

Greek NPLs law: first step towards a secondary market

As part of Greece's Third Economic Adjustment Programme¹, on 16 December 2015 the Greek government introduced a framework for the sale and management of non-performing loan portfolios originated by Greek banks (Greek law 4354/2015, the NPL Law). This came after the introduction of revised rules on civil procedure and enforcement of receivables earlier in 2015, and it is envisaged to be followed by the implementation of a series of other commitments under the Programme that aim to improve Greece's regulatory, legal and judicial environment when it comes to NPLs, enhance the supervisory powers of the Bank of Greece in this respect and allow assistance to be streamlined through the Hellenic Financial Stability Fund.

The newly introduced framework was long awaited to help create the legal environment and practical trails to enhance investors' appetite for the Greek loan market and to facilitate Greek banks in their efforts to address the consequences of a prolonged trend of increased NPL formation and high NPL ratios² resulting from the turmoil marking the Greek economy in the recent years.

Key features of the new framework

Non-performing loans (NPLs) are defined as loans and credits of any type which are in excess of 90 days past due; the explanatory report to the law cross-refers to the definitions of EBA Technical Standards Guidelines on Non-Performing Exposures.

The NPL law introduces and regulates the purchase of NPL receivables portfolios and the management thereof.

The new framework provides for two designated types of special purpose vehicles which may engage in NPL investments (managing and purchasing vehicles, respectively) and their licensing and regulatory requirements, stipulates the process for the entering into sale or management agreements and includes a series of provisions authorising the regulators to take further measures for the implementation of this new set of rules.

1 The link of the Programme MoU:

http://ec.europa.eu/economy_finance/assistance_eu_ms/greek_loan_facility/pdf/01_mou_20150811_en.pdf

2 43.6% market ratio of non performing exposures as a percentage of total exposures as at end September 2015, per BoG's annual report: <http://www.bankofgreece.gr/BogEkdoseis/ekthdkth2015.pdf>

Management & Servicing

NPL Managers

NPL management may only be outsourced to duly licensed special purpose entities in the form of société anonyme companies established or having a branch in Greece (**the NPL Managers**).

The Bank of Greece (**BoG**) is the supervising authority competent to grant and withdraw the license and to monitor the operations and governance of NPL Managers.

Establishment and licensing of an NPL Manager involves significant disclosure on the part of the NPL Manager's UBOs³ and officers. Approval by the BoG is granted subject to satisfactory evidence as to the business strategy of the NPL Manager (to include specific policies on socially sensitive debtor groups) and the suitability of the NPL Manager's officers and senior management teams. The law vests the BoG extensive supervisory and intervention discretions when it comes to NPL Managers. Secondary legislation is expected to further specify establishment formalities as well as the form and content of regular reporting which the law imposes on NPL Managers.

NPL Managers are subject to an annual fee payable to the BoG, yet to be determined; the same applies for Buyer SPVs (as defined below).

Which loans' management can be outsourced and how?

Scope

The law's description of the scope of NPL servicing agreements is non-exhaustive and includes a wide range of operations for the legal and accounting management of NPLs. Contrary to the sale of NPLs, where certain loan categories are excluded from the scope of the NPL Law (at least on a provisional basis), management services may be provided for any type of NPL portfolio. Such services may also include management of performing loans where the NPL Manager services NPLs of the same debtor.

Managers are authorised to interact with debtors, restructure loans, implement forbearance schemes and, subject to a licence by the BoG and the consent of the NPL owner, refinance NPLs. These operations should abide by all applicable banking regulations and primarily the Code of Conduct introduced by the BoG for the restructuring and/or management of non-performing loans by the Greek banks⁴.

NPL Managers are also explicitly authorised to take enforcement actions against defaulted debtors and participate in insolvency procedures for the benefit of the original lender.

³ *Ultimate Beneficial Owners*

⁴ *Greek law 4224/2013 and a series of secondary legislation issued by the BoG (Decisions No 116/25.8.14, 148/5.10.15, 54/15.12.15) have set the rules for informing and interacting with debtors as well as the rules for loan restructuring; these are coupled with NPEs regulatory treatment under BoG's decisions 42/30.5.14 and 47/9.2.15.*

Process

The NPL management agreement must be concluded in writing and meet minimum content requirements. It is subject to prior review by the BoG, though the NPL Law does not provide the exact process, timing or level of intervention by the BoG. No registration of the agreement with a public registry or other form of publicity/notification to the debtor is required.

Sale & Transfer

Who can buy NPLs?

The sale of NPL receivables can only be made⁵ to:

- (a) credit institutions;
 - (b) financial institutions; or
 - (c) duly licensed special purpose entities in the form of société anonyme companies established or having a branch in Greece with a minimum share capital of €100,000 (**Buyer SPVs**)
- (all the above, the **NPL Purchasers**).

Establishment, licensing and supervision processes and considerations for Buyer SPVs are substantially the same with those set out above with respect to NPL Managers.

Which NPLs may be put up for sale?

At least for a transitional phase expiring on 15 March 2016⁶ and reportedly being the subject of ongoing discussions between the Greek Government and its sovereign lenders, NPL Purchasers may not acquire all types of NPL receivables. Certain NPL categories are excluded from the scope of permitted sales, namely consumer loans, loans to SMEs⁷, and loans collateralised with Greek State guarantees or the debtor's primary residence.

NPLs are eligible for sale only if the seller has invited the debtor and the guarantors to settle or reschedule the debt at least 12 months before the contemplated offer for sale. Such requirement does not apply for "non-cooperative debtors"⁸ and for loan accounts under judicial enforcement proceedings.

The pool of loans may also include performing loans, provided that their debtor is the same as the NPL debtor.

5 *Eligible sellers are: Greek credit institutions, Greek branches of foreign credit institutions, securitisation SPVs and Buyer SPVs (as defined herein).*

6 *Initially expiry date was 15 February 2016, and then extended to 15 March 2016 by virtue of Law 4366/2016 published on 15 February 2016.*

7 *SMEs are defined by reference to the EU Commission Recommendation 2003/361 of 6 May 2003.*

8 *The concept is defined under decision No 116/25.8.2014, issued by the Credit and Insurance Affairs Committee of the BoG.*

The sale of an NPL claim does not result in the transfer of the entire loan agreement. Consequently, the contractual obligations of the originating bank under the underlying loan agreement are not transferred to the buyer. Legal obligations, such as the levy of Greek law 128/1975⁹ (to the extent applicable), will burden the NPL Purchaser from the time of the sale onwards.

On the other hand, the sale of the claim has as a consequence the automatic transfer to the buyer of all *in rem* securities (such as pledges and mortgages), personal and corporate guarantees, ancillary rights, as well as privileges related to the enforcement of the claim or of the guarantee; privileges related to the seller are not transferred.

The NPL Purchaser, as owner of the purchased claims, shall have all the rights of a creditor under the underlying contract and, subject to BoG license, the right to refinance purchased loans.

Process

Before the enactment of the NPL Law, sales of NPLs were structured (a) either as a plain vanilla sale and assignment of claims under the general provisions of the Greek Civil Code (**GCC**) or (b) more commonly, as a securitisation transaction in accordance with articles 10 and 14 of Greek law 3156/2003 (the **Securitisation Law**)¹⁰; at the time, the law did not impose licensing or other regulatory obligations to the buyers of NPLs, hence the grey area as to who and under which circumstances could invest in those portfolios. The above analysis continues to apply for the sale of performing loan portfolios.

The NPL Law cross refers to and/or replicates, to a certain extent, provisions of the Securitisation Law whether in terms of process or of substance; this renders the new law relatively familiar to the Greek banking market which has witnessed a wealth of securitisation precedents since the enactment of the Securitisation Law in 2003.

So, similarly to a securitisation transaction, the sale of NPL receivables occurs by virtue of execution and registration with a special public registry of the summary of the sale and transfer¹¹ agreement. The registration concludes the transfer of the receivables on a true sale basis; however, contrary to the Securitisation Law¹², NPL Buyers must notify the obligors of the NPL portfolios in order for the sale to become effective towards the latter.

9 *The levy of Greek law 128/1975 is raised on interest payments of loans granted (among others) by Greek banks.*

10 *The Securitisation Law allows for and regulates the transfer of business receivables to a special purpose vehicle (SPV) under a true sale transaction.*

11 *From a practical standpoint, in most, if not all, securitisations in the Greek banking market the sale agreement was governed by foreign law (UK most commonly) and the transfer agreement (a concise, at times two page, document annexing the list of transferred loans) was governed by Greek law.*

12 *Under the Securitisation Law, the registration itself is a deemed notification to the debtor.*

After the sale – points to keep in mind

Seller's insolvency & clawback

The insolvency of Greek banks is governed by a special liquidation framework, and, ancillary, by the provisions of the Greek Bankruptcy Code. Under the most precautionous view, claw-back rules of the Greek Bankruptcy Code also apply to banking liquidations.

Contrary to the Securitisation Law, the NPL Law offers no protection to NPL Buyers as regards the claw-back risk.

Set off

By way of general Greek civil law provisions, an obligor may set-off claims the obligor had against the seller towards obligations arising from the purchased NPLs provided (a) that the legal basis of the obligor's claims against the seller existed before the notification of the sale to the obligor; and (b) that the obligor's claims against the seller become due and payable not later than the time when the claims arising from the NPLs become due and payable.

Data protection

Greece has transposed the EU data protection directives¹³. Data processing by the NPL Purchaser and/or NPL Manager will require prior approval by the Greek Data Protection Authority (contrary to the explicit exemption provided in this respect by the Securitisation Law.)

Banking secrecy

It is questionable whether non-banks that acquire NPLs, i.e. Buyer SPVs, will be entitled to have access to bank account details and other data of the underlying obligors falling under the banking secrecy principle without specific legislative provisions to that effect.

The NPL Law waives professional secrecy obligations only with respect to NPL Managers in their relation with the owner of the loan accounts and on a need-to-know basis only.

Consumer protection

Buyer SPVs and NPL Managers are considered "traders" under the Greek consumer protection laws and regulations and must abide by those laws, making sure to cater for socially sensitive debtor groups.

13 *Dissemination and process of personal data, including data relating to financial behaviour of individuals, is restricted by several laws (e.g. law 2472/1997 on data protection and law 3741/2006) and secondary regulatory decisions of the Greek Data Protection Authority.*

Thoughts on the new framework

Moving parts

The exact process and criteria for the licensing of NPL Managers and SPV Buyers, as well as their reporting obligations, remain to be determined by secondary legislation, yet to be issued. The same applies for a series of other practical points, such as the minimum content of servicing agreements which, again, is left upon the BoG to further determine.

The perimeter of NPLs eligible for sale remains in a provisional restrictive status which the NPL Law defers to a later stage.

This adds to the wider discussion, among banks and authorities as to the exact strategy¹⁴ and targets on NPLs; the Third Economic Adjustment Programme includes bold initiatives as to the study and assessment of NPLs (segmentation analysis, proposed targets & KPIs, strategy development) calling the banks, the BoG and the Hellenic Financial Stability Fund (the **HFSF**) to produce specific deliverables so as to comprehend and create a dynamic NPL market. The NPL Law makes no reference to the HFSF which is anticipated to have an ancillary, yet pivotal role, in the Greek NPL market, more as a technical assistance vehicle rather than an active market player. Funding of NPL sales through the HFSF is not envisaged in the NPL Law or in the Programme's MoU.

During Q3 2015 the scope of the HFSF¹⁵ was expanded to facilitate NPLs management.

Less regulation, more precision

Certain provisions in the NPL Law are unclear and/or too restrictive for no apparent reason.

For example, the 12-month prior invitation by the banks to obligors to settle their debts as condition precedent to the sale is redundant; it is reasonable to assume that a bank will have exhausted all reasonable measures for the settlement of such loans before deciding to sell them.

Moreover, the bundling of NPL and performing loans of the same debtor is incomplete: the law allows bundling only where the debtor of the NPL and the debtor of the performing loan is the same person. However, more often than not, such debtors may be different (e.g. affiliates or related entities), but the end obligor will be the same (i.e. the individual who is the actual or beneficial owner

14 See EU Commission's report dated 20.11.2015 on Greece's compliance with Programme milestones, action 32 http://ec.europa.eu/economy_finance/assistance_eu_ms/greek_loan_facility/pdf/report_on_greece_compliance_november_2015_en.pdf

15 Law 3864/2010; historical info posted on: <http://www.hfsf.gr/en/legislation.htm>

of all such entities). In addition, the law does not cover loans where the NPL debtor is the guarantor of a performing loan.

Another unduly restrictive requirement is that NPL Managers and NPL Purchasers must have a form of establishment in Greece, whether registered seat or branch.

We are also of the view that some of the supervisory discretions of the BoG are unwarranted – such as its broad authority to approve a management agreement, to the extent that such authority exceeds confirmation of compliance with the minimum legal content of the agreement.

Finally – and most importantly - the requirement under the NPL Law for NPL Managers and Buyer SPVs to aim at “*economic recovery and development*” (*sic*) is contradictory to the private status of such entities. Such aspirations should be reserved for regulators and state authorities only (such as the BoG).

Tax

The NPL Law does not include tax provisions of any type. On the contrary, the Securitisation Law provides for a wide range of tax exemptions and cost reductions. Without such exemptions the sale and purchase of NPLs may incur significant costs and taxes.

Next steps

The path for a Greek NPL market has started to be paved. Regulation and supervision of managers and buyers has been a grey area for the market for a number of years and the law, despite its shortcomings, has set out a general regulatory framework.

Notwithstanding this, the attempt to regulate the mechanics and legal technology by which private entities will enter into commercial agreements should be deterred. On the positive side, we highlight two significant trends: firstly, the law makes use of well-tested tools, such as securitisation law concepts and procedures; and secondly, amendments and reforms are under way to improve other legal texts which, although unrelated to the process of purchasing loans, are pivotal in order to form an efficient basis for creditor-debtor interaction.

We understand that the NPL Law may be amended soon, and we look forward, with the rest of the market, to the improvements that such amending legislation will bring about, along with the secondary legislation expected to be issued by the BoG. One thing is clear: NPLs should be addressed from all possible perspectives and the Greek banks must be provided with all practical tools to use at their discretion depending on the state of the economy, market demand and each bank's strategy and balance sheet.

For further information, please contact:

Christina Papanikolopoulou

Partner

Head of the Banking & Finance and Capital Markets group

T (+30) 210 69 67 101

M (+30) 6970 444 003

E c.papanikolopoulou@zeya.com

Kely Pesketzi

Senior associate

T (+30) 210 69 67 131

M (+30) 6958 462 623

E k.pesketzi@zeya.com

Established in 1893, Zepos & Yannopoulos is one of the leading and largest Law firms in Greece providing comprehensive legal and tax services to companies conducting business in Greece.

280, Kifissias Ave.
152 32 Halandri
Athens, Greece

newsletters@zeya.com
Tel.: (+30) 210 69 67 000
Fax: (+30) 210 69 94 640

www.zeya.com

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