



GUIDANCE NOTE FOR BOARD MEMBERS

SECURITISATION OF RECEIVABLES

WORKING GROUP | BEST PRACTICE
MANAGEMENT & CORPORATE GOVERNANCE

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INTRODUCTION – SECURITISATION OF RECEIVABLES

Pools of receivables are one of the most common types of underlying assets in securitisation transactions. It shall be noted that the value of these assets is determined by the quality of the cash flows they generate, hence appropriate monitoring of the portfolio is required. Among the different categories of receivables, we usually find the following:

- Mortgage receivables.
- Auto/aviation loans/leases.
- Consumer loans and credit cards.
- Trade receivables and factoring.

Regardless of the category, the set-up and structure of receivables securitisation transactions generally follow a common scheme.

On the asset side, the initial purchase of the receivables portfolio at transaction closing is usually followed by a revolving period during which the Seller/**Originator** is entitled to offer to the Financial Vehicle Corporation (“**FVC**”) additional receivables complying with the eligibility criteria as defined in the transaction documents. The frequency will depend on the types of receivables, i.e., credit card receivables will have a short-term revolving period of a month, whilst mortgage receivables are typically long-term contracts. The FVC can then accept to purchase such additional assets to replenish its portfolio. It is typically the responsibility of the **Portfolio Manager** to ensure eligibility of the underlying assets, however the Board of the FVC remains ultimately responsible.

The purchase price for the additional receivables is sometimes paid by the FVC using part of the collections received from the receivables previously acquired or by issuing new notes. In most cases, during the revolving period, the FVC is due to pay only the interests on the notes issued without any principal redemption, leaving in this way enough cash on its account to pay the additional receivables purchase price. The revolving period usually lasts for two or three years after the closing date and is subject to the possible extension, but also early termination under certain conditions. This mechanism is useful especially when the maturity of the underlying receivables is particularly short, as it allows to extend the life of the notes and the whole transaction reducing the impact of the fixed costs on the structure and maximizing the benefits for all the parties involved. At the end of the revolving period, the transaction enters into the amortization phase.

In case of mortgages or auto/aviation loans/leases, the receivables are usually

collateralized by the relevant real estate property, vehicle or airplane. With regards to the notes then, these are often split into two or more tranches each characterized by a different risk/return level. For example, the senior tranche usually carries a predefined interest rate and are further up in order of payments in the waterfall. Subordinated or junior notes on the other hand are first to take losses and also take the residual amounts left after the other waterfall payments. Since the mechanics involve tranching, these structures then typically fall under the EU **Securitisation Regulation** and hence the Originator/Seller of the receivable's portfolio is required to retain a minimum interest of 5% in the transaction, thus is usually the Originator, subscribing the junior tranche or part of it.

In case the notes are admitted for trading on a stock exchange, it is very important to be aware of the issuer's, i.e., the FVC's, on-going obligations set by the relevant exchange. These may vary significantly depending whether the notes are listed on a regulated or unregulated market and in terms of, in particular, publication of financial reports under the transparency law. For example, under the Luxembourg transparency law, issuers who have only debt securities traded on a regulated market and where such debt securities have a denomination of at least EUR 100,000. - (or equivalent in other currency) are exempted from certain requirements with regard to annual and half-yearly financial reporting.

For risk management purposes, the FVC may enter into a swap agreement to hedge certain positions in terms of currency and interest exposure as well as cash flows.

Terms and abbreviations used in this publication are defined in the Glossary at the end of the document.

MAIN PARTIES INVOLVED IN THE SECURITISATION OF RECEIVABLES

With regards to the key parties and their responsibilities in receivables securitisation, the most important are mentioned here below:

ARRANGER

The Arranger is involved, among other things, in setting up the transaction, selection of the pool of assets, defining the terms of the securities to be issued and overall preparation of the structure.

The Arranger is a party to the main transaction documents, including subscription agreements and the FVC has several understandings, representations, and warranties to give to the Arranger.

The Arranger may perform a variety of other functions in the securitisation transaction combination of which may depend on a transaction setup.

CALCULATION AGENT

The Calculation Agent is responsible for calculating and reporting on the distribution of interest, principal repayments, profit participation (if applicable) due to Noteholders.

CASH MANAGER

The Cash Manager acts as agent of the FVC in administrating the transaction account and the funding account in accordance with the applicable terms and conditions. To this extent, the Cash Manager is responsible of making all the administrative arrangements required to facilitate payments or performance as described in the transaction documents.

CLEARING AGENT

The Clearing Agent is usually a financial institution that is interposed between the FVC and the Noteholders. It accepts securities as eligible for settlement and is also responsible to properly service those securities. Having a clearing agent reduces the risk associated with failure to deliver the securities on the settlement date.

DATA TRUSTEE

The Data Trustee is primarily concerned with preserving the rights of debtors and ensuring General Data Protection Regulation (“**GDPR**”) requirements are met and non-public personal information is held independently and securely, thus providing comfort to all parties involved in the transaction.

The Data Trustee is an entity holding the portfolio decryption key allowing for the decryption of personal data which are encrypted and which are necessary for the identification of the names and addresses of the underlying debtors of the receivables.

The Data Trustee has the responsibility:

- (i) to keep the portfolio decryption key on behalf of the Seller and the Purchaser in safe custody.
- (ii) to ensure that the portfolio decryption key is protected in compliance with the secrecy rules.
- (iii) to keep the portfolio decryption key confidential and not to disclose it to anyone except as per the specific conditions/occurrences as stipulated in the data trustee agreement.

To comply with the GDPR, very often it is the Originator or Seller who provides portfolio information (also including encrypted portfolio information in a secured file which is readable only together with the portfolio decryption key) to the Purchaser. The corresponding portfolio decryption key is provided to the Data Trustee by the Seller for the identification of the names and addresses of the respective underlying debtors, and names of guarantors and collateral providers (if any) in accordance with a data trust agreement.

INSURER

Insurer means any credit insurer having a required rating and satisfactory to the Purchaser, consented by the relevant majority of the Noteholders.

The FVC usually enters into a credit insurance policy with the Insurer in order to cover the credit risk relating to the portfolio of the assigned receivables.

The credit insurance policy is most commonly present for a portfolio of trade receivables. The features of the credit insurance policy can be tailored/negotiated with the Insurer to the extent of coverage (usually a percentage, but it can also be a

total maximum absolute monetary limit), eligibility criteria, deductible, threshold loss or a minimum amount, etc.

LISTING AGENT

In case when FVC intends to list its notes, it may appoint a Listing Agent to act as an intermediary between the stock exchange and the FVC, Arranger and/or legal advisor. The role of the Listing Agent is to ensure all required listing documentation is approved by the stock exchange and the listing process is successfully completed. Majority of the stock exchanges have a list of approved listing partners that can assist in this process.

PAYING AGENT

The Paying Agent is usually a credit institution, responsible for the payments of interest and principal to the Noteholders, as authorised and instructed by the FVC, based on a paying agency agreement.

Among the main duties mentioned above, the Paying Agent shall maintain records of all documents received in connection with its duties and shall make such records available for inspection at all reasonable times by the Issuer, the Administrator, the **Calculation Agent**, the **Security Trustee** and the other Agents.

PORTFOLIO MANAGER

Applicable in case of active portfolio management, the Portfolio Manager is responsible for the due diligence assessment on the Originator, the transaction and risks related to the underlying assets, ongoing monitoring of the performance of the assets, regular stress testing on cash flows and collateral, and whenever appropriate executing the portfolio adjustments.

SECURITY TRUSTEE

The Security Trustee is an entity who acts autonomously and independently from the other counterparties involved in the transaction, as it is the entity appointed to protect the rights of the Noteholders, as well as of the other secured parties, as set out in the transaction documents. Whilst not mandatory under the Luxembourg securitisation law, this role is quite common in receivables transactions.

The approval from the Security Trustee is generally required for all major amendments and waivers that may occur or be required during the life of a securitisation transaction. The Security Trustee may also be called to intervene at the occurrence of specific trigger events, such as for example events of default, in order to safeguard the assets and mitigate the impact of any negative event to the transaction.

For these reasons it is always important at FVC level to make sure that the Security Trustee is informed about any event, or possible event, that may affect the performance of the assets or the notes. Details about if and by which deadline the Security Trustee should be informed about events occurring at FVC level are generally provided within the transaction documents.

Often the FVC is required to periodically provide a non-default (or compliance) certificate to the Security Trustee attesting that, until that moment, no default has occurred, and the issuer has complied with all its obligations as set-out in the transaction documents. It is good practice to circulate a 'due diligence email' to all transaction parties in advance of the date at which the non-default certificate is due to give the possibility to all parties to inform the issuer in case they are aware of any event that would render the statements given in the certificate incorrect.

SERVICER / BACK-UP SERVICER

The Servicer is appointed by the FVC to manage the portfolio of receivables on its behalf. This role is fundamental within the transaction, the Servicer duties mainly consist in:

- Monitoring of the receivables portfolio performance and ensuring timely payments from the borrowers.
- If necessary, liaising with the borrowers in respect of prepayments or late payments and taking necessary actions always in the best interest of the FVC.
- Preparation of reports on the performance of the portfolio including all the information as specified in the transaction documentation. These reports are typically prepared on a monthly basis.

Given the context in which the Servicer has to perform its duties, it is often the Originator or the Seller of the receivables who takes over this role. This entity has in fact a privileged position when it comes to liaising with the borrowers and negotiating any terms of the receivables since it is the same counterparty with which the borrowers have interfaced from the beginning.

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The centrality of the Servicer role in this kind of transactions is testified by the fact that, among the transaction parties, often a Back-up Servicer will be appointed, i.e., an entity ready to take over the same duties of the original Servicer should the latter be no longer able to perform this function. Alternatively, a Back-up Servicer Facilitator may be appointed: the role of this entity is to quickly find a new Servicer to replace the original Servicer, if needed. It is important for the Back-up Servicer Facilitator to be well positioned and have good knowledge of the market to find suitable replacements.

The appointment of a Back-up Servicer or a Back-up Servicer Facilitator provides additional comfort to all parties, but especially to the Noteholders, about the continuity of monitoring of the assets and therefore better performance of the portfolio.

COMMON REPORTING IN RECEIVABLES SECURITISATIONS

The frequency with which reports must be prepared is generally aligned with the frequency of the interest payment dates (“**IPD**”) scheduled for the notes. Main types of report are:

SERVICER REPORT

This report is prepared by the **Servicer** and serves as starting point for the calculations and preparation of the other reports related to a specific IPD. In fact, it includes information about the performance of the pool of receivables during the period since the previous IPD (collection period), in detail:

- Portfolio overview and main characteristics of the receivables.
- New receivables included in the pool (during the revolving period).
- Payments of principal and interest received.
- Information about the overall and historical performance (unpaid interests, delinquencies).
- Compliance with predefined criteria (e.g., delinquency ratio, default ratio, concentration limits).
- Repurchased receivables (the seller may be obliged to repurchase non-compliant receivables).
- Details loan by loan (including balances, delayed payments, interest rates, currencies, countries, industry, maturity, etc.).
- Confirmation of filing and copy of the **ESMA** reports filed by the Servicer.
- Data to compile statistical reporting to Central Banks.

Some of the ratios included in the Servicer report may trigger changes affecting the continuation of the transaction, for example a poor performance may trigger an early amortization, meaning that the revolving period is stopped before the date originally set and the redemption of the notes must start immediately.

The event of default does not have a static definition, this is usually defined in the transaction documents, and it may be different from one FVC to another, or from one transaction to another.

Most commonly met default definitions cover the inability of the debtors to perform regular payments of principal and/or interest. To assess objectively the inability to repay the receivable, certain thresholds are used, like the number of overdue days (most common threshold is 90 overdue days).

The Board of the FVC has to monitor the reporting and performance of the portfolio. In the event of default, the Board needs to ensure that appropriate steps are taken, which typically would be defined in the transaction documents.

The servicer report is often distributed by the Trustee to the Noteholders.

CASH MANAGER REPORT

The Cash Manager report means a report prepared by the **Cash Manager** in accordance with the Cash Management Agreement in the form agreed between the Cash Manager, the Issuer (FVC), the Seller, the Facility Agent (acting on the instructions of the instructing party), the Noteholders, the **Calculation Agent** and the Hedge Counterparty prior to the funding date and such other form as may, from time to time, be agreed between these parties.

INVESTORS/NOTEHOLDERS REPORT

This report is prepared by the **Paying Agent**, has wide distribution in the format of PDF and usually includes data about:

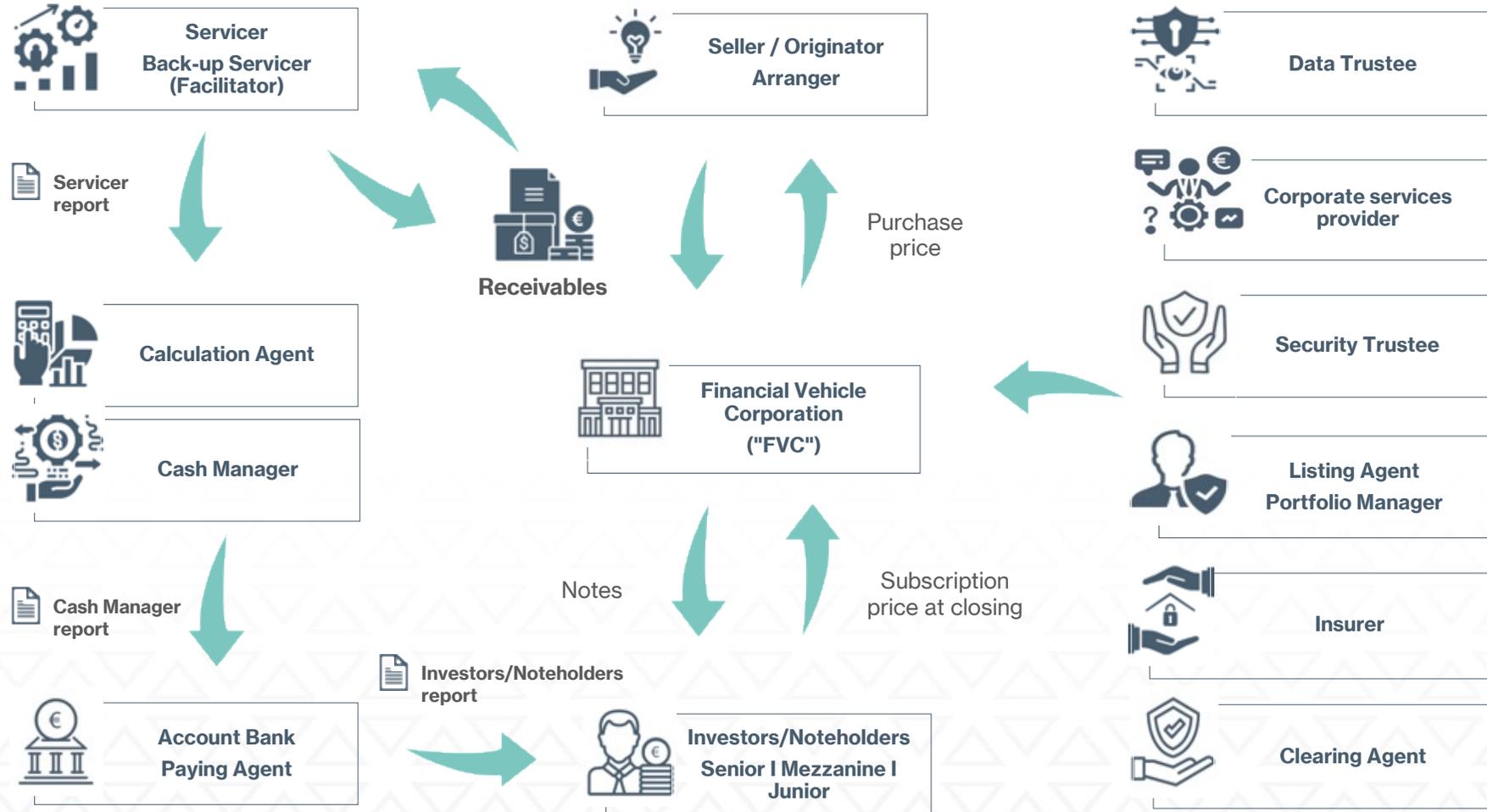
- Underlying portfolio.
- Details about relevant transaction parties and related rating.
- Bank accounts – available funds.
- Information about cash reserve and other credit enhancement measures.
- Principal amounts outstanding and interests payable for each note tranche.
- Information about the swap.
- IPD calculation – waterfall of payments.

In certain transactions also a payment report is prepared, basically including details about all payments to be made by the issuer at the relevant IPD.

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TYPICAL RECEIVABLES STRUCTURE ILLUSTRATION



GLOSSARY AND ABBREVIATIONS

<p>A</p>	<p>Arranger</p>	<p>means the party involved among other things in setting up the Securitisation transaction, the selection of the pool of assets, defining the terms of the securities to be issued and overall, the preparation of the structure. Full definition and roles can be found in the dedicated section in this publication.</p>
	<p>C</p>	<p>Calculation Agent</p>
<p>Cash Manager</p>		<p>means the party acting as agent of the FVC in administrating the transaction account and the funding account in accordance with the applicable terms and conditions. To this extent, the Cash Manager is responsible of making all the administrative arrangements required to facilitate payments or performance as described in the transaction documents. Full definition and roles can be found in the dedicated section in this publication.</p>
<p>Clearing Agent</p>		<p>means a party, usually a financial institution, that is interposed between the FVC and the Noteholders. It accepts securities as eligible for settlement and is also responsible to properly service those securities. Full definition and roles can be found in the dedicated section in this publication.</p>
<p>D</p>	<p>Data Trustee</p>	<p>means an entity holding the portfolio decryption key allowing for the decryption of personal data which are encrypted and which are necessary for the identification of the names and addresses of the underlying debtors of the receivables. Full definition and roles can be found in the dedicated section in this publication.</p>

E	<p>ESMA means the European Securities and Markets Authority.</p>
F	<p>FVC means the Financial Vehicle Corporation as per ECB definition laid down in Regulation ECB/2013/40.</p>
G	<p>GDPR means General Data Protection Regulation, the European Union’s new legal framework which governs the collection and processing of users’ personal data. The GDPR applies to all entities based in an EU country that process personal data, as well as all entities worldwide that process personal data belonging to EU residents.</p>
I	<p>Insurer means any credit insurer having a required rating and satisfactory to the Purchaser, consented by the relevant majority of the Noteholders. Full definition and roles can be found in the dedicated section in this publication.</p>
	<p>IPD means Interest Payment Dates. Dates on which lenders receive interest payment on the debt instrument they hold. Interest payment dates are usually set at the outset and usually correlate closely to rental quarter dates.</p>
L	<p>Listing Agent means an intermediary between the stock exchange and FVC, Arranger and/or legal advisor. The role of the Listing Agent is to ensure all required listing documentation approved by the stock exchange and the listing process successfully completed. Majority of the stock exchanges have a list of approved listing partners that can assist in this process. Full definition and roles can be found in the dedicated section in this publication.</p>

	LuxCMA	means the Luxembourg Capital Markets Association.
O	Originator	means the party assigning assets to the FVC/SSPE in a securitisation transaction.
P	Paying Agent	means a party, usually a credit institution, responsible for the payments of interest and principal to the Noteholders, as authorised and instructed by the FVC, based on a paying agency agreement. Full definition and roles can be found in the dedicated section in this publication.
	Portfolio Manager	means the party responsible for the due diligence assessment on the Originator, the transaction and risks related to the underlying assets, ongoing monitoring of the performance of the assets, regular stress testing on cash flows and collateral, and whenever appropriate executing the portfolio adjustments. Full definition and roles can be found in the dedicated section in this publication.
	Publication	means this document as well as the information contained herein.
S	Securitisation Regulation	means Regulation (EU) 2017/2402 of the European Parliament and of the Council of 12 December 2017 laying down a general framework for securitisation and creating a specific framework for simple, transparent and standardised securitisation.
	Security Trustee	means an entity who acts autonomously and independently from the other counterparties involved in the transaction, as it is the entity appointed to protect the rights of the Noteholders, as well as of the other secured parties, as set out in the transaction documents. Whilst not mandatory under the Luxembourg securitisation law, this role is quite

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	<p>common in receivables transactions. Full definition and roles can be found in the dedicated section in this publication.</p>
	<p>Servicer</p> <p>means a party appointed by the FVC to manage the portfolio of receivables on its behalf. Full definition and roles can be found in the dedicated section in this publication.</p>



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Working Group – Best Practice

The aim of this working group is to find practical solutions (or answers) to practical problems. Capital market participants are often confronted with varying practices among the numerous practitioners active in Luxembourg, including when it comes to compliance, accounting, presentation of the financial statements, clearing, reporting, or general legal questions, and the purpose of the group will be to identify any recurring problems or inconsistencies in such practices and to analyse whether it is possible to work out practical recommendations and good market standards which address such issues.

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