Luxembourg—cross border banking and finance guide

Produced in partnership with Charles Russell Speechlys LLP Speechlys for LexisPSL Banking and Finance

Loan market and developments

Please provide a brief overview of the current state of the loan markets in your jurisdiction and any significant recent market developments.

The Grand Duchy of Luxembourg (Luxembourg) has a well established reputation as a financial and business centre. Luxembourg's geographic position, political stability, competent and well trained workforce together with a solid legal and tax framework have contributed to this reputation as a financial and business centre and as being a hub for international trade and financing. The loan markets, be it those provided by banks or private loan financing, play a major role in Luxembourg and in the considerable volume of debt financing structured through Luxembourg.

Since the launch of the first worldwide listing of green bonds on the Luxembourg Stock Exchange (the 'Climate Awareness Bond' issued by the European Investment Bank in 2007), the Luxembourg financial market has made significant steps towards creating a legal framework for loans financing renewable energies and adopted on 22 June 2018 a law amending certain provisions of the law of 5 April 1993 on the financial sector (the **Financial Sector Act**) (ie Art. 12–1 and following of the Financial Sector Act), and introducing renewable energy covered bonds in its legal system. That law integrated into the existing legal framework a new type of renewable energy bond (**Green Bonds**) and allowed Luxembourg to rank as the leader of listed Green Bonds, with nearly 400 Green Bonds listed on the Luxembourg Stock Exchange through more than 100 individual issuers. This demonstrates the importance that Luxembourg attaches to the achievement of the sustainable development objectives and strengthens Luxembourg's position as a leading centre in the field of green finance. It is also worth mentioning that the Lux FLAG labelling agency launched the Climate Finance Label in 2016 for investment funds and the Green Bonds Label in 2017 specifically dedicated to green bonds. The granting of the Climate Finance Label ascertains for investors that the investment product invests at least 75% of total assets in investments related, with a clear and direct link, to mitigation and/or adaptation of climate change or cross-cutting activities. The granting of the Green Bonds Label ascertains for investors that the Green Bond follows internationally recognised standards and uses its proceeds to finance green projects.

Over the last years, the strong development of the alternative investment funds industry has had a significant impact on fund financing. Liquidity facilities initially developed to bridge capital calls are increasingly being used. Equity bridge financings are commonly used to pre-finance the investments or expenses of the fund. Depending on the dilution of the investors' basis, these can significantly shorten the funding of new investments and win competitive deals, switching from the burden of making capital calls to the investors which may take several weeks to a drawdown on a facility that may take two days. In complex umbrella structures, capital calls might become a time consuming exercise, both for asset managers and limited partners, and subscription facilities enable a streamlined and predictable process. Further, having recourse to bridge financings improves the internal rates of returns for the fund in the current financial environment where credit is cheaper than investors' equity. Many financial institutions now offer a large range of credit solutions and all indicators seem to confirm that this trend will strengthen in the coming years, sustained by a low level of defaults and better knowledge from the investors of the risks and benefits this strategy creates for them.

At this stage, no other significant market developments affecting the existing framework of the loan market have been observed. The general trend throughout Europe that private non-banking financing is favoured to bank loans and that loan transactions tend to be secured rather than unsecured loan transactions also applies to Luxembourg practice.

Please provide a brief overview of forthcoming changes to the law or other matters that may affect the loan markets or the responses to the questions below.

With the exception of the below, no major legislative initiatives are expected to directly affect the Luxembourg loan market in the foreseeable future.

The Luxembourg law of 8 January 2013 on over-indebtedness (*surendettement*) (the **Over-indebtedness Act**) came into force on 1 February 2014. The new law replaces the previous act of 8 December 2000 on over-indebtedness and amends, among others, article 2016 of the Luxembourg Civil Code (**LCC**) with respect to the validity of a guarantee (*cautionnement*) granted by a natural person.

On 6 April 2013, the Luxembourg Parliament adopted the law on dematerialised securities which was published in the *MÈmorial A* and entered into force on 18 April 2013.

On 1 February 2013, a bill amending and restating Luxembourg insolvency proceedings was presented to the Parliament (n∞. 6539 related to the protection against corporate insolvency). For the past two years, parliamentary work has been at a standstill and resumed from January 2020 following the complementary opinion of the *Conseil d'Etat* of 20 December 2019, following the recent adoption of the Directive (EU) 2019/1023. The adoption of such law will substantially affect the framework of Luxembourg insolvency proceedings without however having a materially adverse bearing on secured financings transactions.

On 15 May 2014, the Council adopted a Regulation establishing a European Account Preservation Order procedure to facilitate cross border debt recovery in civil and commercial matters. This Regulation aims at facilitating cross-border debt recovery by creating a European procedure leading to the issue of a European Account Preservation Order. The European procedure is an alternative to the national procedures in the case of cross-border debt recovery.

On 28 July 2014, the Act on the immobilisation of bearer shares was adopted (the **Immobilisation Act**). Pursuant to the Act, bearer shares must be entrusted to a depositary and the information concerning their holder must be contained in a specific register. The immobilisation obligation applies to all bearer shares issued before and after the entry into force of the Immobilisation Act. Legal status of bearer shares remains unchanged as the Immobilisation Act does not create a new type of shares, but it provides for new practical modalities, such as those pertaining to the perfection of security interests. That is, a pledge over bearer shares shall from now on be perfected by registration in the bearer shares registry as opposed to physical dispossession.

On 13 July 2016, the Parliament adopted the long awaited bill N∞ 5730 modernizing Luxembourg company law (the **Companies Act (2016) Amendments**), further consolidated by a Grand-Ducal regulation of 5 December 2017. Certain market practices now have a formal legal basis, and discussions on a number of questions have been put to rest. Freedom of contract and flexibility have, in keeping with Luxembourg tradition, been maintained while legal certainty has been enhanced. The changes are expected to make Luxembourg even more attractive for multinationals, private equity firms and investors seeking to structure their investments internationally, as well as for banking and finance operations involving Luxembourg corporate entities.

On 23 December 2016, the law transposing Directive 2014/17/EU on credit agreements for consumers relating to residential immovable property and amending the Luxembourg Consumer Code (*code de la consommation*) was adopted (the **Mortgage Credit Act**). The new regime applies to (i) credit agreements with consumers secured either by a mortgage or by a comparable security interest commonly over residential immovable property or credit agreements secured by a right related to residential immovable property and (ii) credit agreements the purpose of which is to acquire or retain property rights in land or in an existing or projected building. Prior to the adoption of the Mortgage Credit Act, the Luxembourg Consumer Code provided for a carve-out of the credit agreements with consumers secured by a mortgage. The newly introduced valuation methods and early repayment regime laid down by the Mortgage Credit Act have been transposed in the contractual framework of most of the Luxembourg banks and other lenders, since such requirements were not imposed by the Luxembourg legislator prior to the implementation of Directive 2014/17/EU.

On 18 January 2017, EU Regulation 655/2014 establishing a European account preservation order procedure to facilitate cross-border debt recovery in civil and commercial matters became fully applicable, making it possible for creditors in Luxembourg to obtain a preservation order for the bank accounts of a debtor situated in another EU Member State (except Denmark and the United Kingdom) and vice versa. The European account preservation orders (**EAPOs**) provide for greater transparency than existing Luxembourg law with regard to a debtor's assets (those held in a bank account), by allowing a creditor which possesses insufficient information about its debtor's assets to petition the court to order the Luxembourg financial sector regulator (**CSSF**)—the competent authority in Luxembourg under the new Act dated 17 May 2017 and transposing Regulation 655/2014—to produce information to this end.

On 27 February 2018, the law implementing EU Regulation 2015/751 of 29 April 2015 on interchange fees for card-based payment transactions was adopted. This implementation provides the CSSF with additional regulatory and sanction powers with respect to the caps of transaction interchange fees.

Luxembourg is often used as an intermediary jurisdiction for finance transactions, and once the term and content of the regulations on shadow banking have been defined, these could impact some of the comments below.

The Luxembourg legislator adopted on 10 July 2020 a law on the professional guarantee of payment (the **Professional Guarantee Act**). This new security shall usefully complete the legal framework of personal guarantees and solve certain legal risks existing in the case of the granting of first demand guarantees. In particular, a professional guarantee of payment can be granted to a security agent/trustee acting for the benefit of secured parties and the obligations of the guarantor are not affected by the opening of insolvency proceedings as against the original obligor of the secured obligation.

Lending

Is it necessary to obtain any consents or licenses in order to lend in your jurisdiction or enforce rights under a loan agreement and if so what is the process for obtaining the consent or license? Are there any other restrictions on lending that foreign lenders should be aware of?

The enforcement of rights under loan agreements or ancillary security interests or guarantees in principle does not require any licence. However, although some exceptions may apply, the granting of loans to the public can be made solely by (i) a duly authorized credit institution or (ii) a duly authorized professional of the financial sector carrying out lending operations, within the meaning of the Financial Sector Act.

A credit institution is authorized by the Minister of Finance and may act as a 'universal bank' (*banque universelle*), meaning it can perform all activities provided for and governed by the Financial Sector Act, including the granting of loans to the public.

Besides credit institutions, the Financial Sector Act allows the granting of a specific licence to professionals of the financial sector engaging in the business of granting loans (**Professionals Performing Lending Operations**).The main difference between credit institutions and Professionals Performing Lending Operations is that the latter cannot refinance themselves through deposits from the public.

Obtaining a licence as a credit institution in Luxembourg requires meeting various requirements as regards capital structure, shareholding structure, transparency and management. It is a long and expensive process the business rational of which shall be carefully assessed. The licence for a Professional Performing Lending Operations is conditioned by similar requirements although the capital basis requirements are much lower. In both cases, the authorization is granted by the Minister of Finance after a process of review of the application which must be submitted to the CSSF.

In any case, such authorization only concerns Luxembourg and foreign entities (which have no establishment in the EU) as EU based credit institutions and investment firms may provide cross-border services in Luxembourg through a branch or under the freedom to provide services within the limit of the activities they are allowed to perform under the licence delivered by the authority of their home Member State.

The Financial Sector Law defines the activity of Professionals Performing Lending Operations as the granting of loans to the public for own account and on a professional basis, which includes financial leasing and factoring as well as the acquisition on the secondary market of undrawn or partially drawn facilities, but excludes financing operations that are incidental to the pursuit of a commercial activity (eg financial leasing). Securitization transactions as well as undertakings for collective investments (**UCIs**), specialised investment funds (**SIFs**), pension funds, and risk capital investment company (**SICARs**) and their wholly owned subsidiaries are out of the scope of the Financial Sector Act.

The administrative practice of the CSSF allows several exemptions to licencing on the grounds that loans are not made to the public, or not made for own account or not made on a professional basis:

- as a result, unique or one-off credit operations are exempted because the activity is then not conducted on a professional basis

- similarly, the reference to own account leads to the exclusion of passive credit or investment activities and lending that are not financed out of own funds. The activity of a Luxembourg lender acting as a conduit for a foreign investment fund, where the borrowers are sourced by the fund and/or its advisor and the loan agreement is pre-negotiated, such that the Luxembourg special purpose vehicle enters into a turn-key agreement, merely following the lead of the fund for the management of its relationships with the borrowers, are generally considered by the CSSF as falling outside the ambit of the regulation because these are then not concluded for own account, and

- the granting of loans to a pre-identified limited group of persons—be it professionals or consumers—does not fall in the scope of the Financial Sector Act because the loans are not being granted to the public. While the CSSF does not set a limited number of persons above which it considers the activity to be made for the public, it insists that the persons be identified or identifiable based on an existing relationship or predetermined criteria which shall form the basis for the future relationship

In light of the latest international developments on shadow banking regulation, the CSSF invites investors who wish to take advantage of a regime of exemption to seek a clearance from the CSSF. Depending on how the overall transaction is designed, such clearance may be recommended, or absolutely necessary. In terms of risk management, it shall be highlighted that the conduct of operations of the financial sector without the required license exposes the persons participating in it to criminal sanctions, and expert advice should be sought.

There are as such no particular legal restrictions specific to the granting of loans to foreign borrowers, except for mandatory local public policy provisions (eg lenders, even acting from Luxembourg, may have to comply with the mandatory local consumer protection provisions).

Are there any taxes, duties or other charges associated with making loans to entities that are incorporated in your jurisdiction?

Except in the case of voluntary registration with the *Administration de l'Enregistrement et des Domaines*, as a matter of principle, under Luxembourg tax laws and administrative practice as at September 2020, it is not compulsory to file, record or enrol with any court or other authority in Luxembourg loans granted to Luxembourg entities.

In this respect, and provided that parties are not proceeding with a registration of the loans on a voluntary basis, no stamp duty, transfer, capital, registration, issue or similar duties or taxes or governmental fees and charges should be levied in Luxembourg.

Are there any restrictions, controls, fees, taxes or charges on foreign exchange in your jurisdiction?

No specific exchange control provisions exist as a matter of Luxembourg law. However, foreign exchange control provisions should be respected when performing contracts and a party may be bound by anti-money laundering/terrorism financing regulations and by any restriction imposed by Luxembourg authorities in any given circumstances.

On 20 July 2018, the law implementing Directive EU 2015/2366 (**PSD2**) of the European Parliament and of the Council of 25 November 2015 on payment services was adopted and entered into force on 29 July 2018 and amended the law of 10 November 2009 relating to payment services (as amended the **PSL**). The directive aims to create a more integrated and secured European payment services market that takes into account technological innovations in the field of financial services. The most innovative parts of the PSL are those aimed at adapting the existing legal framework to new technologies. In the interest of legal certainty and for user protection purposes, the new account information services and payment initiation services are now legally supervised and the providers of these services are supervised. The PSL explicitly provides for the right of payors and payment service users to apply to payment initiation service providers and account information service providers in order to obtain such services. The PSL continues to regulate currency conversions, and provides that the payment services provider shall disclose to the payment service user, the actual or reference exchange rate to be applied to the payment transaction. In case the exchange rate used is different from the exchange rate previously disclosed, the payment services provider shall disclose the exchange rate used in the payment transaction by the payer's payment service provider and the amount of the payment transaction after that currency conversion.

No specific taxes apply on currency conversion. Foreign exchange gains realized by Luxembourg resident corporations are subject to corporate income tax and municipal business tax at a combined rate of 24.94% (in Luxembourg City). Conversely, conversion losses should in principle be tax-deductible.

How is debt normally transferred in your jurisdiction?

Under Luxembourg law, debts may be transferred either by way of assignment (*cession de crËance*) or by way of a novation (*novation*).

The assignment of a debt is most commonly used to effect the transfer of the rights and obligations of a creditor towards a debtor without altering the legal relationship between the new creditor and the debtor, the contract formalizing the claim of the original creditor remains in existence despite a new creditor is substituted to him.

The governing law of a debt determines its assignability, the relationships between assignee and debtor and the rules of enforceability of the assignment towards the debtor Art. 14.2. of the EU Regulation 593/2008 of 17 June 2008 on the law applicable to contractual obligations (the **Rome I Regulation**). As a result, it is recommended that Luxembourg law governs the assignment of a Luxembourg law governed debt. As a matter of Luxembourg law an assignment of debt is enforceable towards the debtor thereof and third parties once the debtor has accepted it or was notified thereof.

In cross border lending transactions, however, the Rome I Regulation does not determine which law governs the enforceability of an assignment vis ‡ vis third parties. In the circumstances where the debtor of the assigned debt is a Luxembourg entity, such assignment will be enforceable towards third parties as from acceptance, or notification to the debtor (Art. 1690 of the LCC). If the debtor of an assigned Luxembourg law debt is located abroad, Luxembourg conflict of laws rules designate the law of the jurisdiction of the borrower to determine the conditions for enforceability towards third parties and it will therefore be necessary to ensure that the notification or acceptance of the assigned debtor is sufficient in the debtor's jurisdiction to make the assignment perfected as against third parties.

The assignment of a debt has no adverse effect on the security rights given as collateral to secure that debt. The assignee will thus benefit from any collateral securing the payment obligation of the debtor (Art. 1692 of the LCC). Similarly, the assigned debtor will remain entitled to invoke vis ‡ vis the assignee any exception it may have against its original creditor eg such as the occurrence of a legal set-off.

In very limited instances, novation may be used to substitute a new creditor to the existing one but it is much more regular to have recourse to novation to transfer the debt to a new debtor.

Novation is an extinguishment mechanism whereby the parties agree to substitute a new legal relationship to an existing one. The novation must be express (Art. 1273 of the LCC). It may be performed through substitution of the creditor or

the debtor, or by substitution of the obligation (debt) (Art. 1271 of the LCC). In the absence of an express contractual provision, the accessories (eg the security interests securing such payment obligation) of the old debt do not benefit the new one.

If the new debt is created by substitution of the debtor:

- the creditor may declare that the original debtor is fully discharged of its payment obligation, in which case the creditor will have no further recourse as against the original debtor, or
- the creditor may not discharge the original debtor, in which case both the original debtor and the new debtor are liable for the entire debt

Security and guarantees

Is it possible to take security over each of the following types of assets in your jurisdiction (including future assets) and what form does that security usually take?

Under Luxembourg law, several types of security interests may be granted, governed by specific provisions of the LCC, general law principles, or specific laws such as the Luxembourg law of 5 August 2005 on financial collateral arrangements, as amended, implementing the Directive 2002/47/EC of the European Parliament and of the Council of 6 June 2002 on financial collateral arrangements (the Directive 2002/47) and Directive 2009/44/EC of the European Parliament and of the Council of 6 May 2009 amending Directive 98/26/EC on settlement finality in payment and securities settlement systems (the Collateral Act). Other provisions regulate certain more specific security rights, such as the Luxembourg law of 27 July 2003 on trusts and fiduciary contracts (the **Fiduciary Contracts Act**) (implementing the Hague Convention of 1 July 1985 regarding the law applicable to the trust and its recognition, the **Hague Convention**), as well as the Grand Ducal Decree of 27 May 1937 (the **GDD 1937**) regulating the pledge over business (*gage sur fonds de commerce*).

The table below lists the assets and security that are available:

Assets	Availability of Security	Mostly used Security	Legal Basis
Equity Securities	Yes	Pledge	Collateral Act
Debt Securities	Yes	Pledge	Collateral Act
Receivables/Claims	Yes	Pledge	Collateral Act
Contractual Rights	Yes (limited to receivables, claims or obligations to deliver financial instruments (eg call option rights) deriving from contract. Most other obligations cannot be secured)	Pledge	Collateral Act
Bank Accounts	Yes (covers cash deposits and/or securities held on account)	Pledge	Collateral Act
Land and Buildings	Yes	Mortgage, Antichresis	LCC
Intellectual Property	Yes	Pledge (some restrictions apply), Security Assignment, Pledge over Business	LCC, Fiduciary Contracts Act, GDD 1937
Moveables	Yes (rarely taken because it generally requires the physical dispossession of the asset by the security provider)	Pledge, Pledge over Business	LCC, GDD 1937
Aircraft	Yes	Mortgage	Cape Town Convention & Aircraft Protocol, Aircraft Mortgages Act
Ships	Yes	Mortgage	Inland Vessel Mortgages Act, Maritime Mortgages Act

- *Basic considerations on civil law security rights*

  These considerations on civil law security rights apply to Luxembourg security arrangements that are governed by the LCC and, as such, relate primarily to property rights over tangible and/or moveable assets (ie civil law pledges), or immovable real property (ie mortgages), as well as to pledges over intangible intellectual property rights (**IP Rights**) and that are not subject to the specific regime of the Collateral Act or to special rules such as for instance those relating to international interests in aircraft or other high value mobile equipment.

  It is possible to grant a security covering both present and future assets requiring the debtor to cover all its commitments on its present and future assets. Given that physical transfer is required to perfect a mere civil law security right *in rem*, a security right with respect to future assets will in principle be considered as a promise to pledge (*promesse de gage*), ie to deliver the after-acquired collateral for the purpose of a security right and such promise will become an actual and effective security right once the physical transfer of the collateral is effected.

- *Basic considerations on security rights governed by the Collateral Act*

  The Collateral Act applies to pledges and transfer of title for security purposes over receivables and financial instruments (Art. 2075 of the LCC) in the broadest meaning and including without limitation securities issued by private and public companies. Security rights granted under the Collateral Act can only secure financial obligations or the obligation to deliver financial instruments (eg a pledge can secure a call option over shares). As a consequence, these security rights are often used in financial transactions to secure various financing agreements.

  The Collateral Act is a creditor-friendly legislation: by contrast to civil law security rights, the Collateral Act aims to offer to creditors the utmost protection against nearly any type of impairment, including Luxembourg and foreign insolvency proceedings affecting rights of creditors generally (by application of article 20 (4) and 24 of the Collateral Act), while offering the possibility to appoint a security representative or trustee to manage and hold the security rights for the benefit of secured creditors without having recourse to the mechanism of parallel debt.

  Under the Collateral Act and provided that assets are located or deemed to be located in Luxembourg, collateral may be given under the form of a pledge, or to a lesser extent, a transfer of property for security purposes. Such security constitute financial collateral arrangements and may cover present and/or future obligations. The Collateral Act further regulates netting and set-off arrangements in an insolvency remote environment, which is of particular interest in repository and hedging arrangements.

  By its essence, the transfer of title for security purposes implies the transfer of the ownership of the collateral to the beneficiary, which implies afterwards an obligation to retransfer the security assets (or equivalent collateral as agreed among the parties) to the security provider upon expiry of the security period (in the absence of an enforcement event). This form of collateral arrangement consists in the transfer of, including on a fiduciary basis, assets belonging or going to belong to the security provider to a secured creditor for the purpose of securing the debts owed by the security provider or a third party to the secured creditor.

  By contrast, a pledge governed by the Collateral Act is duly perfected and enforceable against third parties through the deemed dispossession (most commonly through registration in a register of title or notification to the debtor or a third party custodian) of the pledged assets on which the pledgor in principle keeps the ownership during the lifetime of the pledge. Receivables and financial instruments do not necessarily need to be clearly identified in the security agreement, the latter may only refer to the pledge of any such assets presently or in the future belonging to the pledgor, as long as those security assets can be identified.

- *basic considerations on fiduciary agreements concluded for collateral purposes*

  The Fiduciary Contracts Act provides that such fiduciary agreement may be entered into to secure present or future receivables. It may for extent be used in a context where the actual owner of an asset wishes for any reason to remain undisclosed to a third party, and finances the acquisition of the fiduciary assets from a third party. The fiduciary agent will then act as custodian to the finance parties. One must remain aware that the quality to act as fiduciary agent

is restricted by law and in practice this security is relevant in limited circumstances. Fiduciary arrangements may be concluded out of the scope of the Fiduciary Contracts Act but in these circumstances, the fiduciary estate is not legally segregated from the personal estate of the person acting as fiduciary agent.

- *basic considerations on pledge over business (gage sur fonds de commerce)*

  The GDD 1937 regulates the pledge over business. It may refer to the provisions of the LCC and Luxembourg Commercial Code as long as they do not derogate from the GDD 1937. It is very useful to allow small businesses that do not have real estate to mortgage to obtain credit. The main characteristic of this pledge is that the collateral is not subject to a dispossession, certain assets secured thereby being only sealed. Within a certain extent, a pledge over business can secure future assets.

- *basic considerations on mortgage over aircraft*

  This is a specialised area and particular rules provided for in the Convention on International Interests In Mobile Equipment dated 16 November 2001 (the **Cape Town Convention**) and its aircraft protocol (the **Aircraft Protocol**) apply. A Luxembourg Act of 29 March 1978 as amended pursuant to the law of 9 December 2008 (the **Aircraft Mortgages Act**) also allows setting up aircraft mortgages which do not fall within the scope of the Cape Town Convention. In any case, specialist advice shall be sought.

- *basic considerations on mortgage over ships and inland vessels*

  Security rights over vessels may be granted by way of ship mortgage, either under the Luxembourg law of 14 July 1966 on the registration of inland navigation vessels and on the mortgage on inland navigation (for inland ships with a weight of more than 20 tons or a length of more than 20 metres, the Inland Vessel Mortgages Act) or under the Luxembourg law of 9 November 1990 as amended on the register of international navigation vessels (such as container ships, the Maritime Mortgages Act, which implements the Brussels Convention of 27 May 1967 for the unification of certain rules relating to maritime liens and mortgages), or by way of title transfer for security purposes in application of the Fiduciary Contracts Act.

Land (immoveable property)

Immoveable property (real property) may be secured either by a mortgage (*hypothÎque*), ie a non-possessory registered security right or an 'antichresis' (*antichrÎse*), the latter being rarely used in Luxembourg as such registered pledge requires the transfer of possession of the real estate to the secured creditor including the fruits or rent income in lieu of payments on the secured obligations, whereas the mortgage still allows the security provider to occupy the land or building. The mortgage covers immovable assets, fixtures and fittings that are treated as immovable, eg contents of an immovable asset (fruits, harvesting, vintaging...), contents of the subsoil (sand, clay ...).

A mortgage is contractually taken by a notarial deed (*acte authentique*) and rendered effective as against third parties by registration with the mortgage register of the judicial district where the property is located. The registration is valid and enforceable against third parties for 10 years (Art. 2154 of the LCC) and is renewable for an unlimited number of 10-year periods, provided that the underlying debt for which the mortgage was created is not extinguished and the 10-year term has not expired. In the absence of such renewal in due time, the security will no longer be enforceable and the secured creditor will lose its preferential rank over such immoveable property.

In the case of mortgages, the specificity principle requires the document to clearly identify the immoveable property and to clearly specify the amount which the mortgage secures in the constituting deed. In addition, the secured obligation must be certain and liquid, otherwise no registration of the mortgage will be authorized. Therefore, it is impossible to grant a mortgage (*hypothÎque*) or an 'antichresis' (*antichrÎse*) over future properties (Art. 2129 of the LCC), because both require a clear and precise identification of the property in order to effect a valid registration.

Shares and other securities

- *Shares and equity securities*

  Security rights over financial instruments (shares/debt securities) and over claims are in principle governed by the Collateral Act, if these assets are located or deemed to be located in Luxembourg.

  As such, any security right over registered shares (*actions nominatives*) or another form of equity interest is normally taken in the form of a pledge (gage) governed by the Collateral Act, if such company is governed by Luxembourg law. It is also possible to take a security right in the form of a transfer of title for security purposes (*transfert de propriËtË ‡ titre de garantie*).

  The Collateral Act allows for multiple pledges on the same asset in favour of first, second (…) ranking pledgees (Art. 6 of the Collateral Act). This has the advantage of providing better financing capabilities, particularly in the case of high-value assets and creating multi-level financing structures (senior, mezzanine, junior) with a clear hierarchy between the various secured creditors. The terms of a pledge are governed by written agreement executed between the pledgor and the pledgee and the pledge is perfected and rendered enforceable against third parties by the dispossession or deemed dispossession of the pledged assets (please refer to the perfection formalities below for further details).

- *Bonds, notes and other forms of transferable debt securities*

  Bonds, notes and other forms of transferable debt instruments may also be secured by a pledge and the formalities required for the dispossession/perection will depend on the type and form of such debt instruments in accordance with the Collateral Act.

  For registered securities, the perfection of the pledge is effected by registration of the pledge in the relevant register of the issuer of such instrument. As with the shares, the lower ranking pledge is only possible with the consent of the higher-ranking pledgee.

  For some bearer debt instruments (such as bills of exchange, promissory notes or commercial paper (*billet de trÈsorerie*)), a transfer by way of endorsement can be made. The mechanism of endorsement (*endossement*) used for the transfer of ownership or for the perfection of security rights over these bearer debt instruments does not apply to the transfer or the creation of security rights over equity instruments. Under Luxembourg law, the endorsement consists of the inscription of the name of the bearer onto the bearer debt instrument. Endorsing such certificate is not a condition to its transfer, but any future bearer of the certificated debt instrument may request, in principle, the payment of the underlying debt from any person having endorsed the certificate prior to its acquisition. Security rights granted over certificated debt instruments transferable by way of endorsement are perfected through a specific form of endorsement, for the purpose of granting such security right (*endossement ‡ titre pignoratif*) and which indicates the name of the pledgee (or its security representative) on the certificate. Otherwise, an acquisition without endorsement will constitute a 'transfer in blank' made through physical delivery of the debt instrument (*tradition manuelle*) and such bearer will therefore not appear in the chain of possession as evidenced by any endorsement on the bearer debt instrument.

Cash deposits in bank accounts

Security rights over cash claims as well as over accounts are governed by the Collateral Act. Security rights can take the form of an account pledge or of a transfer of title for security purposes (please refer to the section Shares and other securities above). A security interest to be taken under the form of a pledge over a cash deposit account may either be considered as a security interest under the form of a pledge taken over a cash claim held against the bank or a security interest over an account (to the extent cash can be assimilated to financial instruments) held by that bank. In practice however the differences in the drafting of the pledge agreements are minor as both pledges take the form of a pledge over account and it is commonly agreed to notify such pledges to the account bank to ensure perfection. Technically however, and since all banks' general conditions in practice contain a right of pledge, a clause of unicity of accounts and a general right of set off, the account bank, as first ranking pledgee, shall waive those rights that may invalidate the third party pledge or reduce its basis. This waiver is traditionally called the "acknowledgment" and is paramount to the creation

of a valid first ranking security interest. In the case of enforcement, priorities between competing pledgees are governed by specific rules which will be further developed below.

Receivables (non-contractual and contractual rights, including rights under insurance policies)

- *Receivables*

  Security over rights to claim payment of a monetary sum (*crËances de sommes d'argent*) are governed by the Collateral Act. Security rights can take the form of a pledge or of a transfer of title for security purposes.

  The receivables pledge takes effect between the parties, and is automatically perfected as against the relevant debtor and against third parties (debtor and competing creditors) as of the date of execution of the pledge agreement. However, for a pledge over receivables to be fully effective, it requires the notification of the acceptance of the debtor, without which the latter may validly discharge its payment obligations towards the pledgor.

  The parties can establish in writing a list of receivables pledged, or otherwise identify the pledged receivables by any other means to identify the pledged receivables and evidence the scope of the pledge towards the debtor of the receivables or any third party.

  In an international context, the law governing a receivable subject to a pledge or security assignment governs the enforceability of the pledge or security assignment against the debtors of the receivable, in accordance with Article 14 (2) of the Rome I Regulation. The law governing the receivable therefore determines whether the receivable can be pledged and regulates the relationship between the pledgee and the debtor of the secured receivable, inter alia with regard to perfection, enforcement and discharge of the secured obligation. As a result, when structuring the security package, it is advisable to secure receivables under the same law as the one that governs such receivables in order to avoid any potential conflict of laws. While perfection requirements as against the debtor are determined by the law governing the receivable in pursuance of the Rome I Regulation, the latter is silent on the law that shall govern the enforceability of a pledge over receivables as against third parties. Luxembourg conflict of law rules designate the law of the jurisdiction of the debtor. As a result, a particular caution shall be taken as to matters of perfection each time (i) a Luxembourg law pledge over receivable aims to secure a claim the debtor of which is based out of Luxembourg and/or (ii) a foreign law security interest aims to secure a claim the debtor of which is based in Luxembourg and it may be necessary to ensure that any relevant foreign perfection requirements under the laws of the jurisdiction of the relevant debtor be complied with following the execution of the pledge agreement. Similarly, it may be necessary that foreign law security rights over receivables whose debtor is located in Luxembourg be perfected in Luxembourg, as a result of the traditional conflicts of laws rule according to which the proprietary effect on third parties of the security right is governed by the law of the debtor's domicile (as the *situs* of the receivable).

- *Contractual rights*

  Contractual rights have to be considered either as financial instruments or as claims (*crËances*) depending on the type of rights concerned, to benefit from the Collateral Act. Security is available over receivables or claims deriving from a contract. Most other rights resulting from a contract are not capable of being secured. A security right over the relevant contractual right is created and perfected by written agreement between the pledgor and the pledgee, as further explained below.

Intellectual property

IP rights are intangible personal property and are normally subject to security rights in the form of a civil law pledge governed by LCC.

Given that physical transfer is required to perfect a civil law pledge, a pledge with respect to future assets will in principle be considered as a promise to pledge (*promesse de gage*), ie to deliver the subsequently-acquired collateral for the purpose of a security right and such promise will become an actual and effective security right once the physical transfer of the collateral is effected. Therefore, any security right with respect to future IP rights will in principle be considered as a promise to pledge.

In order to be enforceable against third parties, pledges over registered IP Rights must be registered with IP registers such as the Benelux Office of Intellectual Property (for trademarks and designs) at The Hague (Netherlands), or the Intellectual Property Department of the Luxembourg Ministry of Economy, in Luxembourg, or the European Patent Office In Munich (Germany), or the European Intellectual Property Office (for trademarks and designs) in Alicante (Spain) and respectively, in accordance with the law where the register is held. Security rights over unregistered IP Rights (such as copyrights) are created by private agreement and perfected through notification to the debtor in accordance with civil law. No mandatory public registration is as such required for unregistered IP Rights.

A security right over registered IP rights may also be granted by way of title transfer for security purposes to a licensed fiduciary (*fiduciaire*) under a fiduciary contract, as provided for by the Fiduciary Contracts Act. Perfection against third parties is then effected by registration with the relevant register. In the case of unregistered IP Rights (such as copyrights), the title transfer for security purposes to a licensed fiduciary can be made by private agreement without any third party notification or any mandatory public registration which allows the fiduciary security right to remain entirely undisclosed.

Tangible assets such as ships, aircraft, machinery, etc.

- *Aircraft and ships*

  Security rights over aircraft may be granted in accordance with the Cape Town Convention in conjunction with its Aircraft Protocol, as ratified by the Luxembourg law of 28 May 2008, in force as of 1 October 2008 (similar to the regime under the Collateral Act). An international security interest over aircraft constituted (by private deed) under the Cape Town Convention and the Aircraft Protocol prevails over any aircraft mortgage under internal Luxembourg law, even if the latter was registered earlier. The nature of the asset makes it highly relevant to privilege an international security interest enforceable in several jurisdictions over a Luxembourg law mortgage under the Aircraft Mortgages Act. Further, contrary to a mortgage granted under the Aircraft Mortgages Act, an international security interest over aircraft will take precedence on legal privileges.

  International security interests fall within the scope of the Cape Town Convention when created pursuant to agreements where (i) the debtor of the secured claim is situated in a contracting State of the Cape Town Convention or (ii) an airframe (not an engine) is registered in a contracting State of the Cape Town Convention. International security interest means an interest in an airframe or an aircraft engine or a helicopter (i) vested in a lessor under a leasing agreement, (ii) granted to a secured creditor under a mortgage or (iii) vested in a seller under a title reservation agreement.

  Internal Luxembourg security right over aircraft that does not fall within the ambit of the Cape Town Convention may be created under the Aircraft Mortgages Act, either in the form of a mortgage or by way of title transfer for security purposes (*transfert de propriËtË ‡ titre de garantie*) in application of the Fiduciary Contracts Act. Title to an aircraft can be transferred for security purposes only to a licensed fiduciary or to a (foreign) trustee, in which case such quality of licensed fiduciary or trustee must be registered at the aircraft mortgage register (*Bureau de la conservation des hypothÎques aËriennes*) in addition to registration with the Luxembourg Administration of Registrations and Domains (*Administration de l'Enregistrement et des Domaines*). Registration is valid for a renewable 10 year period. If the security interest is an international interest over aircraft governed by the Cape Town Convention and the Aircraft Protocol, such interest is perfected (and its priority established on a first-to-file basis) upon the registration with the International Registry of Mobile Assets in Dublin (Ireland). In the case of mortgages, the civil law rules on mortgages are applicable.

  Inland ship mortgages and maritime mortgages are in principle constituted and perfected in accordance with the civil law rules on mortgages, except where otherwise provided by the Inland Vessel Mortgages Act or the Maritime Mortgages Act. Accordingly, registration with the inland ship mortgage register (*Bureau de la conservation des hypothÎques fluviales*) or the maritime mortgage register (*Bureau de la conservation des hypothÎques maritimes*), as applicable, is required following constitution of the mortgage (either by notarial deed or by written agreement with the declaration or certification set out under Section Land above). The registration is valid for a renewable 10-year period.

If the ship loses its Luxembourg nationality because it is not registered with the relevant Luxembourg register and/or is not authorized to sail under the Luxembourg flag, the mortgage will continue to exist until it expires, but no additional Luxembourg mortgage may be created over such asset.

In any case, a security right granted over an aircraft, an inland ship (with a weight of more than 20 tons or a length of more than 20 metres) and/or an international vessel (such as container ships) shall require a notarial deed or a written agreement unless governed by the Cape Town Convention and Aircraft Protocol, as applicable.

- *Moveable property (including machinery)*

  Security rights over moveable personal property are created by a civil law pledge under the LCC. Civil law pledges can be granted over most categories of moveable property, either tangible or intangible, on present and future assets, and also on fungible goods, such as agricultural products. A civil law pledge may be created by a private written agreement.

  However, in practice security rights are rarely taken over tangible moveable's (eg plant and machinery) because of the requirement that the tangible moveable be in the possession of the secured creditor which most commonly renders this security commercially unacceptable for the security provider. Pledges over movables without dispossession are only available in limited circumstances and under specific legislation, including under the form of a pledge over business (*gage sur fonds de commerce*). Given that moveables can be transferred from one jurisdiction to another, the legislation of their situation (*lex rei sitae*) may be replaced by the legislation applicable to the contractual relationship that they derive from. Parties to a contractual relationship may choose to submit their contract to a foreign law in accordance with the Rome I Regulation, within its scope of application. A Luxembourg court could thus decide to apply the law chosen by the parties rather than the lex rei sitae, although there is no court precedent on this point and we do not express any final view hereon, particularly in respect of mandatory publicity of possession (or false wealth) aspects in a perfection context which would need to be evaluated by a Luxembourg court.

Inventory or stock

A civil law pledge with respect to assets such as inventory or stocks is excluded in practice because such pledge necessarily implies a delivery (*dispossession*) of the collateral from the pledgor to the pledgee. Inventory or stock may be the subject matter of a pledge over business (*gage sur fonds de commerce*).

A pledge over business usually includes all the assets of the pledgor (in a broad meaning) such as the goodwill, the trade name (*enseigne*), customers, tools, the concession, the commercial organisation, the trademarks, the patents, the machinery, equipment and part of a stock, unless otherwise agreed between the parties. The pledgor who pledges its business as a going concern acts as custodian (*gardien*) of the collateral as long as the secured obligations remain unpaid.

A pledge over business is subject to specific requirements set out in the GDD 1937, it can only be granted to authorized credit institutions, breweries and notaries, and the secured debt may only be assigned to persons or institutions approved by the Luxembourg government.

In order to be valid, a written agreement is required, which is enforceable against third parties after registration at the mortgage register of the judicial district in which the business is run or the stock or goods are located. In light of the latter and given that an authorization has to be obtained from the government, the perfection of a pledge over business is a lengthy and costly process that may take several months to complete (unless the relevant credit institution is already authorized). For that reason, in the limited instances where the finance parties are willing to obtain this security, it generally completes the wider security package and is made a condition subsequent to drawdown. In addition, the pledge may cover only 50% of the stock (if any) of the pledgor, and will be valid for a renewable 10 year period. Where there are no specific provisions (including under the Luxembourg Commercial Code), the civil law rules on pledges over moveable personal property remain applicable. Under Article 119(2) of the Luxembourg Commercial Code, the rights of the pledgee under such pledge are suspended neither by the opening of insolvency proceedings in respect of the pledgor nor by the death of the pledgor but any such security granted during the clawback period preceding the insolvency of a pledgor will remain voidable according to common insolvency regulation.

In relation to each type of asset listed above:

What formalities are necessary or desirable to perfect the security and what is the effect of the formalities not being carried out?

Depending on the type of security right, specific perfection requirements must be met to ensure that the security right is valid and enforceable as against third parties, or remains valid and enforceable as against third parties. Luxembourg law does not require information concerning the existence of a non-possessory security right over assets located in Luxembourg (other than mortgages and antichresises) (*antichrÎse*)) to be made publicly accessible in a public filing, recording or registration system. As such, public searches are generally not available in the area of Luxembourg-based secured transactions, except in respect of mortgages, where secured creditors may request from the relevant register in writing information concerning any security right of record attaching to the collateral (real property, pledge over a going concern, ship or aircraft) in question.

In the case of a personal property security (other than mortgages or antichresises), the pledgor will usually be required to perform the perfection requirements, on a first-in-time basis. In the case of a mortgage or an antichresis, the secured creditor will perform the perfection requirements on a first-to-file basis.

The perfection of a security right over qualifying collateral under the Collateral Act does not prevent a competing creditor from bringing an action to obtain attachment or seizure of the collateral for the purposes of a forced sale, but the priority of the secured creditor under the security right over the proceeds of such sale will not be impaired. Similarly, pledges under the Collateral Act are protected against any criminal attachment order, whose effects are suspended until the release of the pledge by the pledgee.

Depending on the type of security right, the following perfection steps are required:

- **civil law pledges**: dispossession through physical delivery of the collateral from the pledgor to the secured creditor as pledgee.

- **mortgage and antichresis**: (registration at the mortgage register on a first-to-file basis by or on behalf of the secured party (please refer to our explanations under the Section Land above)).

- **ship mortgage**: for inland vessels, the registration with the inland vessel mortgage register in Luxembourg. If the mortgage was constituted by written agreement under private form (instead of a notarial deed), the required information on the parties and the vessel may be replaced by a written declaration at the end of the agreement or by a certification of the shipping court for the Mosel (*Tribunal de navigation pour la Moselle*) in Luxembourg that is annexed to the deed. The perfection of the maritime mortgage constituted by a notarial deed will be made by the registration at the maritime mortgage register (*Bureau de la conservation des hypothÎques maritimes*). If the mortgage was constituted by written agreement, it will have to be notified to the registrar (*conservateur*).

- **security rights over registered IP Rights**: registration with the relevant IP register. Security rights over unregistered IP Rights are perfected as against the debtor through notification to the debtor in accordance with civil law.

- **pledge over claims**: perfection as between the parties, automatically against the debtor and third parties as of the date of execution of the pledge agreement, without prejudice to any foreign law specific perfection requirements.

- **pledge over shares**: perfection depends on the nature of the shares.

- **a pledge over registered shares/equity securities**: is perfected by the registration of the pledge in the share register of the issuer or the register for the relevant equity which shall remain at the registered office of such issuer in Luxembourg.

  Notwithstanding the foregoing, a pledge over shares in a private limited liability company (*sociËtË ‡ responsabilitË limitËe*) may have limited bearing in the circumstances where such pledge would not have for basis the entire share capital of the issuer. Indeed, the Luxembourg law of 10 August 1915 (the **Companies Act**) (Art. 710–712 of the Companies Act) restricts the transferability of shares in a private limited liability company through conditioning

the validity of a share transfer to a third party (ie a person who is not yet a shareholder) to the prior approval of its shareholders representing at least 75% of the shares outstanding in issue (albeit the articles of the issuer may reduce that majority to 50%). As a result, a pledgee seeking to enforce his rights under such a share pledge agreement will be confronted to the corporate inability to, or have a third party nominated by him or a third party purchaser to, become a shareholder in the private limited liability company as a result of the enforcement of his security right. The Collateral Act allows to obtain such corporate approval at any time prior to the enforcement of the pledge but in practice such corporate approval must be made a condition precedent to the financing at stake to ascertain the economic efficiency of the security interest. Once granted, such approval is irrevocable (Art. 12 of the Collateral Act).

- **a pledge over bearer shares** is, as a result of the Immobilisation Act, perfected through the registration of the pledge in the register of bearer shares that must be held by the depositary entrusted with the bearer share certificates representing those shares.

- **pledge agreement over financial instruments (securities) held in an account**: perfection occurs (including through the concept of control) as follows:

    - the mere execution of a pledge agreement by the depositary if the depositary is also the secured creditor (automatic perfection/control by status);

    - a control agreement between the pledgor, the pledgee and the depositary bank, or an agreement between the pledgor and the pledgee, notified to the account bank, according to which the latter will comply with instructions by the pledgee without further consent of the pledgor;

    - the registration of the financial instruments in the account of the pledgee (control by becoming the account holder)—this rule also applies in the case of a security assignment;

    - registration in an account opened with a depositary in the name of the pledgor or in the name of an agreed third party custodian (*tiers convenu*), the financial instruments being designated as pledged individually or collectively by reference to the relevant account in which they are recorded (book-entry perfection or earmarking), this rule also applies in the case of a security assignment.

      A lower ranking pledge is perfected only with the consent of the higher-ranking pledgee(s). This implies an automatic waiver by the depositary of its priority over the financial instruments except where agreed otherwise or in the case of a notification made where the depositary has not expressly accepted such waiver of its priority.

- **pledge over business**: does not require the transfer of the collateral, however it must be entered into under private or notarial deed, with registration at the mortgage register (*Bureau de la conservation des hypothÎques*).

There are no ongoing requirements in relation to the maintenance of the security outside the obligation to renew registration with the mortgage registers, IP registers or ships and aircraft registers (please refer to our explanation above).

It is however common market practice that pledges over registered securities are contractually confirmed and re-recorded (i) when the security obligations are extended and/or (ii) when the pledgor subscribes for further securities due to be pledged as future collateral assets pursuant to the original pledge agreement. If perfection requirements have not been validly performed, the pledgee may not obtain the benefit of a valid security right over such collateral asset, may have no preferential rank and/or may be unable to enforce its security right as against third parties benefiting from a validly perfected security right, even if his security right predates the one of a third-party secured creditor. The pledgee may also be in competition with other unsecured creditors of the debtor over the same asset and be paid on a first-to-file basis or at the pro rata of the claim it has against the debtor (*au marc le franc*).

What costs are involved in taking security over each asset, including notarial fees, registration fees and taxes and are there any ways to minimize these costs?

In general, security rights require a private written agreement but not necessarily a notarial deed (*acte notariÈ*), therefore no public registration is required and the costs of such documents are rather limited. However, mortgages, antichresis (*antichrÎse*), IP Rights, pledges over a going concern and security rights over real estate, aircrafts, inland ships or

international vessels may require a notarial deed, a registration in a public register and the renewal of such registration for the continuation of the security right. Proportional registration duties may apply on the registration of these notarial deeds. The registration of a mortgage on real estate, aircrafts, inland ships or international vessels is generally subject to proportionate registration duties.

Does your jurisdiction recognize the concept of a trust? If not, is there an accepted method of ensuring all lenders get the benefit of security? Are there any limits on action a security agent could take on behalf of the secured parties?

In general, the legal concepts of 'trust', 'trustee' and 'security trustee' and related legal concepts do not exist in Luxembourg law. However, Luxembourg law recognizes trusts in the specific circumstances outlined below:

- Foreign trusts may be recognised under certain circumstances under the Fiduciary Contracts Act. A trust is therefore considered a foreign legal institution which may be granted effect in Luxembourg through recognition. The Hague Convention merely regulates the conditions for such recognition, including the requirement of a valid trust in accordance with its own governing law, the ability of the trustee to manage the collateral and represent the beneficiaries (eg, in the case of judicial proceedings) and the segregation of the trustee's assets from the beneficiaries' assets. Once recognized, the trust remains subject to its own governing law, chosen by the parties, subject to certain exceptions (including the non-recognition of the chosen governing law in the case of a closer connection with another jurisdiction which does not recognise trusts, the application of mandatory provisions and the general exception of public order). In light of the above, the use of a foreign law trust may be recognized in Luxembourg. As a consequence, any asset eligible to be managed in Luxembourg under a trust in accordance with the law chosen to govern such trust, may be subject to the trust that is to be recognized in Luxembourg (eg real estate, properties).

- Article 2(4) of the Collateral Act provides that financial collateral may be granted by a person acting on behalf of the beneficiaries of the financial collateral, a fiduciary or a trustee to secure the claims of third party beneficiaries, present or future provided that such third party beneficiaries are identified or can be identified. The persons acting on behalf of third party beneficiaries, the fiduciary or the trustee enjoy the same rights as those granted to direct beneficiaries of the financial collateral arrangement by virtue of the Collateral Act, without prejudice to their obligations towards the third party beneficiaries of the collateral.

- Article 18 3. of the Aircraft Mortgages Act, which in essence replicates Art. 2(4) of the Collateral Act.

- Article 4 (3) of the Professional Guarantee Act, which also in essence replicates Art. 2(4) of the Collateral Act.

A *contrario*, the concept of security agent / trustee does not exist in relation to real estate mortgages. In that scenario, the mechanism of parallel debt is commonly used in foreign law credit facilities and should be legal and valid as a matter of Luxembourg law although we have no knowledge of a Luxembourg case law ruling on the subject matter such that a certain level of uncertainty remains.

In practice, a specific circumstance in which the lack of recognition of the trust in Luxembourg raises reservations in cross border financing transactions is when the intercreditor agreement provides that any sum received by the Luxembourg junior creditor (which is most commonly also an obligor) shall hold on trust for the benefit of the finance parties any assets distributed to it in breach of the intercreditor agreement. While the provision is not per se invalid, those assets deemed to be held on trust will not be segregated of such junior creditor's assets which may by hypothesis dilute the economical recourse of the senior creditors vis ‡ vis such obligor in an insolvency scenario.

Will changes to the group of lenders adversely affect the security or require any steps to be taken as regards the security package in your jurisdiction?

Under Luxembourg law, debts may be transferred either by way of assignment (*cession de crËance*) or by way of novation (*novation*) (please refer to our explanations above).

As a result, it is necessary to provide, in the security documentation, a specific provision allowing the transfer of such security rights with a power for the transferee to exercise all rights and powers which were available to the former pledgee.

In addition, it is possible to appoint a security representative (security agent) or trustee to act on behalf of a group of secured creditors, and such creditors do not have to be listed in the security documentation: a mere reference to the intercreditor agreement or the document by which the creditors have appointed the security representative or trustee (which is to be amended in the case of a change in the group of creditors) will suffice to have a valid pledge granted to the security representative or trustee, regardless of any change that may occur within the group of creditors.

How is security commonly released in your jurisdiction?

In general, a security right is released in the reverse manner as it is created and perfected (the principle of parallelism of forms).

In the case of a civil law pledge or a pledge requiring physical delivery under the Collateral Act, the restitution of the asset to the debtor will be operated by a release of the security from the collateral (*mainlevËe*). The release will be documented by a release agreement. In the case of a mortgage, the registration will be deleted from the mortgage register, in accordance with a specific procedure applicable to such register.

Under the Collateral Act, where the security concerned is an account pledge, the release of the security over the account will require the information of the account bank, to ensure it has knowledge of such release and is properly instructed as to whom any payments may be directed following the release. In the case of a share pledge agreement over registered shares, the release of the pledge will be mentioned in the share register of the relevant company.

What forms of quasisecurity are common in your jurisdiction?

In general, Luxembourg law distinguishes between personal guarantees (*s˚retËs personnelles*) and personal property security rights (*s˚retÈs rËelles*).

Personal guarantees can be of several types. The most common are (a) the suretyship (*cautionnement*), (b) the autonomous (or first demand) guarantee (*garantie autonome/‡ premiÎre demande*) or (c) the letter of comfort (or letter of patronage).

The suretyship has long been the reference security in Luxembourg, and results in a triangular relationship between the guarantor, the secured debtor and the lending creditor. There are three relationships in a suretyship between:

- the creditor and the secured debtor
- the secured debtor and the guarantor, and
- the guarantor and the creditor

The suretyship implies the necessary existence of a principal obligation, without which there can be no suretyship. This dependence expresses the essential characteristic of a suretyship: its ancillary nature to the principal secured obligation. As a result, the guarantor may in principle (ie unless waived) invoke all remedies that are available to the principal debtor in respect of the (non) performance of its obligation. As a result, any circumstance that affects the obligation of the secured debtor similarly affects the guarantor's obligation such as:

- the secured obligation is invalid or reduced for any cause
- the secured obligation has not fallen due, and/or
- the secured obligation is extinguished for any cause

In order to be valid and enforceable, a civil suretyship will require certain hand-written annotations.

Most regularly, the suretyship is in practice granted as a joint and several suretyship (*cautionnement solidaire*) which in essence means that the guarantor waives the benefits of discussion and division and hence the secured creditor may directly action the guarantor and may claim payment of the whole debt from any guarantor.

The autonomous or first demand guarantee is a type of guarantee that was created by international commercial practice and recognized by Luxembourg case law in 1980 (Tribunal d'Arrondissement, 17 June 1982, n∞ Role 26426). It is characterized by its autonomous nature meaning that the obligation on the guarantor must remain independent of the underlying secured obligation. As a consequence, and in order to avoid any risk that the autonomous or first demand guarantee may be requalified by a Luxembourg court into a suretyship (ie an accessory to the secured obligation), the guarantee must be drafted so as to avoid the assessment of the performance of the secured obligation, nor any reference to any outstanding payment obligation thereunder. As such, there is a risk that a Luxembourg court requalifies a guarantee into a suretyship if the guaranteed amount is defined as "*the outstanding debt of the secured debtor from time to time*". The guarantee must further be unconditional and irrevocable. When properly drafted, the guarantor will not be able to oppose to the beneficiary any exception arising from the contract formalizing the secured obligation, or specific to the debtor thereof.

In most cross border financing transactions, the guarantees granted by the Luxembourg obligors are governed by a foreign law or if Luxembourg law governed, take the form of an autonomous or first demand guarantee. The recent adoption of the Professional Guarantee Act creating the professional guarantee of payments may nevertheless affect this trend.

The professional guarantee of payments leaves to the parties a substantial contractual freedom and consists of the commitment of a guarantor to pay to a beneficiary or an agreed third party a given sum determined by their agreement in relation to receivables or risks attached thereto. The professional guarantee of payments must be granted in writing and be expressed to be governed by the Professional Guarantee Act. The purpose and payment modalities of the professional guarantee of payments are determined by the agreement of the parties. The guarantee may be called upon the occurrence of any event contractually agreed, whether or not the secured debtor is defaulting under his payment obligations. No exception can arise from the secured obligation or personal to the debtor thereof, to limit the rights of the beneficiary or agreed third party. Last but not least, a professional guarantee of payment can be granted to a security agent/trustee acting for the benefit of secured parties and such new security may therefore fully find its place in any syndicated financing.

Can entities in your jurisdiction give guarantees? If so are there any restrictions or limitations on an entity incorporated in your jurisdiction granting such guarantees and are there any common ways of minimizing the impact of these?

Breach of constitutive documents

Any company may only act within the limits of its corporate object or purpose, as described in its constitutive documents, in the case of a holding company, its articles of association and the case maybe its shareholders' agreement, in the case of funds, also taking into account any specific provisions in their prospectus or private placement memorandum, or any side letter or other standalone agreement entered into with one or several of their investors.

The corporate object clause of a Luxembourg company often limits the granting of financial assistance to affiliated entities and/or entities in which they hold an interest. Sometimes, the granting of financial support is restricted to direct or indirect subsidiaries. A guarantee granted in breach of the corporate object of the guarantor, or of any other restrictions imposed in its constitutive documents, would however in principle remain binding on the company, even in the circumstances where such limitations and restrictions are published, save in the circumstances where the company can demonstrate that the beneficiaries had knowledge of such restriction or could not ignore such restriction in the given circumstances (Article 441–13 (for *sociËtËs anonyme*) article 710–15 (5) (for *sociËtË ‡ responsabilitË limitËe*) of the Companies Act). In the context of cross border financing where the parties are most commonly each represented by a lawyer, it is in our opinion likely that a Luxembourg court would rule that the counterpart could not ignore this factual circumstance and thus declare the guarantee null and void.

The risk of such requalification is higher where such guarantee hinders considerably the credit of the company or appears to be obviously disproportionate as regards the financial capacity of the company and not to the benefit of the company. In addition, directors of a company may even incur criminal penalties for misappropriation of corporate assets (*abus de biens sociaux*, Article 1500-11 of the Companies Act) if they derive a personal benefit (not necessarily pecuniary) from the granting of such guarantee.

Corporate interest

The concept of corporate interest as such is not expressly qualified in Luxembourg law, neither in the Companies Act nor in the LCC. The concept of corporate interest is distinct from the individual interest of each shareholder as well as from the particular interests of a majority group of shareholders. As a result, any transaction shall be appraised by the management of the company in light of the corporate interest and benefit that the company may obtain from entering into a given contract.

While no specific issues arise for downstream guarantees, where the guarantor is securing its own or its direct or indirect subsidiaries' indebtedness, the appraisal of the corporate interest of the guarantor will be critical for all parties to the transaction each time the guarantee secures parent or sister companies (up-stream and cross-stream guarantees).

Luxembourg practitioners do commonly take into account the interest of the group to which a Luxembourg entity belongs, which may validly sustain the company's own interest, having regard to the group financial and strategic policy for the realization of a common goal. A financial assistance grounded on the economic, social or financial interest of the whole group may validly sustain the corporate interest of a Luxembourg obligor provided that such financial assistance does not break the balance between the different commitments of the group companies and is given adequate financial consideration, as long as the financial aid or guarantee does not exceed the financial means of the guarantor.

That assessment is fundamentally the responsibility of the management body which shall run an analysis of the risk / benefit ratio taking into consideration the granting of an arm's length guarantee fee or the benefit of an on-lending, the duration of the guarantee, its amount, the financial capabilities of the guarantor and the adequacy of the risks under the guarantee, the likelihood of the guarantee being called, the commercial benefit of the relationship between the borrower and the guarantor (...).

In the scenario of up-stream and cross-stream guarantees, in the case where the grantor is securing the obligation of third parties through the granting of rights *in rem*, it is commonly considered that the guarantee is commensurate to the financial capabilities of the guarantor as the guarantee is limited to a given asset, which does not mean that the guarantee necessarily falls within the corporate interest of the guarantor, but de facto limits its bearing. In the case where the grantor is securing the obligation of third parties through the granting of a personal guarantee, it is of common standard that such security is in principle unlimited, and for that reason it is customary that lenders' and borrowers' counsel agree on a suitable guarantee limitation language in order to limit the risk bearing on the Luxembourg obligor. The purpose of that clause is to limit the amount guaranteed by the guarantor to its predictable financial capabilities as of the date the guarantee is being granted and it thus traditionally takes the form of an adaptive limitation based on the higher of a contractually agreed percentage of the guarantor's owners' equity (*capitaux propres*) (i) as of the date of the granting of the guarantee and (ii) as of the date the guarantee is called, increased of any amounts owed by the guarantor to any other member of the group and that have not been financed (directly or indirectly) by a borrowing under the secured financing. The guarantee limitation language may become far more complex where several third parties' financing have to be taken into account.

The lack of corporate interest is certainly a risk for the guarantor and the members of its management body, but it is also a risk for the lenders as their security interest may in theory be invalidated and if they knew or could not ignore that the members of the management body where breaching their duties, the lenders may be held jointly liable for such breach.

Financial assistance

Prohibition of financial assistance in public limited companies has been introduced into Luxembourg law in transposition of the Directive 77/91/EEC (Article 23 of the Second Council Directive 77/91/EEC of 13 December 1976) implementing uniform capital maintenance rules for all public limited companies in the European Union. The prohibition has been softened through Directive 2006/68/EEC (Directive 2006/68/EEC of the European Parliament and of the Council of 6 September 2006) which inter alia introduced an exception regime (the **White Wash Proceeding**). The White Wash Proceeding is conducted under the responsibility of the management body and requires a careful assessment of the risk / benefit ratio for the company (please refer to our development under the Section Corporate interest above), based on a special auditor's report, approved by the shareholders' meeting and management report produced to the shareholders'

meeting is published in the Luxembourg official gazette. The White Wash Proceeding imposes that the net assets remains above the share capital and the unavailable reserves of the company and that a special reserve be booked as a liability in the balance sheet of the company, in the amount of the aggregate financial assistance provided by the company. In practice, those rules limit the circumstances where a public limited company may have recourse to a White Wash Proceeding to those companies largely financed through owners' equity other than share capital (eg share premium or special equity reserve contributions).

Traditionally, the prohibition of the financial assistance does not apply to private limited liability companies (*sociËtË ‡ responsabilitË limitËe*). However, following the amendments to the Companies Act of 2016, a doubt arose on this interpretation since the criminal law provisions of the Companies Act now incriminates managers who knowingly used funds of a private limited liability company to grant any kind of financial assistance with a view to acquiring the shares in the company (Article 1500–7 2∞ of the Companies Act).

Specific funds financing aspects

Each time an investment fund is a guarantor or otherwise an obligor in a financing transaction, particular care shall be given to the applicable regulatory framework in which the fund operates.

Certain regulatory regimes impose a limitation on leveraging investments, for example for Specialized Investment Funds (SIF) and Part II UCI, where the maximum level of leverage must be pre-approved by the CSSF, or for UCITs, where borrowings are strictly restricted to the financing of a redemption request from their investors or to the financing of real estate acquisitions essential to their business (in both cases, capped at 10% of their net assets, provided that the combination of those borrowings cannot together exceed 15% of their net assets).

Further, unregulated alternative investment funds within the meaning of the law of 12 July 2013 on alternative investment fund managers (the **AIFM Law**) managed by alternative investment fund managers operating under the specific regime provided for in article 3(2) of the AIFM Law and did not opt to be authorized on the basis of article 3(4) of the AIFM Law cannot be leveraged, and may exclusively have recourse to equity bridge financings.

Works council

Under Luxembourg law, a works council (*comitË mixte d'entreprise*) is required for any industrial, commercial or craft undertaking which had at least one hundred and fifty (150) regular employees over the past 3 years. The functioning of the works council is governed by articles L-421–1 ff. of the Luxembourg labour code (*Code du travail*).

If there is no specific provision requiring the entity's directors/managers to inform or consult the works council prior to granting a guarantee or security rights, a general provision requires the mandatory information and consultation of the works council as regards any economic or financial decision which may have a determining impact on the structure or the employment within the undertaking. Therefore, it may be possible that a transaction with an impact on the structure of the undertaking itself, requires the consultation of the works council, prior to any decision being taken. In case of consultation, the works council will provide advice (or several pieces of advice in the absence of agreement within the council) to the director or the board of managers/directors of the undertaking. The proceeding is not applicable should the company not be a stock company (*sociÈtÈ par actions*) and the director/manager has been present during the discussions. Then, such recipient shall make an informed decision as regards the works council's advice(s) and record its decision in the minutes.

Would there be any concerns in terms of validity or enforceability for an entity in your jurisdiction to grant an English law guarantee as typically included in syndicated loan agreements governed by English law?

In principle, an English law guarantee will be recognized and enforceable in Luxembourg under its terms, in accordance with the principles of the regulation (EU) No 1215/2012 of the European Parliament and of the Council of 12 December 2012 on jurisdiction and the recognition and enforcement of judgments in civil and commercial matters (the **Brussels I bis Regulation**) and the Rome I Regulation, unless such foreign law provisions are contrary to the Luxembourg overriding mandatory provisions (*lois de police*) or manifestly incompatible with Luxembourg public order (*ordre public*).

As such, the expressly agreed terms of such English law document may not be enforceable under Luxembourg law or before a court of competent jurisdiction in Luxembourg if and to the extent that their performance would be unlawful,

unenforceable or contrary to public policy. In general, it will be required that the relevant provisions are contrary to a matter of Luxembourg international public policy, ie embody the essentials of the country's moral, political or economic order, such as certain consumer code provisions (that cannot be waived or overridden by express contractual agreement), the appointment of a Luxembourg insolvency receiver or official in relation to the assets of a debtor located in Luxembourg or abroad, the use of a Luxembourg enforcement official for civil law security rights (ie no self-help enforcement), provisions on usury or contractual penalties or, subject to important exceptions, the equal treatment of creditors. The guarantee provisions customarily contained in the forms of facilities provided by the Loan Market Association do in practice raise limited reservations and are unlikely to be ruled as breaching Luxembourg international public policy rules.

Enforcement

When in your jurisdiction would a lender be entitled to enforce its security or guarantees?

Suretyships and mortgages can only be enforced upon the occurrence of a default of payment of the debtor of the secured obligation.

Autonomous guarantees, Professional Guarantee of Payment and any security right governed by the Collateral Act may in principle be enforced according to the terms of the agreement formalizing those security interests.

On 29 January 2014, the Luxembourg District Court sitting in commercial matters held that a secured creditor's right to enforce a pledge governed by the Collateral Act upon the occurrence of a default of payment at maturity is of the very essence of the pledge, irrespective of whether non-payment at maturity was expressly defined as an enforcement event and that any clause depriving a creditor of such right must be considered null and void. A recent decision of the Luxembourg Court of Appeal of January 2020 Court of Appeal of Luxembourg (4th Chamber) of 22 January 2020 (No CAL-2017–00004) reminds that the enforcement of a pledge, albeit unrelated to the default of payment of the secured debt, but due to the occurrence of a contractually determined enforcement event, as permitted by the Collateral Act, is not in itself fraudulent and does not constitute an abuse of right.

In brief, for each type of asset referred to above, what are the procedures for enforcing security and guarantees in your jurisdiction:

Inside insolvency

Luxembourg civil law security rights may be affected by the opening of insolvency proceedings against the pledgor. However, all security rights governed by the Collateral Act benefit from the utmost protection against Luxembourg or foreign insolvency proceedings, by application of Article 20(4) of the Collateral Act.

- Civil law rights:
    - Immoveable property

      Given that such security right is registered in a public register, a sole first ranking mortgagee may enforce by way of fast track based on the notarial deed (which constitutes an enforceable title (*titre exËcutoire*)), if the notarial deed provides that the mortgagee is authorised to sell the real property through a notary public without having to follow the statutory attachment procedure (*clause de voie parÈe*). In this case, the public auction may occur thirty (30) days after the summons to pay. If there is a dispute, the notary suspends all actions and brings the parties before the president of the competent court who will make a ruling in a summary proceeding (*procËdure de rËfËrË*).

      Under the statutory attachment procedure, a writ to attach (*exploit de saisie*) must be served by a process server/bailiff on the mortgagor fifteen (15) days after the summons to pay and must be registered where the mortgage was initially registered. Thereafter, the mortgagee must file an application for a hearing with the clerk of the competent court and have it served (through a process server/bailiff) on the mortgagor. The court assesses the validity of the attachment and appoints a notary public to organise and conduct a public auction. Following adjudication at the highest bid the proceeds are first paid to the notary up to the amount of its fee, then to other preferred creditors (such as preferred creditors by operation of law, eg the Luxembourg Treasury…) and then to the mortgagee.

Moreover, a Luxembourg bankruptcy receiver (*curateur*) may ask the court (with the intervention of the mortgagee and notification to the company and any other creditors) for authorisation to (i) proceed to foreclosure proceedings if no such proceedings were initiated by the mortgagee or (ii) order an end to any foreclosure proceedings already initiated by the mortgagee if that would be more beneficial to the estate (eg to avoid depreciation or to maximise the price), and to sell the property itself by public auction or private sale, distributing the proceeds to secured creditors in the order of their priority.

It should be noted that Luxembourg courts recently held that a mortgage validly constituted may be enforced in good faith notwithstanding a criminal freezing order (*saisie pËnale*) which would have occurred subsequently.

- Contractual rights, Plants and machinery, IP Rights

There is no need for lenders/creditors to act on their own behalf if a security agent has been appointed (where applicable). As a general rule, civil law security rights or mortgages may only be enforced after a prior summons to pay (mise en demeure) has been served on the debtor of the secured obligation (in the case of a mortgage, served by a process server/bailiff (huissier de justice)). Civil and commercial pledges over movables, including pledges in respect of intellectual property rights, that have been perfected by delivery of collateral to the pledgee are enforced either by judicial attribution (following valuation by a court-appointed independent expert) or, more typically, through public auction in accordance with Articles 116 to 119 of the Luxembourg commercial code and, in the case of mortgages, Articles 809 ff. of the Luxembourg new code of civil procedure, and satisfaction from the proceeds of sale, but not through self-help appropriation, which would constitute a forbidden *pacte commissoire or clause de voie parÈe*.

A public auction of collateral subject to a civil law pledge may be made at a stock exchange (in the case of unlisted financial instruments, eg commercial papers...) or outside the stock exchange, in each case under the supervision of a public officer (such as a notary, a bailiff or a clerk) designated by the competent court. Sales have to be made in cash, therefore it is not possible, for example, for lenders to bid their credit. A public auction at and by the Luxembourg Stock Exchange (**LxSE**) is made at a date and time published by the LxSE.

- Security rights governed by the Collateral Act
  - Shares and debt securities

The Collateral Act provides a number of enforcement remedies that may be varied by agreement. As such, the Pledgee may, unless otherwise agreed, without prior summons to pay:

- *appropriate the collateral (without court intervention)*

The appropriation is by far the most efficient and generally preferred manner of enforcement of pledge over nominative securities and generally is the preference of the secured parties.

The appropriation method allows the pledgee to enforce the pledge without court intervention, subject to the existence of an agreed valuation method. Contrary to the judicial attribution under civil law, the expert or financial advisor who values the collateral in accordance with the agreed valuation method, may not be approved by a Luxembourg court but is designated by the parties in accordance with the terms of the security agreement.

Subject to any delays due to the need for a valuation (which will depend on the existence of an agreed valuation method and on the diligence of the appointed expert) and assuming no provisional measures will be permitted by a competent court, which is unlikely in the current state of Luxembourg law, appropriation can happen relatively quickly in accordance with the terms of the pledge agreement.

A recent decision of the Luxembourg Court of Appeal of January 2020 (Court of Appeal of Luxembourg (4th Chamber) of 22 January 2020 (No CAL-2017–00004)) reminds that a bad valuation is not likely to lead to the cancellation of the enforcement of the pledge, but at most may engage the creditor's liability for fault.

Also, the realisation of a pledge, albeit for purposes unrelated to the payment of the secured debt, but due to the occurrence of a contractually determined event, as permitted by the Collateral Act, is not in itself fraudulent and does not constitute an abuse of right.

Further to the appropriation, the pledgee (or any other person designated by it, such as a special purpose vehicle) will become the direct owner of the shares of the company. It should be verified whether such appropriation cause(s) any tax, accounting or regulatory issues for the pledgee.

- *sell at a private sale*

  The only requirement for a private sale is that it must be made on 'normal commercial terms' (*conditions commerciales normales*), meaning in a commercially reasonable manner (without which any aggrieved party is entitled to a claim for damages), in a sale organised by a stock exchange (to be chosen by the pledgee) or in a public sale (organised at the discretion of the pledgee and which, for the avoidance of doubt, does not need to be made by or within a stock exchange), subject only to an ex-post control by the courts in relation to the assessment of the 'commercially reasonable' realisation or valuation of the collateral.

  There is little guidance as to what the expression 'normal commercial terms' means. It is common practice to refer to the market value of the collateral at the time of the sale. The purpose of the rule is the protection of the pledgor against an arbitrary sale by the pledgee, at an undervalue. Once an enforcement strategy has been decided, a detailed analysis should be undertaken in order to verify if the private sale can be characterised as occurring on normal commercial terms. For the avoidance of doubt, it is normally recommended to carry out a sale by cash consideration, as opposed to credit bidding or giving in payment, because the law requires a 'sale'.

- *sell at a public auction*

  In general, if the parties have agreed on a public auction of the collateral, unless provided otherwise, the auction shall be effective at and by the LxSE at a date and time published by the LxSE. According to the regulations of the LxSE, all sales have to be made in cash. A public auction may also be made outside a stock exchange under the supervision of a public officer.

- *sell on the stock exchange*

  In the case of collateral admitted to the official list of a stock exchange located in Luxembourg or abroad, or if it is traded on a regulated market functioning regularly, recognised and open to the public, appropriate the collateral at its trading price

- *judicial attribution*

  The pledgee may request a judicial decision attributing the collateral to the pledgee in discharge of the secured liabilities following a valuation of the collateral made by a court appointed expert (*attribution judiciaire*).

  On 27 January 2016 the Luxembourg court of appeal held that, although the Collateral Act does not preclude a judge hearing summary proceedings from taking urgent measures, such measures cannot render inoperative the provisions under which the enforcement of the pledge agreement and the fulfilment of the obligations undertaken by the parties under those contracts is ongoing, notwithstanding any other kind of coercive measures provided for in the Collateral Act.

◦ Bank accounts

Upon the occurrence of an enforcement event, the account pledge will, unless agreed to the contrary, become immediately enforceable and the pledgee may thereupon immediately exercise any or all of its rights and powers of execution, realisation and foreclosure under the pledge agreement or otherwise provided by law. In particular,

it may give instruction to the account bank with which the cash account is maintained to pay to the pledgee the amount it has indicated for setting-off against the secured obligations.

- Receivables

  If the collateral is a receivable, the pledgee may provide notification upon an enforcement event and instruct the debtor of the receivable to make payment directly to the pledgee (whether or not the pledgor was making collections on the receivable before such notification and instruction) to apply any money paid to the pledgee to its satisfaction and set-off against all or any part of the secured obligations.

  On 12 July 2017 the Luxembourg District Court sitting in commercial matters broadened the scope of enforcement triggering events under a Luxembourg receivables pledge. In the case at hand, despite the breach of the Real Financial Leverage (RFL) contained in the bond documentation, the lenders did not call for an early termination of the senior bonds or declare their early maturity, but instead enforced the pledges. The Court held that the non-compliance with the RFL constitutes, in the same way as a default equivalent to a non-satisfaction of the guaranteed obligation, a case of valid enforcement even if the claim is not due.

- **Outside insolvency**

Outside insolvency, security rights will usually be enforceable in accordance with their terms, depending on the definition given to an enforcement event, justifying the enforcement of the security right. It is however necessary to ensure that the provisions allowing enforcement do not give an arbitrary power to one of the parties that is disproportionate, otherwise a Luxembourg court may consider such provision to be abusive and therefore inapplicable.

Intercreditor issues

In brief, how will security interests over the same asset (where the priority is not contractually regulated) rank as against each other in your jurisdiction?

Luxembourg law grants certain preferential liens on moveable assets of debtors in favour of Luxembourg tax authorities and social security institutions, as well as employees in respect of their claims (if any). Those privileges may take precedence over the rights of other secured or unsecured creditors. The priority of competing secured creditors in respect of the same collateral will be determined by the type of asset and type of security right.

Unsecured creditors rank pari passu unless a contractual subordination has been agreed upon.

- **Civil law rights**

  Although not explicitly recognised in the LCC, rules similar to the priority rules under the Collateral Act are used in practice for civil law security rights such as pledges over IP rights or over moveable assets.

  If the security is a civil law pledge, then the time of delivery, registration or notification of the debtor, as applicable, will determine the priority of the secured creditor ('first-to-file' or 'first-in-time'). If there is no possibility to determine the date on which the security has attached, then the competing creditors will be considered as equally secured. If competing creditors that are equally secured enforce simultaneously, the proceeds of realisation will be distributed proportionally to the amount of each secured creditor's outstanding claim.

- **Security Rights under the Collateral Act**

  Under the Collateral Act, only pledges will be affected by ranking issues, given that a transfer of title for security purposes precludes any conflict between competing secured creditors.

  Under a pledge over registered securities, the time of registration of the pledge in the relevant securities register of the issuer determines the priority of the pledge over the issuer's securities without the need to involve any competing creditors.

In respect of collateral consisting of claims resulting from a receivable, the mere execution of the security agreement perfects the pledge as against the debtor under the receivable, as applicable, but priority is contingent on the acknowledgement of the security by any existing competing creditor.

Under a pledge over financial instruments, the priority of a secured creditor will be determined in accordance with the perfection steps set out above. The priority of a competing pledgee in respect of the same financial instruments is determined in accordance with the following perfection steps, which depend on the type of financial instruments:

- in the case of a pledge over book entry securities:
  - by the approval of the pledgee of higher priority, if the relevant bank account is held in the name of the pledgor;
  - if the relevant account is held in the name of a pledgee of higher priority, by the approval of such pledgee and of any other pledgee of a higher priority;
  - if the relevant account is held in the name of a third party (*tierce personne*), by the agreement of such third party to act as an agreed third party custodian (*tiers convenu*) and the approval of every pledgee with a higher priority.
- in the case of a pledge over securities in bearer form:
  - if the relevant securities were delivered to a pledgee, by its approval to act as an agreed third party and the approval of any other pledgee of a higher priority;
  - if the relevant securities were delivered to an agreed third party, by its approval and the approval of every pledgee with a higher priority.

- in the case of a pledge over registered financial instruments (*instruments financiers nominatifs*), by the time of registration in the relevant register of the issuer.
- in the case of a pledge over order instruments (*billet ‡ ordre*), by a regular endorsement with the indication that the qualifying collateral was pledged in favour of a pledgee with a lower priority.
- in the case of a pledge over other financial instruments, by the express approval or notification to the issuer of the relevant financial instruments, or any third party depositary and the approval of every pledgee of a higher priority.
- in the case of a pledge over receivables, by the approval of every pledgee of higher priority; the debtor of the secured claim may validly discharge its obligations towards the pledgor or any existing pledgee if it was not aware of the constitution of a new security right.

In the case of enforcement, the priority of competing pledgees is implemented as follows (subject to the terms of any relevant intercreditor agreement):

- Where the most senior pledgee(s) realize(s) upon the collateral, any surplus will be held by an agreed third party custodian, acting for the account of pledgee(s) of lower priority. Where the most senior pledgee acted as the agreed third party custodian, it may continue to do so or else remit the surplus to the other pledgees in order of their agreed priority. In the absence of an agreed priority, the most senior pledgee will appoint a Luxembourg credit institution as receiver (*sÈquestre*) and remit the surplus to it for the benefit of the secured creditors of lower priority.
- Where a junior pledgee realizes upon the collateral, enforcement must occur in accordance with the agreed enforcement method and the proceeds must be applied in accordance with the agreed order of priority. In the absence of an intercreditor agreement, the most diligent pledgee (in practice, the first to act) may request provisional measures (*rËfËrË*) from the president of the Luxembourg district court to settle the issue. The competing pledgees are entitled to apply for appeal against the provisional measure. A junior pledgee acting in good faith who ignores

the existence of a competing pledgee with higher priority is entitled (i) to retain the enforcement proceeds up to the amount of its secured obligation and (ii) to remit any surplus to the pledgor, in each case without incurring any liability..

What method(s) of subordination are commonly used in your jurisdiction?

Except as between securitization companies and its creditors and investors, Luxembourg law does not regulate contractual subordination. There exists very limited case law in Luxembourg in relation to the recognition of contractual subordination provisions.

Investors using Luxembourg securitization vehicles and requiring the benefit of security rights may also need to appoint a security representative. Under the Luxembourg Act of 22 March 2004 on securitization, as amended (the **Securitization Act**), a Luxembourg securitization vehicle may grant a security right over its own assets exclusively to secure its obligations under the issued securities for the benefit of the investors, their fiduciary security representatives (*reprÈsentants-fiduciaires*) or the issuing vehicle (if assets are held by an acquisition vehicle).

Under the Securitization Act, investors in a securitization vehicle acting as secured creditors may appoint a security representative as a fiduciary (*fiduciaire*) under the Fiduciary Contracts Act, to represent their interests in security rights or receive payments. The powers, rights and duties of such fiduciary are normally determined by the investors as secured creditors at the time of its appointment, in accordance with the provisions of the Fiduciary Contracts Act. A fiduciary security representative for the purposes of the Securitization Act, whose statutory seat is in Luxembourg, must be approved by the Minister of Finance and is subject to specific requirements (including without limitation its share capital and its shareholder structure). An appointment may also result from the subscription to additional securities issued by the securitization vehicle, where contemplated by the terms and conditions of the securities. For a security representative whose statutory seat is located outside Luxembourg, a general distinction must be made between security rights covering qualifying collateral under the Collateral Act and civil law security rights (please refer to our explanations above).

Subject to any statutory claims of preferential rights (see above), subordinated creditors rank in accordance with the priority agreed in the relevant subordination agreement. Subordination clauses can be specific (for example, limited to a defined operation) or general. In general subordination clauses, the subordinated creditor accepts that, if the debtor becomes insolvent, or is liquidated, its claim is paid after all other creditors have been paid. Such a clause does not prevent the creditor from being paid when the debt becomes due and payable.

The Luxembourg Court of Appeal recently emphasised the main principles applicable to the validity and enforceability of subordination clauses.

Subordination clauses must comply with the general law on validity of contracts. There is very limited case law in Luxembourg in relation to the recognition of voluntary subordination provisions. If a Luxembourg court were to analyse the validity and enforceability of voluntary subordination provisions, it is in our view likely that it would consider the position taken by Belgian legal scholars and more recently by Luxembourg legal scholars based on (limited) Luxembourg court precedent, according to which voluntary subordination provisions are legal, valid and enforceable against the parties thereto, including in case of bankruptcy of such parties, but may not be enforceable against third parties which are not party to the relevant agreement.

Will local courts in your jurisdiction give effect to the contractual terms of an English law governed intercreditor agreement (which may include limitations on enforcement, rights to receive payment and turnover clauses). Would an English law governed intercreditor agreement survive the insolvency of a borrower incorporated in your jurisdiction?

A court of competent jurisdiction in Luxembourg may not apply the chosen English law if such choice is abusive and/or if such foreign law provisions would be manifestly incompatible with the public policy rules (*ordre public*) of Luxembourg.

Generally however, in the case of bankruptcy, the bankruptcy receiver does terminate all existing agreements.

Governing law and disputes

Will a choice of English law as the governing law of the documents and the English courts as the jurisdiction for disputes be upheld in your jurisdiction? Would a judgment given by the courts of England and Wales be enforceable in your jurisdiction without a retrial of the merits of the case?

As a matter of Luxembourg law, there is no obligation to submit the security agency/intercreditor agreement to Luxembourg law.

In application of Article 3 of the Rome I Regulation, the choice of a foreign law as the governing law of the security agency agreement is legal, valid, binding and enforceable against the Luxembourg obligors, and will be recognized and given effect to by a court of competent jurisdiction in Luxembourg, except where Luxembourg courts consider the choice of the foreign law to be contrary to Luxembourg international public policy rules (please refer to our explanations above).

As regards the choice of jurisdiction, the submission to the jurisdiction of the courts of England is legal, valid, binding and enforceable against any Luxembourg obligor and will be recognized and given effect to by a court of competent jurisdiction in Luxembourg in accordance with and subject to the provisions of the Brussels I bis Regulation.

A court of competent jurisdiction in Luxembourg may stay proceedings if concurrent proceedings involving the same parties and the same cause of action have been brought in another court of competent jurisdiction (whether or not covered by the Brussels I bis Regulation) and will decline jurisdiction in favour of that court if its jurisdiction is validly established.

The formal enforcement of a foreign decision may be obtained by submitting a motion for exequatur to the president of the competent Luxembourg district court. The following evidence must be attached to the motion:

- the original or certified true copy of the court decision, translated into French;
- the original or certified true copy of the formal service of process to the parties involved, translated into French;
- a certificate from the court, establishing that no recourse or appeal lies from the court decision (ie a certificate demonstrating that the decision is final and conclusive), translated into French.

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