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I. FRAMEWORK

In Romania the legal basis for covered bond issuance is the Mortgage Covered Bonds Law No. 304/2015 (the "Covered Bonds Law" or the "Mortgage Covered Bonds Law") and the National Bank of Romania's Regulation nr. 1/2016 regarding the issuance of covered bonds. This law replaced the Mortgage Covered Bonds Law Nr. 32/2006 and supersedes the general bankruptcy regulation.

Since the implementation of the Mortgage Covered Bonds Law, no covered bonds have been issued by a local issuer.

II. STRUCTURE OF THE ISSUER

The issuer can only be a credit institution (as defined by Romanian Banking Law, which is in line with the EU legislation). Therefore, all commercial, mortgage banks or cooperative credit organisations may be issuers.

The issuer must obtain an issuance approval from the National Bank of Romania (Art. 4 CB Law). The issuance approval is valid for 15 months and within this timeframe and the approved issuance framework, the issuer has the possibility to make more subscription offers (Art. 7(2) of the BNR Regulation 1/2016). The conditions for the approval of an issuance framework are set in art. 3-9 BNR Regulation 1/2016. The Central Bank is supervising the covered bond issuance activity for fulfilment of the prudential requirements.

Pursuant to the Mortgage Covered 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. 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 the 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 from the rest of the issuing bank's patrimony, in case of bankruptcy. *The legislative provisions in the former Mortgage Covered Bonds Law regarding separate cover pools for each covered bond issue were set aside in the amended Romanian covered bond legal framework*. Real estate receivables, other financial assets and financial derivatives securing the mortgage bonds are structured by the issuer into a single cover pool.

III. COVER ASSETS

The covered bonds issued under the Mortgage Covered Bonds Law can include mainly mortgage loans (i.e. residential or commercial mortgage loans) in the cover pool and, in a smaller proportion, other eligible financial assets. The cover pool must 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 be used for the substitution of the assets included in the cover pool only if the issuer has no other mortgage loans that could be used for such purpose. The list of these other eligible assets which can be included in a cover pool is established by the National Bank.

The issuer can include in the cover pool, apart from real estate receivables, other financial assets and, subject to conditions set out in art. 14 and art. 18 (8) of the Mortgage Covered Bonds Law, also financial derivatives. Derivatives can be included in the cover pool only for the purpose of hedging interest rate risk and foreign currency risk. Financial derivatives may be included in the cover pool only if the agreements related thereto do not contain a clause according to which the bankruptcy or the resolution of the issuer is deemed to be a termination event. The general regulation issued by the National Bank has further details in art. 31 on the conditions which have to be fulfilled by the derivatives included in the cover pool.

The Mortgage Covered Bonds Law stipulates in art. 18 that the mortgage loans must fulfil several eligibility or performance criteria in order to be included in the cover pool:

> The funds under the mortgage loans have been made available in full to the beneficiaries of the respective loans;

> The mortgage loans have been granted for real estate investment purposes in Romania or in the European Union or European Economic Area member states, or for real estate investment purposes in third countries. However, in the latter case, the threshold of real estate receivables which can be included in the cover pool cannot exceed 10% of the real estate receivables included in the pool;

> The relevant real estate receivables should not be subject to any mortgage or legal or contractual privilege;

> The rights *in rem* created to secure the repayment of the real estate receivables have been created solely in favour of the issuer;

> The mortgaged real estate must hold an all-risk insurance for an amount at least equal to the market value of the real estate as of the execution/renewal of the insurance policy, the rights under the insurance agreement have been assigned in favour of the issuer and the insurance has been maintained valid throughout the secured period of the mortgage bonds issues;

> At the time of its inclusion in the cover pool, each real estate receivable must not incur delayed payments, and subsequently, it should not record a delay in payment of more than 15 days throughout the validity of the cover pool;

> The debtor under such receivable must have been notified, pursuant to the provisions of art. 10 par. (1) of the Law, that the receivable the issuer held against it is to be included in the cover pool which will serve as security for the issuance of mortgage bonds;

> The debtor of the relevant receivable has not notified its failure to waive the right to claim compensation against the issuer, according to art. 10 par (2) of the Law;

> Throughout their inclusion in the cover pool, the receivables must comply with any potential additional eligibility conditions provided in the prospectus or, as applicable, in the offering document attesting the conditions of the issue.

> The cover pool shall include the mortgage loans for which the ratio, determined at the date each loan is granted, between the nominal value of each loan and the reference value of the real property serving as security is not in excess of 80% for the residential real estate loans and of 60% for other real estate loans.

> The value of real estate receivables secured with mortgages over land without buildings and of those secured with mortgages over real property under construction cannot exceed the threshold established by the National Bank of Romania in its relevant regulations.

> The value of the receivables against a single debtor, itself or together with the value of the receivables against its affiliated persons, must not exceed the threshold established by the National Bank of Romania in its relevant regulations.

> Re-evaluation of immovable properties securing real estate receivables included in the cover pool is made in accordance with art. 208 par. (3) of the Regulation (EU) no. 575/2013.

> Financial derivatives may be included in the cover pool only if the agreements related thereto do not contain a clause according to which the bankruptcy or the resolution of the issuer is deemed to be a termination event.

> Issuers may establish additional eligibility conditions in their internal regulations, stricter than those specified in par. (1) to (8) of the CB Law and will be made public through the prospectus or, as applicable, are mentioned in the offering document attesting the conditions of the issue.

The Mortgage Covered Bonds Law stipulates that the **cover pool is dynamic**. The replacement/supplementation of the mortgage loans included in the cover pool is compulsory when certain mortgage loans no longer comply with the eligibility criteria, have become non-performing in the meaning of the CB Law, the weighted average maturities of the mortgage loans included in the cover pool decreases below the weighted average maturities of the corresponding covered bonds, the value of the mortgage loans included in the pool or of the interest amount diminishes below the thresholds provided by the CB Law (art. 13 and 16 of the CB Law).

IV. VALUATION AND LTV CRITERIA

Property valuation is regulated and is required to be undertaken by an authorised real estate appraiser. Details about the valuation process and the qualifications of evaluators are regulated by the Romanian Association of Evaluators (ANEVAR). Re-evaluation of immovable properties securing real estate receivables included in the cover pool is made in accordance with art. 208 par. (3) of the Regulation (EU) no. 575/2013. The trustee will check the fulfilment of this issuer's obligation.

V. ASSET – LIABILITY MANAGEMENT

The Mortgage Covered 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. The new Law stipulates in art. 13 a minimum of 2% as overcollateralisation.

VI. TRANSPARENCY

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 separate sections for registering the substitute assets, other eligible assets and derivatives 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.

Issuers shall prepare and publish on their own websites quarterly reports, no later than the 15th day of the month following the end of the quarter for which they are drafted, as regards the risks related to the cover pool, the total volume of the issued mortgage bonds and the structure of the cover pool, including the nominal value of the receivables in the pool, their residual value and the structure of the maturities of the receivables in the pool.

VII. COVER POOL MONITOR AND BANKING SUPERVISION

Under the Mortgage Covered Bonds Law, the activity of a mortgage bond issuer is monitored by the Romanian National Bank ("BNR"). For mortgage covered bonds, the law provides for the mandatory appointment of an agent, as independent auditor of the cover pool. The agent has to be authorised by the Romanian 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).

The agent's main role is to monitor the cover pool, to certify the issuer's reports to BNR and to report itself its findings on the observance of the legal requirements to BNR. 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).

Besides the agent, a representative of the covered bond holders must be appointed by the bondholders in the first covered bond holders meeting, his role being to exercise, on its own name, but on the account of bondholders, the bondholders' rights, except for the voting rights.

VIII. SEGREGATION OF COVER ASSETS AND BANKRUPTCY REMOTENESS OF COVERED BONDS

The issuer has the obligation to keep a **cover register**, which allows for the identification of the cover assets. 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.

The receivables included in the cover pool are mortgaged by the issuer to the agent acting on behalf of the bondholders, under a movable mortgage agreement to be attached to the prospectus or to the offering document. The movable mortgage over the receivables must be registered (by means of a global registration notice) in the Electronic Archive for Security Interests in Movable Property, on the name of the agent and on behalf of the bondholders. This mortgage comprises each and all assets registered in the cover register. After the appointment of the bondholders' representative, the mortgage over the pool of assets is transferred on its name.

These assets are specifically registered (separately) in the accounting books of the issuer and segregated from the estate of the issuer in the event of bankruptcy (Art. 29 CB Law). Publicity formalities with the land book of the relevant real estate properties are not necessary (Art. 29(5) CB Law). 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 movable mortgage over the 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. In case of issuer's bankruptcy, the segregation of the cover assets from the insolvent estate of the issuer is thus a consequence of the movable mortgage over the cover assets and the operation of the CB Law.

In order to fulfil all the obligations of the issuer towards bondholders under the CB Law and under the prospectus, or, as applicable, the offering document attesting the conditions of the issue, the cover pool securing the mortgage bonds represents an autonomous estate, separate from the estate of the issuer subject to the liquidation procedure and shall not be, subject to any liquidation procedure of the issuer's assets. The sale-purchase agreements concluded in breach of these legal provisions are null and void (Art. 48 CB Law).

In case of issuer's default under the cover bonds program, the National Bank of Romania can appoint a portfolio administrator (a specialised portfolio management company), acting under the NBR's supervision.

After the launching of the bankruptcy proceedings, a special portfolio management company carries out the administration of the pool of cover assets (replacing the portfolio manager previously appointed by NBR, if the case). In such case, the appointment of the portfolio manager is made by the syndic judge, after discussion with National Bank of Romania. Any acts or deeds executed by the issuer or by the judicial liquidator, after the appointment of the portfolio administrator (within the bankruptcy procedure) are null.

For the purpose of satisfying the receivables of bondholders in the amount and at the dates provided in the prospectus or, as applicable, in the offering document attesting the conditions of the issue and of the distribution of the amounts owed to them, the pool manager may:

> Continue to collect the amounts owed by the debtors of the cover pool, including by way of restructuring or enforcement of receivables in the event of default by the relevant debtors;

> transfer the obligations undertaken by the issuer to bondholders to another issuer, together with the related cover pool; and

> perform any other activities necessary for the satisfaction of the receivables included in the cover pool.

The pool manager is bound to consult the National Bank of Romania prior to committing to perform the following operations:

> Postponement of mortgage bonds maturity;

> partial or total sale of the cover pool;

> procurement of new financing to cover the temporary liquidity deficit based on the cover pool securing the mortgage bonds; and

> acceleration of mortgage bond payments.

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 allow that.

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.

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 overcollateralization in insolvency. It may be argued that voluntary overcollateralization 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

The pool manager may in accordance with art. 46 and 47 of the Law propose to the approval of the general meeting of bondholders the acceleration of the payment of the mortgage bonds and, in this respect, the assignment of the receivables to a third party, whom is permitted by law to grant mortgage loans as a professional activity.

The distribution of the amounts resulted from the assignment of receivables shall be made in the following order of preference:

> Receivables representing expenses incurred by the pool manager with the sale, its remuneration and the remuneration of the trustee;

> receivables under the financing granted to the issuer with the view to covering the temporary liquidity deficit;

> receivables resulting from the holding of mortgage bonds, pro rata, irrespective of the seniority and maturity of the mortgage bonds issue and receivables held by counterparties under the agreements underlying the financial derivatives included in the cover pool; and

> receivables of the issuer's creditors, according to art. 49 par (3), not paid in full upon the temporary closing of the bankruptcy proceedings.

If the amounts resulting from the assignment of receivables are insufficient to pay the obligations of the issuer, as recalculated to date, to the bondholders, for the remaining balance, they may satisfy their claims against the issuer's estate, together with the other unsecured creditors.

IX. RISK-WEIGHTING & COMPLIANCE WITH EUROPEAN LEGISLATION

The legislation when taken together with the practices, processes and procedures across the industry should fall within the criteria of Article 129 of the Capital Requirements Regulation (CRR).[1] The covered bonds issued under the Mortgage Bonds Law comply with Article 129(1) CRR and 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.

ECBC Covered Bond Comparative Database: http://www.ecbc.eu/framework/99/Obligatiuni_Ipotecare_-_Mortgage_Covered_Bonds.

1 Please click on the following link for further information on the UCITS Directive and the Capital Requirements Regulation (CRR): https://hypo.org/ecbc/covered-bonds/.