

GUIDANCE NOTE FOR BOARD MEMBERS

DIRECT LENDING WITH SECURITISATION VEHICLE AS ORIGINATOR

WORKING GROUP | BEST PRACTICE
MANAGEMENT & CORPORATE GOVERNANCE

NOVEMBER 2023

TABLE OF CONTENTS

INTRODUCTION - DIRECT LENDING WITH SV AS ORIGINATOR	3
MAIN PARTIES INVOLVED IN A DIRECT LENDING STRUCTURE	4
INVESTMENT MANAGER/INVESTMENT ADVISOR	4
PORTFOLIO MANAGER	5
COMMON REPORTING IN DIRECT LENDING	6
LENDING PROCESS	7
TYPICAL DIRECT LENDING STRUCTURE ILLUSTRATION	8
GLOSSARY AND ABBREVIATIONS	9

INTRODUCTION – DIRECT LENDING WITH SV AS ORIGINATOR

Direct lending is a type of financing in which borrowers obtain loans directly from investors or lenders without the involvement of a traditional financial institution like a bank. In such arrangement, the Securitisation Vehicule (“**SV**”)¹ originates and provides loans to borrowers according to eligibility criteria set forth in the documentation of the financial instruments issued by such SV.² It shall be noted that Luxembourg law permits the SV to originate loans without a dedicated license.

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

¹ Ed.: As a general comment, the term Financial Vehicle Corporation (“FVC”) used in other LuxCMA publications is defined by the **ECB** as engaging in “securitisation”, where securitisation is defined as “a transaction or scheme whereby an entity that is separate from the originator [...] and is created for or serves the purpose of the transaction or scheme issues financing instruments to investors, and one or more of the following takes place: an asset or pool of assets, or part thereof, is transferred to an entity that is separate from the originator and is created for or serves the purpose of the transaction or scheme [...]”. It therefore implies that there is a transfer of assets from the originator to the securitisation entity for the entity to qualify as “securitisation” under the [Regulation \(EC\) N° 24/2009](#) of the ECB and for the SV to qualify as a FVC, which is not the case in direct lending where the originator is the same entity as the SV. Therefore, for consistency, we will refer to the securitisation vehicle (“SV”) throughout this paper.

² Please note this paper does not cover lending to retail customers.

MAIN PARTIES INVOLVED IN A DIRECT LENDING STRUCTURE

The key elements and parties remain the same as in other forms of securitisation³ except for some deviation in terms of risk management and borrowers' approval process.

As a result, the following additional parties are involved in a Direct Lending structure:

INVESTMENT MANAGER/INVESTMENT ADVISOR

An Investment Manager identifies and presents to the **Management Board** of the SV a strategy and investment framework for a loan portfolio.

The Investment Manager may appoint an Investment Advisor to act on an exclusive basis as specialised and dedicated intermediary responsible for advising, processing and monitoring of the loan, and as a portfolio advisor for the portfolio managed by the entity. An Investment Advisor follows a defined strategy, identifies and presents each loan separately to the Management Board of the SV for approval.

The activities of the afore-mentioned parties can be broadly described as application processing, pre-selection, credit analysis, approval and documentation, monitoring and portfolio management.

Below is a non-exhaustive list of typical activities in direct lending transactions:

- Ensuring that the loan(s) to be granted comply with the eligibility criteria set forth in the issuing documentation of the financial instruments of the SV;
- Advise the SV concerning all actions related to granting the loans to borrowers from time to time in accordance with the eligibility criteria (as per documentation);
- Perform credit quality analysis of borrowers at inception and periodically update the Management Board of the SV on each borrower credit quality;
- Perform AML/KYC due diligence on borrowers;
- Process loan applications based on defined credit framework and presentation to the Management Board of the SV /investment committee for approval;

³ Please refer to the LuxCMA [Guidance Note for Board Members I Securitisation of Receivables](#) released in April 2023 and available on the LuxCMA website.

- Provide input on loan pricing including credit limit, interests rate and other covenants to be included in a credit agreement;
- Review and register any collateral and perform certain credit services, including the collection of documentation regarding collateral securing the loans, as the case may be;
- Disclose any relationships the Investment Manager or Investment Advisor (as well as their affiliates) may have with the existing/potential borrower(s);
- Provide advice and supporting services to the SV on matters related to the portfolio including loan default situations and restructurings;
- Perform individual borrower credit monitoring;
- Provide input for borrower valuation at reporting date;
- Communication with borrower in case of delays in payments/restructuring, etc.;
- Taking enforcement actions on collateral;
- Depending on scope of work, the Investment Manager may provide support to collection/recovery agents.

The Investment Manager may also at times avail of services of risk manager, should such party be appointed. The Risk Manager would present an overview of the applicable risks to the Management Board of the SV.

PORTFOLIO MANAGER

The role of the **Portfolio Manager** is not materially different than other transactions discussed in these guidelines (e.g., receivable transactions) hence it is not expanded any further in this document. Portfolio Manager may also be referred to as asset servicer or collateral administrator.

COMMON REPORTING IN DIRECT LENDING

The below is a non-exhaustive list of examples of commonly observed reporting in direct lending structures. In practice these reports are often amalgamated.

SERVICER REPORT

This report is prepared by the **Servicer**, on a monthly basis, to provide detailed overview of each loan and borrower details, cash collection, risk ratings, industry concentration, comparison with covenants (traffic lights system), defaults, restructuring of the debt etc.⁴

INVESTMENT MANAGER REPORT

The Investment Manager Report includes a qualitative analysis of each borrower accompanied by the above-mentioned Servicer Report to keep the Management Board of the SV abreast of situations surrounding each borrower and to anticipate any conditions that may arise/require actions. These reports may include the following data/information:

- A file on each borrower containing a review of financial statements and other reports submitted by the borrower to the Investment Manager as per their original agreement;
- Any out of cycle reports requested by investment manager from borrowers, statistical data, new orders/sales projections;
- An overview of business plans submitted by the borrower at inception in addition to their actual accounts/financial reports, and
- Any conclusions/recommendations from the Investment Manager to the Management Board of the SV.

CASH MANAGER REPORT

This report is prepared by the **Cash Manager**, on a monthly basis and in accordance with the Cash Management Agreement, in the form agreed between the Cash Manager, the Issuer (SV), the Seller, the Facility Agent (acting

⁴ For a detailed overview of the Servicer Report, please refer to the LuxCMA [Guidance Note for Board Members I Securitisation of Receivables](#) published in April 2023 and available on the LuxCMA website.

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.

LENDING PROCESS

The credit lines transactions must be in line with a risk policy based on the criteria of prudence and must comply with the eligibility criteria of the loans to be granted by the SV. These transactions may consider, on an individual basis, both personal and financial situation of the borrower(s) and its (their) objectives.

The granting of lending transactions will typically be based on the repayment capacity of the borrower taking into consideration his capacity to fulfill all his (accepted) financial obligations and his income originating from business activity or profession, that are considered as regular income source.

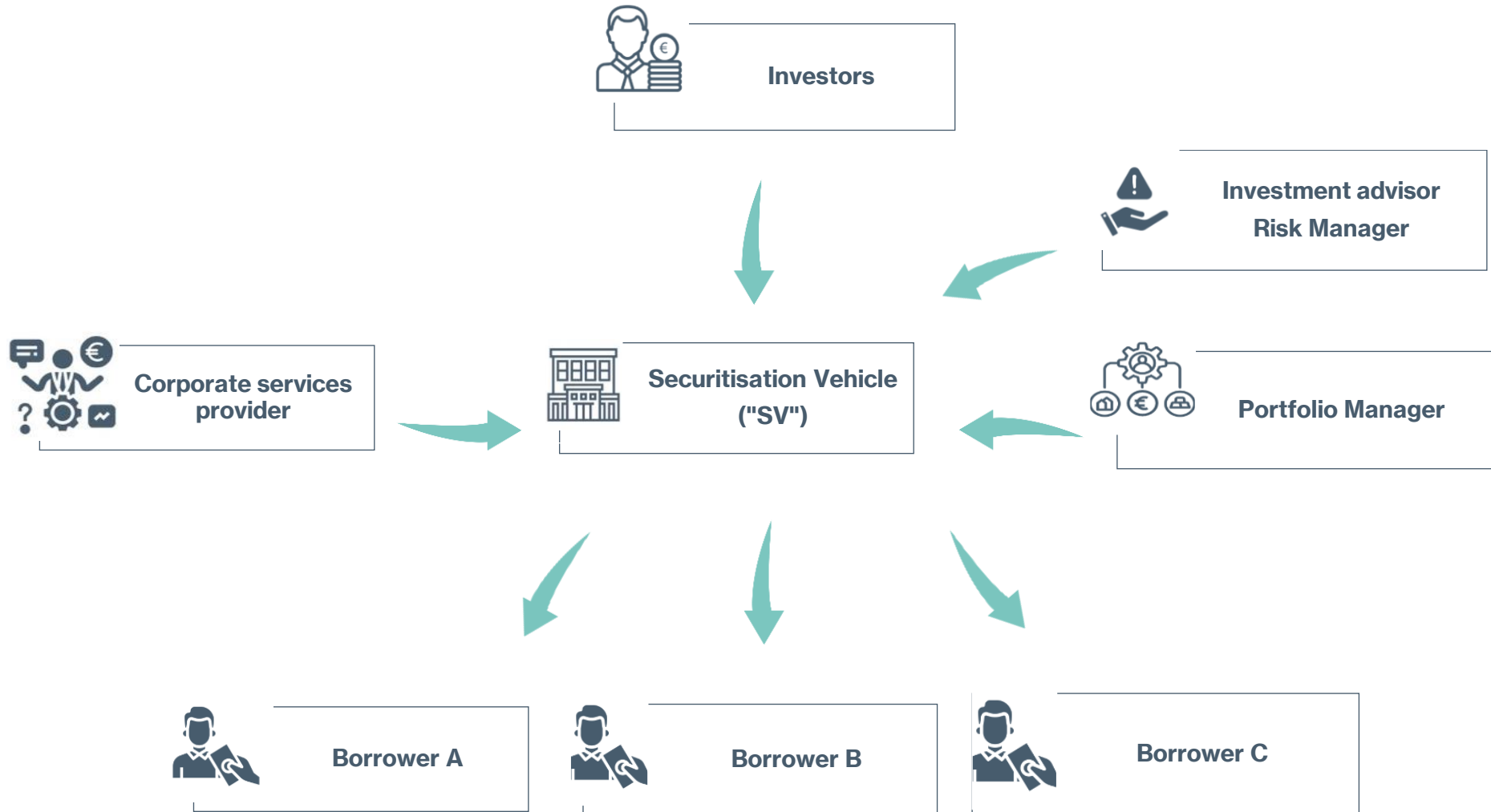
The Management Board of the SV supervises the admission of credit lines based on the reporting provided by the relevant parties. Such review shall be performed on a regular basis.

The continuous risk monitoring remains a responsibility of the SV's Management Board and is typically based on a review of a Servicer report and/or Investment Manager report (if available). An appropriate monitoring of the loan's exposures is necessary to comply with the risk limits approved by the Management Board of the SV. Such supervision includes:

- a. Monitoring collection process of overdue loans,
- b. Collateral monitoring,
- c. Identification of non-performing loan exposure and related default exposure,
- d. Appropriate accounting classification and measurement.

Focus on the management of non-performing and forborne exposure outlines a wide range of sound governance and operational arrangements which are expected to be implemented in a proportionate and effective way by the SV.

TYPICAL DIRECT LENDING STRUCTURE ILLUSTRATION



GLOSSARY AND ABBREVIATIONS

This paper is part of a series of guidance notes for Board Members and we encourage you to read the additional papers focusing on different types of transactions and underlying assets available on our [website](#).

C	Calculation Agent	means the party responsible for calculating and reporting on the distribution of interest, principal repayments, profit participation (if applicable) due to Noteholders. Full definition and roles can be found in the dedicated section in this publication. Full definition and roles can be found in the dedicated section in the LuxCMA Guidance Note for Board Members I Securitisation of Receivables released in April 2023 and available on the LuxCMA website.
	Cash Manager	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. Full definition and roles can be found in the dedicated section in the LuxCMA Guidance Note for Board Members I Securitisation of Receivables released in April 2023 and available on the LuxCMA website.

E	ECB	means the European Central Bank, which manages the euro and frames and implements EU economic and monetary policy.
----------	------------	--

L	LuxCMA	means the Luxembourg Capital Markets Association.
----------	---------------	---

M	<p>Management Board means the Board of Directors or the Board of Managers of the FVC/SV or its Management company.</p>
----------	---

P	<p>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 the LuxCMA Guidance Note for Board Members I Securitisation of Receivables released in April 2023 and available on the LuxCMA website.</p>
	<p>Publication means this document as well as the information contained herein.</p>

S	<p>Servicer 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 the LuxCMA Guidance Note for Board Members I Securitisation of Receivables released in April 2023 and available on the LuxCMA website.</p>
----------	---



Legal disclaimer: This document as well as the information contained herein (collectively the “**Publication**”) was prepared by the Luxembourg Capital Markets Association (LuxCMA).

This Publication has been prepared solely for information purposes. Although the LuxCMA has made reasonable efforts to ensure that the Publication is accurate and not misleading, the LuxCMA does not accept any responsibility or liability of any kind whether for the accuracy, reliability, or completeness of the Publication or for any action refrained or taken or results obtained from the use of this Publication. This Publication does not constitute and is not construed as any advice, recommendation, undertaking or commitment from or on behalf of the LuxCMA. This Publication shall not be substitute for the readers’ own researches, investigations, verifications or consultation for professional or legal advice

About the LuxCMA – Luxembourg Capital Markets Association

Created on 1 March 2019, the LuxCMA is a not-for-profit association (a.s.b.l.), registered at the RCSL (F12205), whose registered office is 6 rue Jean Monnet, L-2180 Luxembourg. The LuxCMA today represents memberships detailed on LuxCMA’s website (www.luxcma.com), which is composed by banks, law firms and services providers, amongst others.

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.

For more information, please contact info@luxcma.lu.

LuxCMA – Luxembourg Capital Markets Association
6 rue Jean Monnet | L-2180 Luxembourg
info@luxcma.lu | www.luxcma.com | Follow us on [LinkedIn](#) and [YouTube](#)