issued by the FCC and the pool of receivables, prepared by a rating agency approved for this purpose by the French Ministry of Finance[148]. The 1993 Law has simplified this approval process, so that only the management company of the FCC requires such prior approval[149].

The rating agency report described above, however, must still be submitted to the COB for consultation, and must be provided with an issue offering circular to the subscribers of the FCC's certificates[150].

A further restriction which the COB has placed on French securitization is that it requires that the offering itself must be made with a firm underwriting commitment that the placement period shall not exceed thirty days[151]. In addition, the COB provides for specific procedures related to the end of the certificates subscription period and provides that certificates of the FCC must be listed on a French exchange market, unless their initial par value is 1,000,000 French francs or more[152]. On a positive note, however, the above-mentioned restrictions may soon be modified by the COB[153].

In addition, French law requires a FCC to provide credit enhancement in the form of an external guarantee of a financial institution, credit institution or an insurance company, over-collateralization or a subordinated class of certificates (such certificates may not be, however, held by individuals or UCITs)[154]. According to practitioners, this system is sometimes inadequate since it is limited to the risk of the debtor's default and it is often too complex, particularly for transactions presenting few risks or already covered through other guaranties[155].

D. Belgium

1. Introduction

Belgium is another interesting case which shows some of the traditional impediments to the creation of secondary markets for receivables in European countries on one side as well as their recent efforts to modernize their financial systems on the other.

Securitization in its proper sense has not been practical in the past in Belgium for several reasons[156]. Belgian law until recently provided no form of entity that could serve as a special purpose vehicle, and the legal procedures governing the assignment and sale of receivables remain burdensome and thus hinder large-scale transfers of receivables.

2. Securitization Framework

a) Assignment of Receivables

The main general legal constraint on securitization in Belgium is found in Article 1690 of the Civil Code. An assignment of receivables is subject to the procedures set forth in this article. In order for the sale of a receivable to be opposable to third parties, Art. 1690 requires either the notification of such transfer to the debtor by bailiff or, alternatively, the acceptance of such transfer by the debtor in a deed drawn up before a notary public. Given the time and costs involved in complying with these requirements, it is obvious that any mass assignment of receivables is impossible in a practical and economic sense. However, draft legislation aimed at abolishing these requirements has been prepared and is currently before Parliament. Under the draft legislation, the assignment of debt will be legally valid and opposable to third parties in the event of mere agreement between the assignor and the assignee. The bill further provides that the assignment of a receivable is opposable to the debtor, on the condition that the debtor has been simply notified (with no formalities required) of the assignment[157].

2. The Special Purpose Vehicle Law of 1992

Until recently, Belgian law did not provide for a form of entity that could serve as a special purpose vehicle. Special purpose vehicle legislation, however, has now been enacted. A new law, as of August 5, 1992 has been enacted to create a legal framework for the "Organismes de placement en cr,ances/Instellingen voor belegging in schuldvorderingen" ('Institutions for investments in receivables", IIR). This form of entity may be set up either under existing corporate law or by way of a contract among the parties. The statutory corporate version ist called a "soci,t, d'investissement en cr,ances - vennootschap voor belegging in schuldvorderingen", and the contractual version is known as a "fonds de placement en cr,ances - fonds voor belegging in schuldvorderingen".

These special Belgian vehicles, whether corporate SPVs or contractual SPVs, must be administered by a separate management company[158]. Royal decrees which are to implement several provisions of the law are still to be promulgated[159].

E. Germany

Asset-backed securitisation has begun only recently in Germany. A few German companies have already securitised auto loans in the U.S. market or German trade receivables via off-shore special purpose vehicles, enabling them to sell their assets anonymously. There have also been two Deutsche Mark-denominated transactions involving consumer loans[160]. Deutsche Bank has recently set up a SPV on the Isle of Jersey with the purpose to fund the acquisition of receivables and similar assets by issuance of notes.

ABS is, in principle, legally feasible in Germany. Loans or other receivables can be assigned easily without the consent of the debtor or additional formalities. Although an Anglo-Saxon style trust cannot be formed under German law, a SPV could be created in the form of a limited liability company[161]. The use of off-shore SPVs so far is mainly tax driven.

Asset-backed products in Germany face some more other obstacles. The attitude of the Federal Banking Supervisory Agency (Bundesaufsichtsamt f•r das Kreditwesen, Berlin) is somewhat reserved as far as sales of loan receivables by banks are concerned. A further impediment lies in the structure of the primary lending market. These are dominated by credit institutions offering the full range of financial products (Universalbanken). Lending markets are very competitive, and the low credit margins make it difficult to cover the additional transaction costs associated with securitization. There may be more incentive for securitization for car loans, leasing firms or firms with large masses of trade receivables.

As to mortgage-backed securities, a similar structure exists in the Hypothekenbanksystem. For over two hundred years, German mortgage banks have funded themselves by issuing *Pfandbriefe*, making these one of the earliest kind of mortgage-backed securities. In contrast with US asset-backed techniques, however, the underlying loans stay on the balance sheet of the mortgage bank. Another difference from the US and UK situations is that a German mortgage bank may exclude the prepayment of a loan secured by a mortgage. Unlike US and UK mortgage-backed bonds, therefore, German *Hypothekenbankpfandbriefe* have no prepayment risk.

This combination of an efficient existing funding system and the strong capitalisation of the mortgage banks suggests that the development of an off-balance sheet mortgage-backed security market is unlikely in Germany[162].

VI. Concluding Remarks

In Europe, securitisation has been more discussed than practised so far. Many structural impediments, tax, regulatory and legal, remain. These will be repealed the more competition and internationalization of the capital markets will develop, and the demands of the originators of receivables as well as of the investors will press legislators and regulators to provide for the necessary frameworks. As always, more in-depth comparative studies than could been made here will help us to develop our national legal and regulatory systems further. While profitting from each other in that way in Europe we should carefully see to maintain the advantage of having various competing sets of rules[163].

[*] Dr. jur, Professor of Law, Director, Institut f•r Handels- und Wirtschaftsrecht, Universit„t Osnabr•ck. Lecture, given before the Forum Internationale, May 3rd, 1994, Peace Palace, The Hague. I am grateful to Brian Swanson, Summer Associate to Shearman & Sterling, Frankfurt/New York, for his research assistance.

1 Joseph C. Shenker & Anthony J. Colletta, "Asset Securitization: Evolution, Current Issues and New Frontiers", 69 Texas Law Review 1369, 1382 (1991).

[2] Robert L. Sheehy, Mortgage-Backed Securities - Where is the MBS market going?, 4 Der Langfristige Kredit 36 (1994).

[3] Cf. ISR-International Securitisation Report, March 1993, Issue 1, at p. 151.

[4] Shenker & Colletta, supra note 1, at 1383. Some commentators argue that the concept of asset securitisation has been with us since before the turn of the century. See, e.g., id. at 1380-82. Nevertheless, it is clear that the widespread use of asset securitisation and its recognition as a "significant financial innovation" only occurred within the past 20 years. Id. at 1382.

[5] Id. at 1383. Underlying the effort to develop a secondary mortgage market was a "federal government policy to increase the availability of funds for housing finance by redirecting capital with the housing finance system between mortgage lenders in different regions with differing demand for mortgage loans and by shifting capital from the capital markets to the housing finance system". Id.

[6] Id. at 1384. For a more complete discussion of the growth of mortgage-backed securities in the United States, see id. at 1383-88.

[7] Shenker & Colletta, supra note 1, at 1389.

[8] Id. at 1391.

[9] Id. at 1391-92. For more detailed discussions of capital adequacy requirements and their relationship to asset securitisation, see id. at 1395-96; Robert I. Reich & Charles W. Sewright, Jr., "The Bank Role", in: Handbook on Asset-Backed Securities 385, 391 (1990).

[10] Shenker & Colletta, supra note 1, at 1392.

[11] Id. at 1391. For further discussions of this advantage, see id. at 1393.

[12] Suzanne Wittebort, "Asset backeds come of age", Institutional Investor, Dec. 1991, at 126-27.

[13] For more detailed discussions on the reallocation of interest rate, credit, and prepayment risks through asset securitisation, see Shenker & Colletta, supra note 1, at 1394; Reich & Sewright, supra note 9, at 389-90.

[14] For an explanation of the role of credit enhancement in asset securitisation, see Zo‰ Shaw (ed.), International Securitisation, 1991, at 164 ff.

[15] Shenker & Colletta, supra note 1, at 1393. It has also been argued that depositary institutions acting as purchasers of asset-backed securities can better match assets with liabilities by selecting securities with lives corresponding with the terms of particular deposits of that institution. Id.

[16] Shenker & Colletta, supra note 1, at 1422.

[17] Id.

[18] Id.

[19] Id.

[20] Michael Marray, "Riding the Rollercoaster", Euromoney, Oct. 1992, at 55.

[21] See Shenker & Colletta, supra note 1, at 1422.

[22] Id.

[23] Id, at 1424, 1425; for a description of the 1992 amendments see the International Securitisation Report (supra note 3), at 135 f.

[24] Federal Financial Institutions Examination Council's Feb. 12, 1993 Letter Requesting Comments on its 'Staff Proposal' (March 2, 1993), at 6.

[25] Id.

[26] "Editor's Introduction", International Securitisation Report (supra note 3), at 6.

[27] Id.

[28] See Jason HP Kravitt, Ian R. Coles & C. Mark Nicolaides, "Coping with Cross-Border Securitization", International Financial Law Review, Nov. 1991, at 34, 38.

[29] See id. For a sample structure for this type of multi-seller transaction, see id.

[30] Henry T. Mortimer, "Development of Asset Securitisation in Europe", in: Structured Finance: Design, Engineering & Production (Seminar Transcripts from Euromoney Conference in Brussels, June 4-5, 1992), at 5; David M.W. Harvey, "Securitisation Goes International", Bankers Mag., May/June 1991, at 27.

[31] "Country-Report and Database: United Kingdom", International Securitisation Report, March, 1993 (hereinafter "UK Report"), at 201, 201.

[32] Id. at 202. In the United States, government agencies such as Freddie Mac and Fannie Mac spurred the development of a mortgage-backed securities market by providing an outlet for sale of mortgage loans and by providing credit enhancement for the issuance of mortgage-backed securities. Id.

[33] UK Report, supra note 31, at 203.

[34] Id. at 207.

[35] Id.

[36] Four of the seven ABS deals in the UK as of mid-1993 had involved car loans, beginning with CARS 1, a July 1990 issuance "based on car loans originated by Chartered Trust". Id. For a more detailed discussion of CARS 1, see Julian Lewis, "Dollar Issues Dominate European Market", Euromoney, Sept. 1990, at 198, 204-205.

[37] Two of the seven ABS deals in the UK as of mid-1993 involved home equity or second mortgage loans. UK Report, supra note 31, at 207.

[38] A December 1992 ABS issuance, Truck Funding, "was an innovative securitisation of tax-based vehicle finance leases". Id.

[39] Id.

[40] Editor's Introduction, supra note 26, at 7.

[41] Ann Dugan, "Finding a Way Through the Maze", Euromoney, Apr. 1990, at 97.

[42] UK Report, supra note 31, at 202. - Specific regulations to deal with securitization were first introduced by the Bank of England in February 1989. This document, "Notice on Loan Transfers and Securitisation" (the "Notice"), sets out the Bank's supervisory policy on the treatment of loan transfers involving banks and has become the backbone of all securitisation transactions done in the UK. The notice deals with the capital adequacy treatment of loan sales and securitisations, including methods of assignment and the status of off-balance sheet Special Purpose Vehicles ("SPVs").

[43] Id., at 208.

[44] Id.

[45] This is true because most mortgage securitisations leave the original lender responsible for remedying deficiencies when "the interest rate on the mortgage is not sufficient to pay the interest on the notes and other costs". Id., at 202.

[46] UK Report, supra note 31, at 202.

[47] Id.

[48] Harvey, supra note 30, at 27.

[49] Id.

[50] See "Securitisation Overhaul in the UK", International Financial Law Review, Jun. 1992, at 10; see also Ian R. Coles, "United Kingdom: Panel Session on Multi-Country Legal Issues" (Seminar Transcripts from Euromoney Conference in Brussels, June 4-5, 1992) at 135, 135; Clifford/Chance (eds.), Asset Securitization 1993, at 2, 3.

[51] Coles, supra note 50, at 135.

[52] Id.

[53] Id. In addition, legal assignment requires that the transfer be in writing and that the whole debt be transferred. Id.

[54] Id.

[55] Jason HP Kravitt, Ian R. Coles & C. Mark Nicolaides, "Coping with Cross-Border Securitization", International Financial Law Review, Nov. 1991, at 34, 35.

[56] Coles, supra note 50, at 135.

[57] Id. at 136.

[58] Id.

[59] Id.

[60] Id.

[61] Securitisation Overhaul in the UK, supra note 50, at 10; Clifford/Chance, supra note 50, at 5 f.

[62] Sec. Overhaul, supra note 50, at 10.
[63] Coles, supra note 50, at 136.
[64] Id. at 135.
[65] Id.
[66] Id.
[67] Id.
[68] "Country Report and Database: Netherlands", International Securitisation Report, Mar. 1993 (hereinafter "Neth. Report"), at 149, 149; Allard Metzelaar, "Netherlands: Panel Session on Multi-Country Legal Issues", Structured Finance: Design, Engineering & Production (Seminar Transcripts from Euromoney Conference in Brussels, June 4-5, 1992) at 147, 147.
[69] Neth. Report, supra note 68, at 149; see also Metzelaar, supra note 68, at 147; Victor de SeriŠre "Securitization in the Netherlands" (paper presented at the International Law Review Annual Forum 1991 in London, Sept. 10-13, 1991).
[70] There are, in principle, no technical reasons preventing securitization in the Netherlands. Neth. Report, supra note 68, at 149.
[71] See SeriŠre, supra note 69, at 3; Neth. Report, supra note 68, at 149.
[72] Id.
[73] Id.
[74] SeriŠre, supra note 69, at 3; see also Neth. Report, supra note 68, at 149.
[75] Metzelaar, supra note 68, at 147.
[76] Id.
[77] Id.
[78] Id.; see also Neth. Report, supra note 68, at 152.
[79] See Metzelaar, supra note 68, at 147 (discussing the possibilities of giving oral notice, or of using an advertisement in the newspaper as notice).
[80] Id. at 148.
[81] Id. Cf. also Wiek Slagter, "Securitisation of Property Assets", Juridisch up to Date Nr. 8, 1994, at 2, 3 who discusses the dangers connected with a structure in which the originator acts as collection agent on behalf of the SPV while remaining the holder of the legal title.
[82] See SeriŠre, supra note 69, at 6.
[83] For a more detailed discussion of these issues under Dutch Law, see id. at 22-26, 28-31.
[84] Id. at 27; see also Metzelaar, supra note 68, at 149.
[85] SeriŠre, supra note 69, at 27.
[86] Id. For a more detailed discussion of this process, see id. at 27-28.
[87] Id. at 5.
[88] For a further discussion of credit enhancement possibilities, see id. at 12.
[89] SeriŠre, supra note 69, at 8.
[90] Id.
[91] See id. If there is any concern, however, that in the context of a SPV bankruptcy the bank would be held liable for the debts of the SPV on the basis of the argument that the SPV was directed by bank officers, then the SPV will have to be managed by outsiders. Id. at 11.
[92] Id.
[93] SeriŠre, supra note 69, at 10; Slagter, supra note 81, at 4.
[94] SeriŠre, supra note 69, at 10. For comments regarding the implication of a bankruptcy of the SPV, see id at 12-14.
[95] See Metzelaar, supra note 68, at 149. It is conceivable, although unlikely, that a SPV could also be classified as a "near bank". For a discussion of this possibility and its ramifications, see SeriŠre, supra 69, at 14-15.
[96] SeriŠre, supra note 69, at 14-15.
[97] Id. at 16.
[98] Id.
[99] Id.
[100] Metzelaar, supra note 68, at 149. For a more detailed discussion of the Dutch Central Bank's treatment of "finance companies", see SeriŠre, supra note 69, at 16-18.

[101] Metzelaar, supra note 68, at 149.
[102] French Securitization: Past und Future, (Transcript of American Bar Association Congress in Paris, April 1-2, 1993) [hereinafter French Sec.], at 1.
[103] Id.
[104] Id. at 3.
[105] Id.
[106] "Country Report and Database: France", in: International Securitisation Report, March 1993 (hereinafter French Report), at 97, 102.
[107] Id. at 99; French Sec., supra note 102, at 3.
[108] French Sec., supra note 102, at 3.
[109] Id. As of June 1988, the average rate of equity of French banks ranged between 5 and 7 %. Id.
[110] Id.
[111] Id. at 4.
[112] See French Report, supra note 106, at 99.
[113] Id. at 102, 103.
[114] Michael D. Leemputte, "Securitisation Developments in France: Anticipated Legislative Changes, False Securitisations, Offshore Structures", in Structured Finance: Design, Engineering & Production (Seminar Transcript from Euromoney Conference in Brussels, June 4-5, 1992) at 120, 121; French Sec., supra note 102, at 1; French Report, supra note 106, at 97.
[115] French Report, supra note 106, at 97.
[116] Id.
[117] Id.; Leemputte, supra note 114, at 120.
[118] Leemputte, supra note 114, at 120.
[119] French Report, supra note 106, at 97.
[120] Id. at 97, 104; French Sec., supra note 102, at 9.
[121] See French Report, supra note 106, at 97.
[122] French Sec., supra note 102, at 10.
[123] Id.
[124] Id. at 9.
[125] Some commentators argue, for example, that this policy may lead to a concentration of risk in the securitising institutions, French Sec., supra note 102, at 9.
[126] Id.
[127] Id. at 11.
[128] Id. Thus a FCC can now acquire debts of more than one type, allowing a FCC to diversify its portfolio of receivables in order to decrease its overall risk. Id. at 11.
[129] Id. at 10.
[130] Id.
[131] French Sec., supra note 102, at 10.
[132] Id. at 16.
[133] Id. at 11. - Generally on the assignment of receivables under French law cf. Clifford/Chance, supra note 50, at 3 f.
[134] Leemputte, supra note 114, at 121; see also French Report, supra note 106, at 97; French Sec., supra note 102, at 11.
[135] French Sec., supra note 102, at 11.
[136] Id. at 12.
[137] Id.
[138] Id. at 17.
[139] French Sec., supra note 102, at 17.
[140] Id.
[141] Id.
[142] Id.
[143] See French Sec., supra note 102, at 17 (describing certain inadequacies in the draft trust law).
[144] See French Report, supra note 106, at 104.
[145] Cf. French Sec., supra note 102, at 7-8.

146 See id. at 7.
147 Id.
148 Id.
149 French Sec., supra note 102, at 7.
150 Id.
151 Id. at 7, 8.
152 Id. at 8.
153 French Sec., supra note 102, at 8.
154 Id.
155 Id.
156 See Andr, Van Landuyt, "The Belgian Law of August 5, 1992, on Special Purpose Vehicles: The Cornerstone of the Evolving Belgian Securitization Law", in: American Bar Association (ed.), The Evolving Worldwide Legal and Regulatory Climate for Securitization, Brussels, 1993, at 6-1.
157 Belgium Report, in: ISR International Securitisation Report, London 1992, at 57. - An alternative transfer method - "subrogation" - is discussed in Clifford/Chance, supra note 50, at 5.
158 Van Landuyt, supra note 156, at 6-3.
159 For the detail see Van Landuyt, supra note 156, at 6-3.
160 See Helena Morissey (ed.), ISR International Securitisation Report, London 1993, at 109.
161 Theodor Baums, "Asset-Backed Finanzierungen im deutschen Wirtschaftsrecht", Wertpapier-Mitteilungen (Zeitschrift f•r Wirtschafts- und Bankrecht), 1993, at 1 ff.
162 Reinhard Preusche, Iris Smolka, Christof von Dryander, "Securitisation in Germany", in: Helena Morissey (ed.), International Securitisation, London 1992, at 405, 406.
163 For a detailed discussion of the "competion of rules" and legal harmonization in the EU see Richard M. Buxbaum and Klaus J. Hopt, "Legal Harmonization and the Business Enterprise", Berlin/New York 1988; most recently Roberta Romano, "The Genius of American Corporate Law", Washington 1993, at 128 ff.