

3.23 ROMANIA

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I. FRAMEWORK

In Romania, the legal basis for Covered Bond issuance is the Mortgage Bonds Law from March 2006. This law supersedes the general bankruptcy regulation.

The legal framework for covered bonds is currently under revision in Romania. Below we will refer also to some important issues which will be amended.

II. STRUCTURE OF THE ISSUER

The issuer can be only a credit institution (as defined by Romanian Banking Law which is in line with the EU Directive). Therefore, all commercial or mortgage banks may be an issuer and no other special covered bond license is required.

Mortgage banks are credit institutions, but their licensing is limited since these types of credit institutions are not allowed to receive deposits. The National Bank has not yet issued the set of applicable regulations for mortgage banks. Up to date no mortgage bank as such is incorporated under Romanian Law.

Pursuant to the Mortgage Bonds Law, the issuer holds the assets on its balance sheet. The covered bond issuer holds the ownership title over the portfolio. A direct legal link between single cover assets and covered bonds does not exist. All obligations from bonds are obligations of the issuing bank as a whole. However, under the current law there is a legal link between each bond issue and its pool of cover assets. In the event of insolvency, the cover pool is segregated by law from the general insolvency estate and is reserved for the claims of holders of the specific bond issue.

Assets servicing may be outsourced, but for covered bonds it is expressly regulated only in case of issuer's bankruptcy.

The covered bonds are direct and unconditional obligations of the issuer. The claims of the holders of covered bonds are secured by a first rank security interest over the cover assets, which are segregated in bankruptcy. Each bond issue is guaranteed by a distinct pool of assets. In the event of bankruptcy, the bonds holders in a specific issue will have first priority over the pool of assets dedicated to the specific issue.

This legislative provision regarding separate cover pools for each covered bond issue will be set aside in the projected new Romanian covered bond legal framework, which is currently under preparation in Romania.

III. COVER ASSETS

In the case of covered bonds structured under the Mortgage Bonds Law, only mortgage loans (i.e. residential or commercial mortgage loans) can be included in the cover pool. The cover pool could be replenished with other mortgage loans if some of the pledged loans don't fulfil the eligibility criteria anymore. Other eligible assets (besides mortgage loans) will only be used for supplementing the cover pool if the issuer has no other mortgage loans that could be used for such a purpose. The list of these other eligible assets which can be included in a cover pool is to be established by the National Bank.

In terms of derivatives allowed to be included in the cover pool, no special provisions are contained in this respect in the Mortgage Bonds Law. However, the National Bank is entitled to regulate the categories of eligible assets that can be used for supplementing the cover pool in case the issuer has no other mortgage loans. The only restriction in this respect imposed by the Mortgage Bonds Law stipulates that the general maximum ratio allowed for supplementing the portfolio and the substitution of the mortgage loans in a cover pool with eligible assets may not exceed 20% of the portfolio value.

The mortgage loans must fulfil several eligibility or performance criteria imposed by the Mortgage Bonds Law in order to be included in the cover pool:

- a. the pool is homogenous comprising of only one type of mortgage loan according to its investment destination;
- b. the weighted average of the maturities of the mortgage loans included in the cover pool securing an issue is higher than the maturity of the mortgage bonds secured by such a cover pool; the weighted average of maturities shall be calculated by weighting the outstanding life time of the loans included in the cover pool with the nominal value of the loan as at the date of issue;
- c. the updated value of mortgage loans securing an issue of mortgage bonds has to be at least equal with the updated value of the payment obligations of the issuer towards the bondholders;
- d. the aggregated value of the mortgage loans secured with mortgages on properties with no constructions built on them and of those secured with mortgages on immovable assets in the process of being built does not exceed 20% of the value of the portfolio;
- e. each mortgage loan in the cover pool meets the general eligibility criteria provided by this law and the performing criteria established through the prospectus;
- f. the nominal value of a mortgage loan does not to exceed, in case of a residential mortgage loan, 80% of the reference value of the immovable asset over which the security interest was created and, in case of a commercial mortgage loan, 70% of the reference value of the immovable asset over which the security interest was created;
- g. the amount representing the principal granted through a mortgage loan agreement has been fully disbursed to the beneficiary;
- h. the amount granted to a single beneficiary or to a single beneficiary and all affiliated persons of the beneficiary does not exceed 10% of the value of the cover pool;
- i. the receivables deriving from the mortgage loans are not subject to a security interest in favor of any other person;
- j. the mortgage loan must not register delayed payments exceeding 61 days;
- k. the real estate over which a security has been created for the reimbursement of the mortgage loan is insured against all risks for an amount equal with the reference value of the immovable established on the date of the mortgage agreement;

In terms of geographical coverage, the sole restriction imposed under the Mortgage Bonds Law, provides that, in order to be included in the cover pool, the mortgage loans were granted for real estate investments on the territory of Romania or on the territory of member states of the European Union or the European Economic Area.

The Mortgage Bonds Law generally stipulates that the cover pool is static. The replacement of the mortgage loans included in the cover pool is prescribed as an obligation only when certain mortgage loans no longer comply with the eligibility criteria, have become non-performing in the meaning of this law or determine the reduction of the weighted average of the maturities of the mortgage loans included in the cover pool, of the value of the mortgage loans included in the pool or of the interest amount, according to the limits provided by law.

In the projected new Romanian covered bond legal framework it will be possible to have only two cover pools (a mortgage cover pool and a public cover pool), which will be dynamic.

Regarding the **disclosure requirements**, detailed information concerning the assets included in the cover pool has to be provided in the offering circular, such as: the value of the mortgage loans included in the cover pool; the reference value of the collateral created for the reimbursement of the mortgage loans as established at the conclusion of the collateral agreement against the nominal value of the issue; the interest coverage provided by the cover pool; geographical dispersion of the mortgage loans, maturity, interest, interest computational method and payment schedule as well as prepayment conditions under the respective mortgage loans.

The internal cover register shall contain detailed information on the cover pool and a separate section for registering the substitute assets included in the cover pool. The internal cover register shall be kept and filled in by the issuer with respect to any amendments or changes to the data since the initial registration.

IV. VALUATION AND LTV CRITERIA

Property valuation is regulated and is required to be undertaken by an authorized real estate appraiser. The reference for a property value is considered to be the market value as opposed to the mortgage lending value. Details about the valuation process and the qualifications of valuers are regulated by the Romanian Association of Evaluators (ANEVAR). The legal framework does not incorporate any special monitoring requirement.

The Mortgage Bonds Law stipulates limits for maximum LTVs on both commercial and residential loans at 70% and 80%, respectively. *These are absolute LTVs referring to the loans granted. No provision is made regarding a relative limit. The new Romanian covered bond legal framework will introduce a lending limit of 60%, so that mortgages may be used as cover only up to the first 60% of the value of the property*

V. ASSET - LIABILITY MANAGEMENT

The Mortgage Bonds Law stipulates that the net present value of the outstanding bonds must be covered at all times by the net present value of the assets and that the weighted average term to maturity of the assets should be higher than the bonds' maturity. The issuer can provide overcollateralization up to a maximum ratio of 20% of the cover pool value.

If any of these limits are breached, the bondholders may request that the bonds are immediately repaid, unless the breach is redressed within 30 days.

The new Romanian covered bond legal framework will introduce details about the calculation of a stress-tested NPV, the liquidity needed and hedging with derivatives.

VI. COVER POOL MONITOR AND BANKING SUPERVISION

Under the Mortgage Bonds Law, the activity of a mortgage bond issuer is monitored by the National Securities Commission (CNVM) and the National Bank (BNR). For mortgage bonds, the law provides for the mandatory appointment of an agent. The agents have to be authorised jointly by the National Securities Commission and by the National Bank. Initially, the agent shall be appointed by the issuer from a list of agents, approved by the National Bank (mandatory pre-requisite for the issuance of mortgage bonds). Upon subscription of the mortgage bonds by the investors, the revocation/appointment of the agent shall be made exclusively by the general meeting of bondholders.

The agent's main role is to monitor the cover pool on behalf of the bondholders. Its monitoring obligations shall be performed on a monthly basis, based on the synthetic documentation provided by the issuer. The agent has to observe issuer's compliance with the law and prospectus requirements. Based on the documentation provided by the issuer, the agent shall issue a certificate attesting the issuer's compliance with the provisions of the law and with the offering curricular regarding the cover pool structure. The agent shall be jointly and severally liable towards the bondholders with the issuer, with the financial investment services company handling the sale and with the issuer's financial auditor for the damages caused by non-fulfilment of several duties provided for under the law (including the obligation to monitor the issuer's compliance with the requirements related to the cover pool).

The qualification, role and duties of the agent will be clarified in the new Romanian covered bond legal framework.

VII. HOW ARE SEGREGATION OF COVER ASSETS AND BANKRUPTCY REMOTENESS OF COVERED BONDS REGULATED?

A cover register allows for the identification of the cover assets for each issue. The issuer has the obligation to keep a cover register for each mortgage bond issue.

Registration in the cover register reflects the structure and dynamic of the portfolio at any time throughout the life of the issue. The cover register contains information with respect to each mortgage loan included in the cover pool (i.e. type: commercial or residential, beneficiary of the loan, immovable asset over which the security for reimbursement of the mortgage loan has been created, land book number, value of the mortgage loan and reference value of the immovable asset, any other collateral and its nominal value) and substitute assets.

Registration in the cover register triggers an obligation for the issuer to have a security interest, which is registered with the Electronic Archive and covers each and all assets registered in the register. These assets are specifically registered in the accounting books of the issuer and segregated from the estate of the issuer in the event of bankruptcy. The cover register is kept by the issuer and subject to checks by the agent and supervision by the National Bank of Romania.

Asset segregation

By registration of the security interest over the pledged cover assets and the entry into the internal cover register of the mortgage loans or other assets included in the cover pool, such assets are segregated from the other assets of the issuer. The segregation of the cover assets from the insolvent estate of the issuer is thus a consequence of a contractual pledge and the operation of the law.

After the launching of the insolvency proceedings, a special portfolio management company carries out the administration of the cover assets. The appointment of the cover pool manager is made by the general meeting of bondholders.

Impact of insolvency proceedings on covered bonds and derivatives

Mortgage bonds do not automatically accelerate when the issuing institution becomes insolvent, but the bondholders could be obliged to accept payments in advance, with the corresponding recalculation of their rights if the cash-flows in the cover pool allows that.

The new Romanian covered bond legal framework will clarify the asset segregation provisions, set aside the de facto acceleration provision and will also clarify the regime of derivatives registered in the cover register.

Preferential treatment of covered bond holders

Mortgage bond holders enjoy preferential treatment as the law stipulates the separation of the cover assets from the insolvent issuer's estate.

In the event that the cover assets of a specific issue are not sufficient to cover the payments of that issue, the Mortgage Bonds Law provides for a cross-subsidy principle amongst different issues of cover bonds of the respective issuer if there is a surplus after payment of all the obligations towards the bondholders in a specific issue. If the cover assets are not sufficient, the bondholders have an unsecured claim towards the bankrupt estate for the difference.

A moratorium on the insolvent issuer's estate cannot delay the cash flows from the cover assets and, therefore, endanger the timely payment of covered bond holders.

A special insolvency procedure could be commenced against the cover pool only by the bondholders.

Access to liquidity in case of insolvency

After bankruptcy proceedings are opened, with the appointment of an asset management company as the cover pool administrator, the right to manage and dispose of the recorded assets is transferred to this company by law. Thus, the cover pool manager first has access to the cover assets and collects the cash flows according to their contractual maturity and pays the amounts due by the issuer to the bondholders.

There are no specific regulations expressly addressing the issue of voluntary overcollateralisation in insolvency. It may be argued that voluntary overcollateralisation is part of the cover pool with all legal consequences regarding segregation in the event of bankruptcy applicable to the respective pool.

Sale and transfer of mortgage assets to other issuers

A bankrupt issuer cannot be liquidated until it has assigned the cover pool to another issuer. The portfolio of assets may be sold to other issuers in a transaction concluded after the launching of the bankruptcy proceedings if the liquidator's report provides the sources from which the insolvent issuer may pay in full the amounts due to the bondholders and if the bondholders in each issue (if more than one) have decided in the general meeting of bondholders to accept payment in advance under the terms provided in the liquidator's report.

VIII. RISK-WEIGHTING & COMPLIANCE WITH EUROPEAN LEGISLATION

The covered bonds issued under the Mortgage Bonds Law fulfil the UCITS 52(4) criteria. The law requires such bonds to be issued by a credit institution, which is subject by law to special public supervision designed to protect bondholders (i.e. supervision by the National Bank of Romania and respectively by the National Securities Commission) and provides coverage by law of the claims attaching to the bonds in the event of failure of the issuer, on a first priority basis for the reimbursement of the principal and payment of the accrued interest.

Covered bonds under the Mortgage Bonds Law also comply with the CRD Directive Annex VI, Part 1, Paragraph 68 a) to f). Therefore they should enjoy a 10% risk weighting.