

15 June 2018

Maria Vilar Badia
Legislative Officer
Directorate-General for Justice and Consumers
European Commission
Office M059 02/096
1049 Bruxelles/Brussel
Belgium

Dear Maria

Proposal for a Regulation of the European Parliament and of the Council on the law applicable to third-party effects of assignments of claims (COM (2018) 96 final) (the "Proposed Regulation")

The Loan Market Association¹ ("LMA") welcomes the opportunity to provide further feedback on the Proposed Regulation and would like to thank you for taking the time to meet with us on 1 June 2018 to discuss the potential impact of the Proposed Regulation on the European syndicated loan market. In preparing this response, we have consulted widely with bank and non-bank LMA members that are active across the primary and secondary syndicated loan markets and this letter reflects their feedback.

The LMA recognises the positive legislative intention of the Proposed Regulation to foster cross-border investment in the EU and, thereby, facilitate access to finance for firms (including SMEs) and consumers by providing a uniform conflict of laws rule to address the third-party effects of assignments of claims. The very function of the European syndicated loan market is to facilitate liquidity and provide access to cheaper credit. In 2017, over €1 trillion in loans were made by investors (comprising banks and non-banks) in the European syndicated loan market and over €50 – 60 billion of these loans were traded in the secondary market, providing significant liquidity to the European banking sector.

As discussed with you on 1 June 2018, we are concerned that the proposal under the Proposed Regulation for the "habitual residence" of the assignor to determine the national law which applies to the third-party (or proprietary) effects of cross-border assignments of claims, if adopted, would in fact cause significant uncertainty and disruption to primary and secondary syndicated loan markets - which will reduce liquidity, and ultimately, reduce the

¹ The LMA is the trade body for the European, Middle Eastern and African syndicated loan markets. Its aim is to encourage liquidity in both the primary and secondary loan markets by promoting efficiency and transparency, as well as by developing standards of documentation and codes of market practice, which are widely used and adopted. Membership of the LMA currently stands at over 680 organisations across EMEA, including the European Commission, and consists of banks, non-bank investors, borrowers, law firms, rating agencies and service providers.

amount of finance available to firms (including SMEs) and consumers and will increase the cost of the credit that is available. This would be entirely contrary to the stated legislative intention.

The reasons for our concerns are specifically:

1. **Established market practice:** The long-established practice in the European secondary loan market for determining the third-party effects of transfer of loans in that market is that the law applicable to the transferred loan shall govern the third-party effects of claims arising from the transferred loan.
2. **Fundamental differences between syndicated loans and factoring:** Syndicated loans are a fundamentally different form of financing to that provided in the factoring market (which was the market considered in the Explanatory Memorandum) and the factoring market operates in a fundamentally different manner to the global syndicated loan market. *For the reasons set out below, it is impracticable, if not impossible, to apply the proposed "habitual residence" test to determine who might have a proprietary interest in a claim under a syndicated loan.*
 - Syndicated loans are typically made by multiple banks to a borrower in amounts greater than €25m. Factoring claims are generally much smaller.
 - Claims under syndicated loans are traded frequently (although not as frequently as listed securities and bonds) and can be traded more than once in a day. Factoring claims are traded much less frequently, often only once or twice before the claims are repaid. *Because syndicated loans are traded so frequently, it is impracticable to apply a different legal test each time a loan is traded to determine whether the claim has been effectively transferred.*
 - Claims under syndicated loans are traded individually and in part (e.g. a syndicated loan of €100m can be traded many times over to multiple purchasers in multiple parts, ranging in size from as small as €500,000 up to the full €100m). Factoring claims are transferred in large portfolios consisting of hundreds, if not thousands, of claims, and each claim is only transferred in whole (e.g. a claim of €100,000 will only be transferred with other factoring claims made by the same lender and the whole amount of €100,000 owed will be transferred to a single purchaser). When syndicated loan claims are traded in parts, each traded claim merges with other portions of the claim held by the purchaser upon acquisition, so *it will be impossible in such case to determine which portion of the loan was on-sold in any given sale – and therefore impossible to determine who owned any given portion of the claim.*
 - Loans traded in the syndicated loan market are typically administered by a facility agent, who acts on behalf of each of the lenders in the loan syndicate. While facility agents hold a register of lenders for the purposes of determining who is entitled to payments received from borrowers and other matters, they do not as a matter of market practice make such registers public or available to lenders in the loan syndicate. This is for a number of reasons, including contractual limitations and concerns around the mis-use of such information in breach of regulatory codes of market conduct. *Therefore, as facility agents do not make loan registers publicly available, it is practically impossible to*

establish the chain of ownership of the loan, and the identity of the owner of that loan at any given time; it is thus impossible to know which applicable law is relevant to each assignment of the loan.

3. **Increased complexity and creation of unfair commercial advantage:** Purchasers of syndicated loan claims may purchase the claims in the same credit facility from different lenders. At present, purchasers only have to consider the perfection requirements of the law of the underlying claim (which is currently the same for all assignments of the same debt claim). The Proposed Regulation would result in the purchaser also having to perfect each assignment in the jurisdiction of the habitual residence of each assignor. This adds unnecessary complexity to assignments of debt claims in a secondary loan trading context but may also result in some sellers in some jurisdictions being seen as more attractive because the perfection steps required by the law of the country of their habitual residence are minimal, less costly and/or less time-consuming than those in the habitual residence of other lenders. *This could create an unfair advantage to sellers in some member states, which is contrary to the generally accepted principle of harmonisation.*
4. **Transfer of claims and obligations not effectively covered:** Paragraph (17) of the preamble to the Proposed Regulation states that it does not cover transfers of contracts (such as derivative contracts, which are financial instruments under Directive 2014/65/EU on markets in financial instruments) in which both rights (i.e. entitlements to claims) and obligations are transferred.
 - Claims under syndicated loans are transferred by way of assignment of rights and assumption of obligations or by way of novation (where the contract with the borrower and the assignor is cancelled and replaced by a new contract between the borrower and the assignee).
 - The only exemption from the habitual residence test for contracts in which both rights and obligations are transferred is for financial instruments (as defined above) in Article 4(2) of the Proposed Regulation.
 - *If any transfer of any contract where both rights and obligations are transferred (in addition to financial instruments) are to be excluded from the habitual residence test, the Proposed Regulation must be amended to provide for this expressly in the body of the Proposed Regulation, as it currently only mentioned in the preamble which has no legal effect.*
5. **Adverse impact on market liquidity:** Fast settlement of trades in syndicated loans improves liquidity in the market. The LMA and market participants in the European secondary loan market have over time introduced a variety of initiatives to improve loan trade settlement times. The Proposed Regulation, if it applies to claims under syndicated loans, will increase settlement times and increase costs of trading whilst advice is obtained in all relevant jurisdictions and while local perfection steps are followed in addition to those required by the governing law of the transferred claim. This will undermine the efficiency of the European secondary loan market, which will result in fewer loans being traded, thereby reducing the liquidity in the market. *As noted above, any reduction in liquidity will reduce the amount of finance available to firms (including SMEs) and consumers and will increase the cost of the credit that is available.*

We are grateful for the confirmation provided at our meeting that it is not the Commission's intention to create legal uncertainty or to disrupt or damage an established market such as the European syndicated loan market where that would impact on the availability of finance to firms, SMEs and consumers.

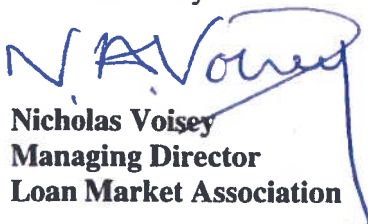
As discussed, we have provided suggested drafting amendments for your consideration in the Appendix which amend the Proposed Regulation so that the governing law of an assigned claim under a syndicated loan (rather than the habitual residence of the assignor) governs the third party effects of the assignment of such claims.

We hope that these comments and the comments included in our response provided on 23 May 2018 and suggested drafting amendments will be useful in shaping the debate as the Proposed Regulation makes its way through the EU legislative process.

Please note that we have, following our conversation with you, revised the drafting amendments which we requested in our letter of 23 May 2018. Accordingly, please consider only the requested amendments in the Appendix to this letter.

We would be happy to discuss any aspect of this response with you in more detail and to meet with you again as required to make the necessary amendments so as not to damage the European syndicated loan market. If we can be of any further assistance, please do not hesitate to contact either myself or Faizal Khan via email at nicholas.voisey@lma.eu.com / faizal.khan@cliffordchance.com or by telephone on +44 207 006 5364 / +44 207 006 2158.

Yours faithfully



Nicholas Voisey
Managing Director
Loan Market Association

Appendix

1. Requested Amendment to Article 4(2) of the Proposed Regulation

We request that Article 4(2) of the Proposed Regulation be amended to include additional exceptions to the habitual residence test in Article 4(1) as follows:

"The law applicable to the assigned claim shall govern the third-party effects of the assignment of:

- (a) cash credited to an account in a credit institution;
- (b) claims arising from a financial instrument;
- (c) claims arising out of syndicated credit agreements and wholesale credit agreements;
- (d) claims where corresponding obligations relating to such claims are also transferred or assumed by the assignee."

The requested new paragraph (c) of Article 4(2) provides for an exception to syndicated credit agreements and wholesale credit agreements. The inclusion of "wholesale credit agreements" is intended to ensure that larger loans which are made on a bi-lateral basis and are actively traded in the European syndicated loan market are not excluded from the requested new Article 4(2)(c) above. This gives clarity to the Proposed Regulation such that the habitual residence test will apply as contemplated by the Explanatory Memorandum to claims owed by SMEs and consumers. We consider this to be the simplest solution, and one which would minimise any potential disruption to European syndicated loan market.

The requested new paragraph (d) of Article 4(2) is intended to give broader effect to paragraph (17) of the preamble to the Proposed Regulation.

2. Requested Amendments to Article 2 of the Proposed Regulation

We request that Article 2 of the Proposed Regulation be amended to include the following definitions for the purposes of the requested new Article 4(2)(c) above:

- "'syndicated credit agreement' means a credit agreement that provides for, or contemplates, two or more creditors;"
- "'wholesale credit agreement' means a credit agreement concluded between a creditor and a business borrower, other than a business borrower who is a micro, small or medium-sized enterprise within the meaning of Article 2 of the Annex to the Commission Recommendation 2003/361/EC of 6 May 2003;"

3. Requested Amendments to Article 5 of the Proposed Regulation

We request that Articles 5(d) and (e) of the Proposed Regulation be deleted. Articles 5(d) and (e) are inconsistent with Article 4(2). The consequence of including Articles 5(d) and (e) is that where a claim is assigned by Person A and, subsequently, Person A purports to transfer both the rights and obligations in respect of the same claim to

Person C, such purported transfer to Person C *will always be subject to the law of the habitual residence of Person A* when establishing whether Person B or Person C has priority of ownership in the claim. This directly contradicts Article 4(2), and therefore creates legal uncertainty for transfers of financial instruments (and, if included in Article 4(2), syndicated loan claims and any other transfer which is intended to be excluded from the habitual residence test as set out in paragraph (17) of the preamble to the Proposed Regulation). To avoid such uncertainty, there should only be one uniform rule applicable.