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Securitisation in Portugal: an introduction to the legal framework

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AS A DYNAMIC EUROPEAN FINANCIAL HUB, PORTUGAL HAS CRAFTED A BESPOKE REGULATORY ENVIRONMENT THAT CATERS TO INVESTORS' NEEDS AND SAFEGUARDS THEIR INTERESTS. IN THIS ARTICLE, WE DELVE INTO THE PILLARS OF PORTUGAL'S SECURITISATION FRAMEWORK, HIGHLIGHTING ITS REMARKABLE FEATURES SUCH AS BANKRUPTCY REMOTENESS FOR ISSUERS, STRINGENT INSOLVENCY LIMITATIONS, AND THE NOTICEABLE DIVERSITY OF ASSET CLASSES SECURITISED THUS FAR.

Introduction and applicable legal framework

Securitisation saw its first developments in the United States at the beginning of the 1980s and have already been the subject of legislative treatment in most of the member states of the European Union. Its use has been quite successful, and it has quickly become an important factor in the competitiveness of global and modern economies. Our country is no exception to this trend and the first securitisation carried out in Portugal dates back to 1997. At the time no specific regime was applicable to securitisation in Portugal and such transactions were structured by finance lawyers and market players under the general rules set out in the Portuguese Civil Code and the Portuguese Commercial Companies Code.

Since then, the financial and social usefulness of this tool has been increasingly recognised and its complexity has grown, presenting new challenges and risks for those involved, which the general legislation was not prepared to respond to. This led the Portuguese legislator to enact Decree-Law No. 453/99 of November 5, 1999, which was amended several times and most recently on September 23, 2019 (the “**Securitisation Law**”). The concept of

securitisation was thus formally introduced into the Portuguese legal system in 1999, providing economic agents in general, and the financial system in particular, with an important financial tool that is widespread - and frequently used - in other developed economies.



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As cornerstones regulated under the Securitisation Law we would highlight the following matters:

- (a) incorporation of securitisation vehicles;
- (b) receivables eligibility criteria for securitisation purposes;
- (c) licensing, authorisation and assignment requirements;
- (d) notification of borrowers;
- (e) servicing of the assigned assets; and
- (f) segregation of assets and bankruptcy-remoteness.

Finally, we would also highlight that European regulations are also directly applicable in Portugal, leading to the potential need for Portuguese securitisations to additionally comply with Regulation (EU) 2017/2402, laying down a general framework for securitisation and creating a specific framework for simple, transparent and standardised securitisation (the “**Securitisation Regulation**”) and Regulation (EU) 2017/1129 on the prospectus to be published when securities are offered to the public or admitted to trading on a regulated market.

If a transaction meets the definition of securitisation provided under the Securitisation Regulation, certain parties to that transaction will or may have additional regulatory obligations, such as (a) due-diligence requirements for institutional investors, (b) risk retention and (c) transparency requirements for originators, sponsors and securitisation special purpose entities.

It should be noted however that not all Portuguese securitisations fall under the definition of securitisation provided under the Securitisation Regulation.

Securitisation structures in Portugal: the STC

Securitisations under the Securitisation Law may be structured in two different ways, depending on the type of securitisation vehicle to be used.

The transaction may be either structured through a securitisation fund (also known as an FTC) or through a securitisation company (also known as an STC) and only these entities are eligible assignees for the purposes of the Securitisation Law. The incorporation of both these

vehicles is subject to prior approval from the Portuguese Securities Market Commission (the “**CMVM**”) which also carries out their ongoing supervision.

Given the complexity of fund structure and the alternative offered by the STC, the use of FTCs in Portugal is currently quite low when compared to that of STCs. For this reason, we’ll focus on the use of STCs.

STCs are public limited liability companies whose exclusive corporate purpose is to carry out credit or risk securitisation transactions, through their acquisition and the issuance of securitisation notes (debt instruments) for payment of the credits or risks acquired. STCs are multi-securitisation SPVs, operating on a silo-by-silo basis. Each securitisation transaction corresponds to a separate silo, without cross-contamination across silos. When entering into a transaction, the STC will acquire a receivables portfolio and fund it through the issuance of securitisation notes, normally (but not necessarily) tranching in two or more classes. This receivables portfolio will be used to pay the liabilities under the issued securitisation notes, with the notes being repaid by means of cash flows generated by the underlying receivables portfolio.

STCs: bankruptcy remoteness and legal creditor’s privilege

The Securitisation Law provides for several rules that ensure that securitisation transactions structured through an STC benefit from bankruptcy remoteness of the STC and that the proceeds arising from collection of the receivables are exclusively allocated to repayment of transaction creditors and investors. The transaction creditors (including the investors) will have the benefit of the statutory segregation provided for under the Securitisation Law which provides that the assets and liabilities of the STC in respect of each issuance of securitisation notes by it are completely segregated from the other assets and liabilities of the STC. Conversely, the rights of the investors and of any service providers existing specifically in the context of the issuance of the notes, are of limited recourse to the assets collateralising the issuance of such notes, i.e., collections and transaction accounts.

Accordingly, repayment of principal, payment of interest or other amounts in respect of the notes issued by an STC, as well as any fees and expenses owed to the relevant services providers existing specifically in the context of the issuance of such notes, are collateralised by the transaction assets existing at a given moment (e.g., collections and transaction accounts) and forming part of the separate estate connected with the issuance such notes.

The right of recourse of such transaction creditors is therefore limited to the specific transaction assets, which constitute an autonomous and ring-fenced pool of assets, exclusively allocated to the issuance of the notes and which is not, therefore, available to creditors of the STC other than the investors and other services providers. Accordingly, the transaction assets of a given securitisation cannot be used to satisfy any other debts that the STC has or may have in the future in relation to other series of notes or other obligations. This is what is known in Portugal as the “segregation principle”.

In addition to the above, and in order to render this segregation principle effective, the investors and the other transaction creditors are further entitled to a legal creditor’s privilege (equivalent to a security interest) over all of the transaction assets, including those assets outside of Portugal, such as is usually the case for some transaction accounts. Therefore, the rights of the investors and other transaction creditors, regarding the repayment of principal and interest and other amounts that may be due, will, in respect of the transaction assets, rank senior to the rights of any other third-party creditor of the STC.

Given the limited corporate purpose of the STC, besides shareholders and directors, if remunerated, the only creditors of the STC will be the general providers of corporate and other services required for the carrying out of the STC’s activity (which are always limited in type and number), the tax authorities for amounts due in respect of taxes, the investors and creditors of each issue of securitisation notes benefiting from the statutory privilege.

Insolvency limitations

In the event of an insolvency of an assignor or a servicer, the Securitisation Law also contains key provisions which aim to protect the investors’ position as set out below.

On one hand, no assignment of credits for securitisation purposes under the Securitisation Law may be challenged for the benefit of the assignor’s bankruptcy estate, unless an assignment is concluded in bad faith.

On the other hand, all collections held or received by the servicer will not form a part of the servicer’s bankruptcy estate.

Common asset classes in Portugal and underlying benefits of their securitisation

Due to the tailor made and investor-friendly regime referred to above, Portugal’s securitisation markets have experienced a dynamic transformation over the past decade, with securitisation emerging as a pivotal instrument in driving economic growth and financial stability. We’ve been advising on a diverse range of assets being securitised by different originators. These diverse asset classes, including non-performing loans, mortgage-backed loans, tax and social security credits, regulatory credits from the electricity sector’s tariff-deficit, highway toll receivables, future receivables, TV broadcasting rights, advertising rights, and sponsorship rights receivables, play a crucial role in the Portuguese financial landscape. Below we list some benefits of these transactions, considering typical asset classes securitised in Portugal:

- (g) **Non-Performing Loans (NPLs):** the securitisation of NPLs has been instrumental in cleaning Portuguese banks’ balance sheets, enabling them to allocate resources more efficiently and allocate capital to new lending opportunities. This process has played a crucial role in revitalising the Portuguese banking sector’s health.

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- (h) **Mortgage-Backed Loans:** securitising mortgage-backed loans has provided Portuguese financial institutions with a means to diversify their portfolios and increase the availability of mortgage financing, stimulating the real estate market and homeownership, which is currently under threat in Portugal.
 - (i) **Tax and Social Security Credits:** the securitisation of tax and social security credits offers a reliable source of funding for the Portuguese government while providing investors with a stable and low-risk asset class.
 - (j) **Regulatory Credits from Tariff-Deficit in the Electricity Sector:** the electricity sector's regulatory credits are unique to Portugal's market, one of the largest companies in Portugal being the most relevant originator in this respect. Securitising these credits has helped distribute the regulatory burden more evenly among market participants, promoting sustainability and stability in the sector.
 - (k) **Highway Toll Receivables:** Securitising highway toll receivables has facilitated infrastructure development in Portugal while offering investors a predictable income stream.
 - (l) **Future Receivables:** Future receivables, such as those arising from long-term contracts or subscription-based services, can be securitised to unlock immediate capital and finance expansion projects.
 - (m) **TV Broadcasting Rights Receivables:** The securitisation of TV broadcasting rights provides broadcasters with upfront capital, which can be invested in content production and technological advancements.

- (n) **Advertising Rights and Sponsorship Rights Receivables:** some of the most famous media companies and sports organisations in Portugal have been monetising future advertising and sponsorship agreements by securitising these receivables, enhancing their financial flexibility.

Finally, as the sustainable finance trend progresses swiftly, sustainable securitisation is expected to become a trend in Portugal, noting that the first Iberian green RMBS was originated and issued out of Portugal in 2020.

Conclusion

In conclusion, Portugal's securitisation regime stands as a shining example of a tailored and investor-friendly framework. With a well-tested track record in the market, Portuguese legislation offers invaluable benefits such as the robust bankruptcy remoteness of the issuer and stringent insolvency limitations. Furthermore, Portugal's versatility shines through as it has successfully securitised a diverse array of asset classes. This adaptability, coupled with its protective measures, cements Portugal's position as a prime destination for securitisation, providing both security and opportunities for investors.

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