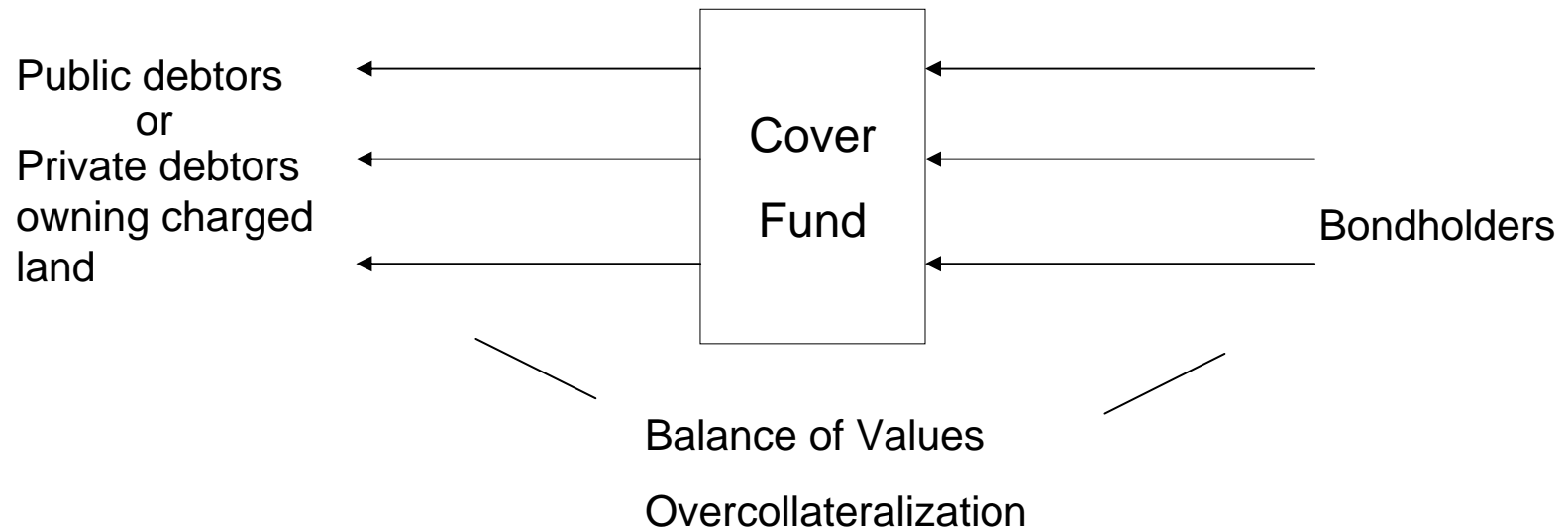


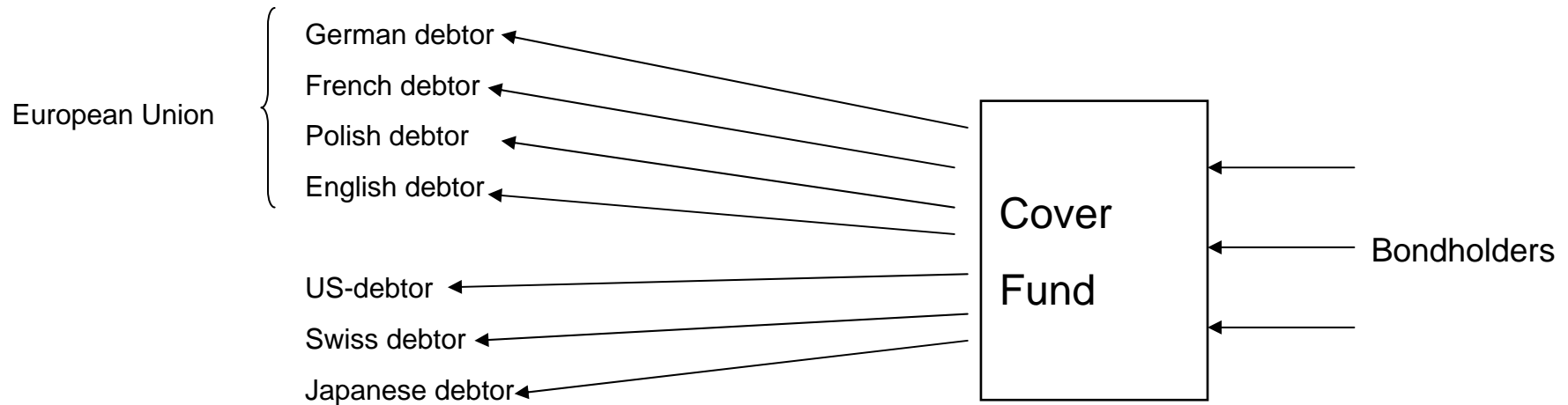
# **Legal Questions of Cross Border Cover Assets**

Professor Dr. Rolf Stürner  
University of Freiburg  
Germany

## Model of Covered Bonds

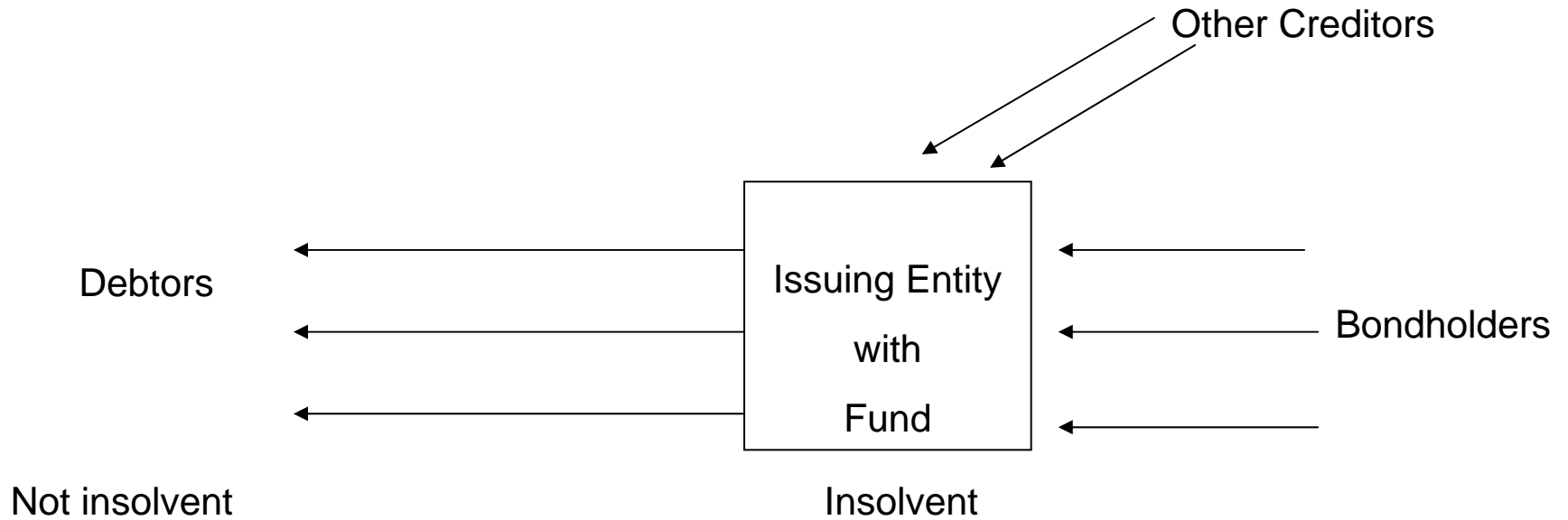


## Cross Border Cover Assets

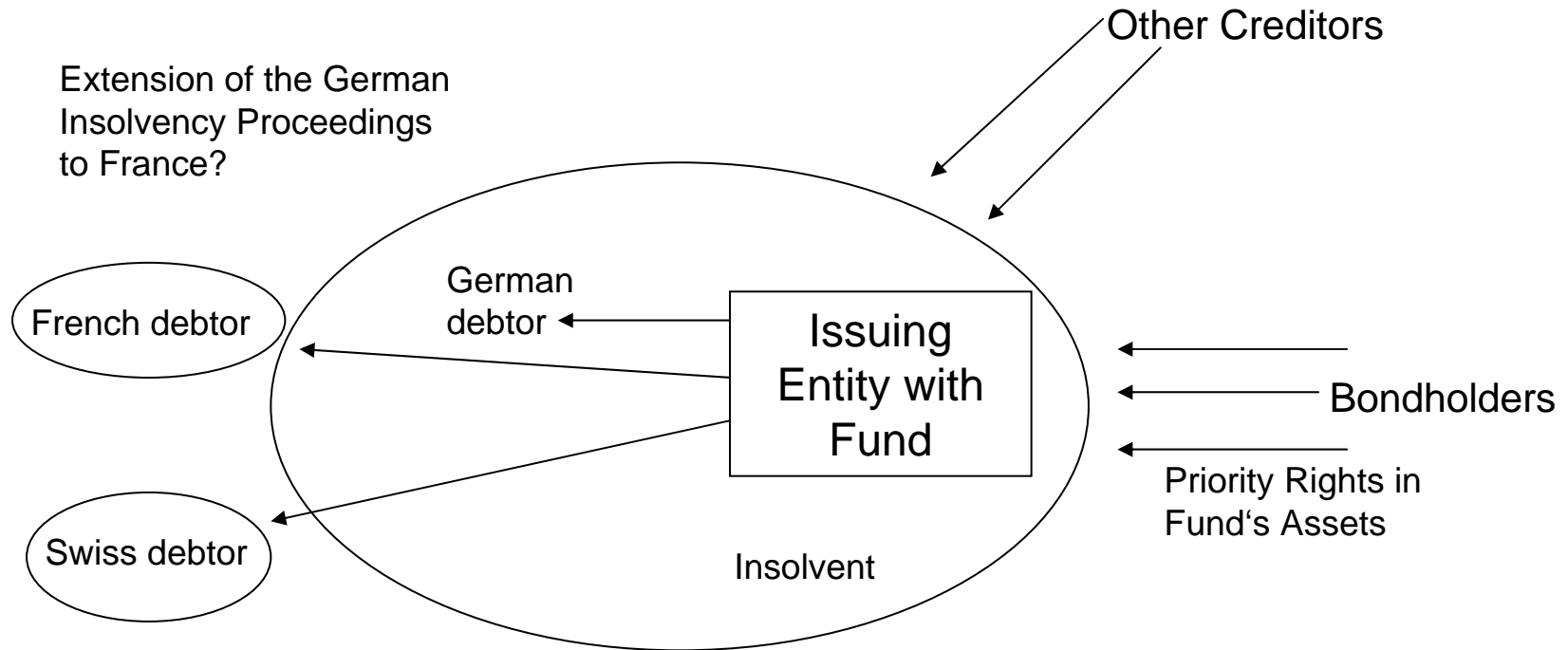


- More complicated enforcement of claims
- Distribution of risk of debtors' break down

The Topic:  
Issuer's not Debtors' Insolvency



# Insolvency of the Issuing Entity and Debtors in Foreign Countries

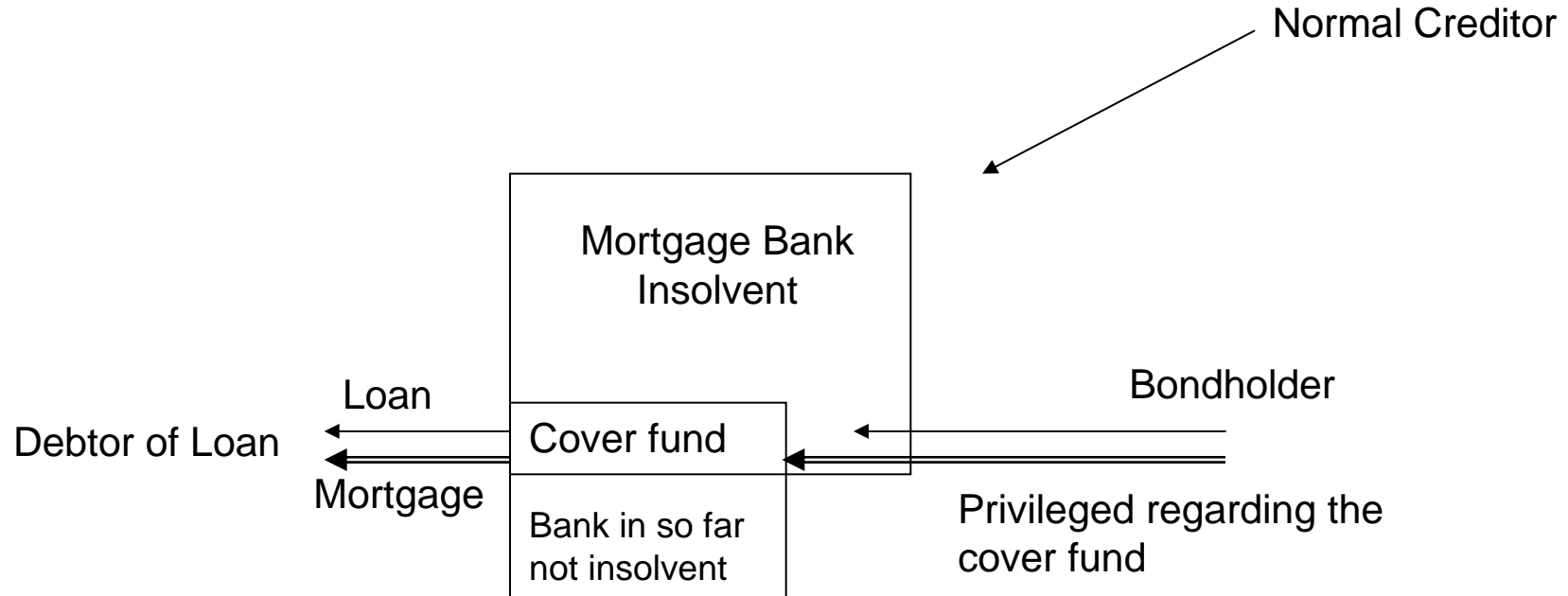


Extension of the German Insolvency Proceedings to France?

Separate Swiss Insolvency Proceedings  
Acknowledgement of Bondholders Priority Rights?

German Insolvency Proceedings  
No Danger for Priority Rights

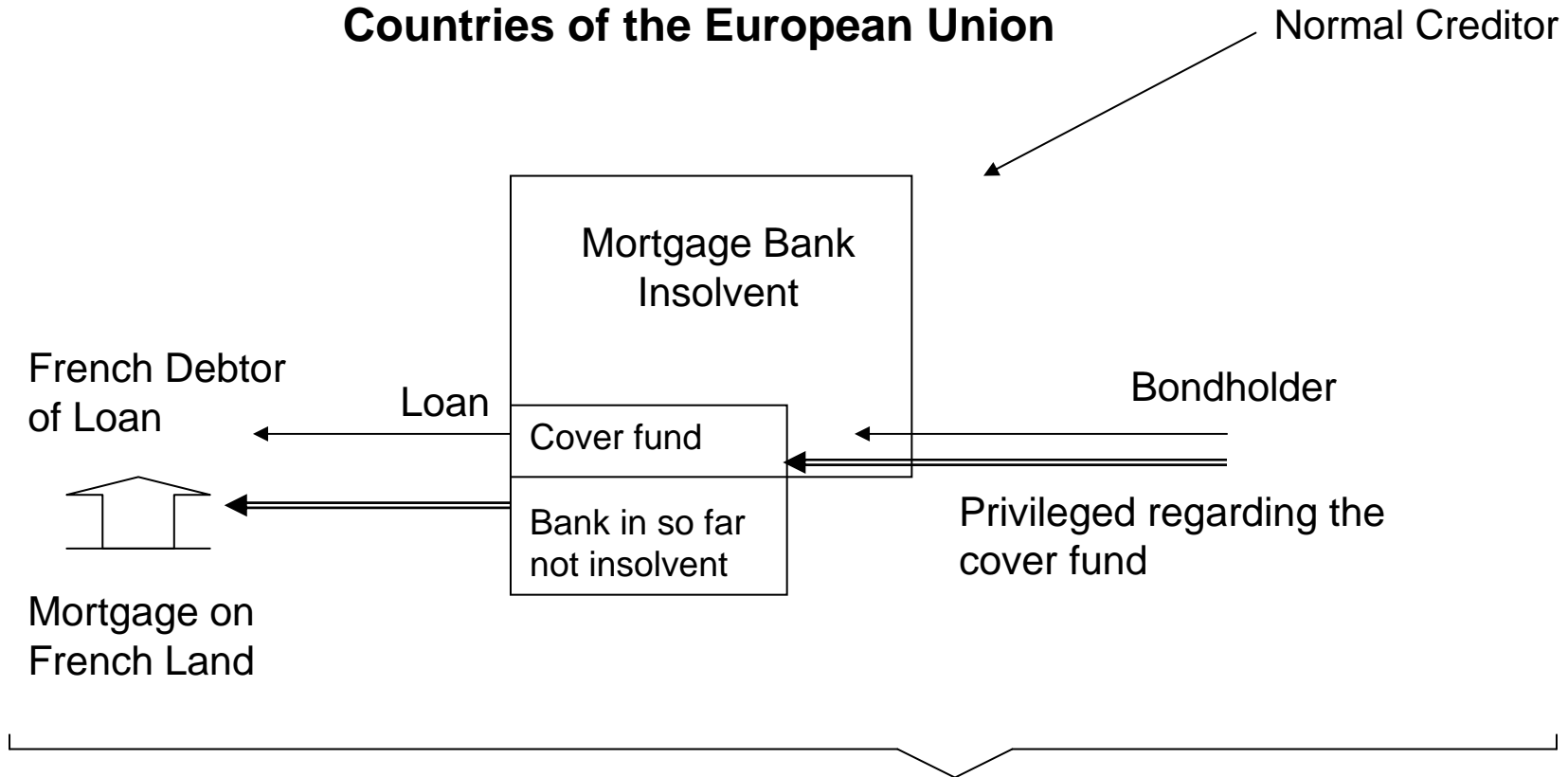
## German Covered Bond Model



### Insolvency of the Mortgage Bank

1. Cover fund not affected – not a part of the insolvency estate – continuing payments to bondholders – clear legal provisions
2. Special Receiver for cover assets acting in the interest of the bondholders only
3. No Execution by Normal Creditors in Cover Fund Assets

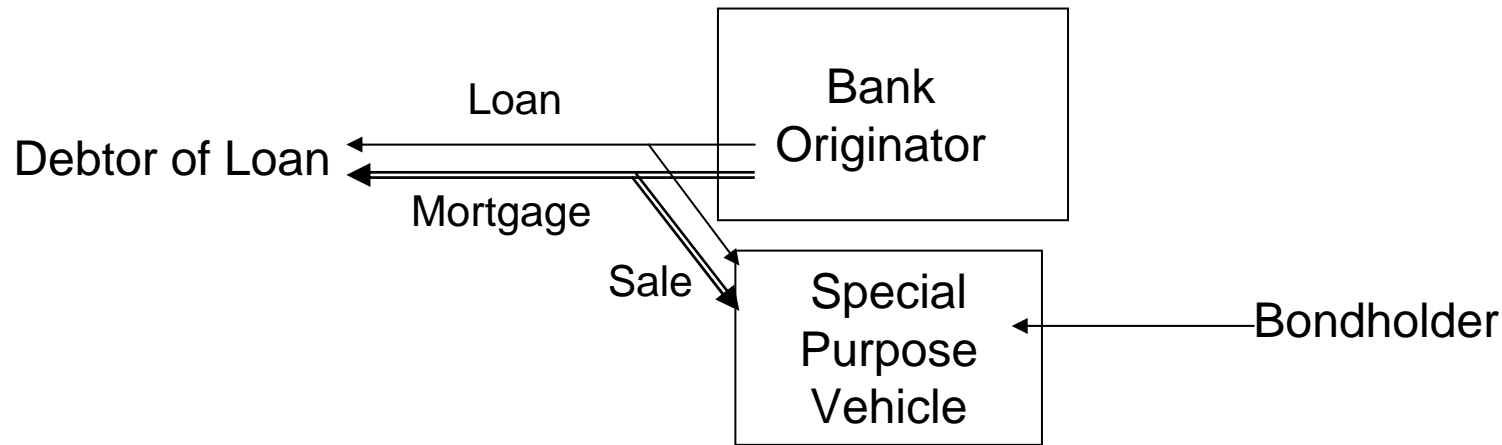
## Insolvent German Bank and Cover Assets in Countries of the European Union



European Directive on the Reorganization and Winding Up of Credit Institutions

1. One Single Insolvency Procedure in Germany
2. Extension of the German Insolvency Proceedings to France

## True Sale Model (simplified)

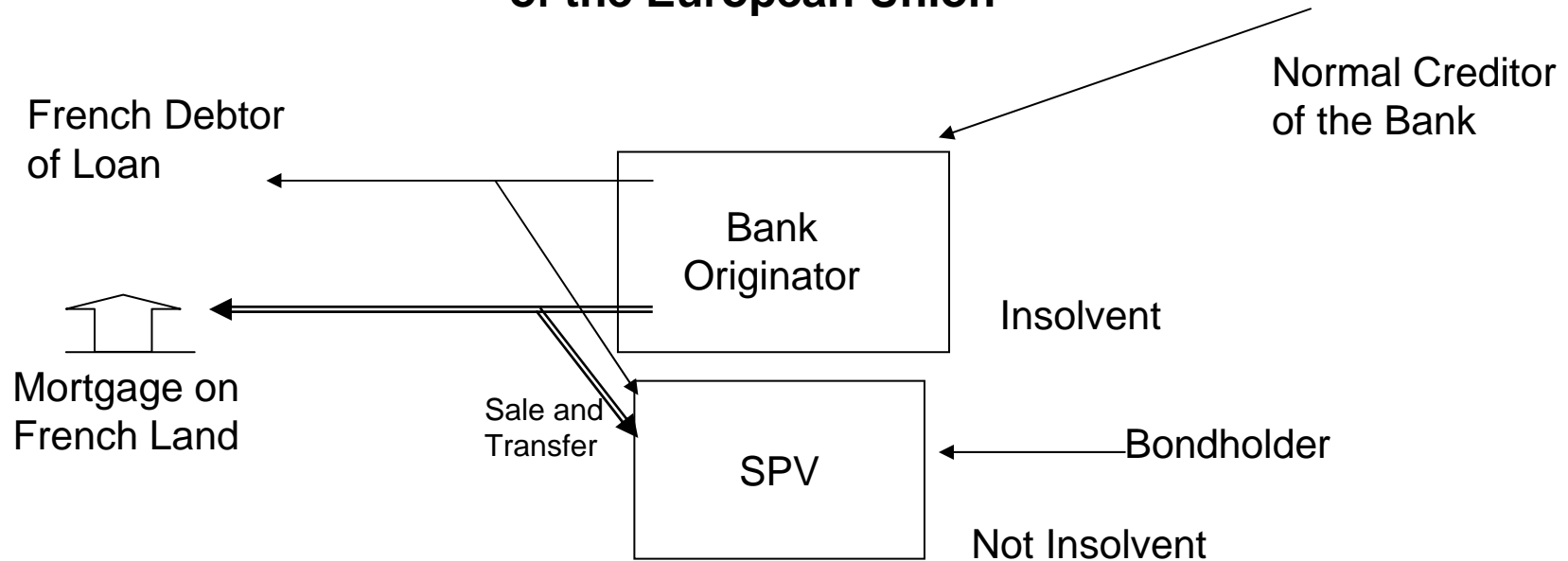


### Underlying Theory:

- Insolvency of the Originator does not affect the Cover Assets held by the SPV
2. No Execution of the Originator's Creditors in Cover Assets of the Special Purpose Vehicle

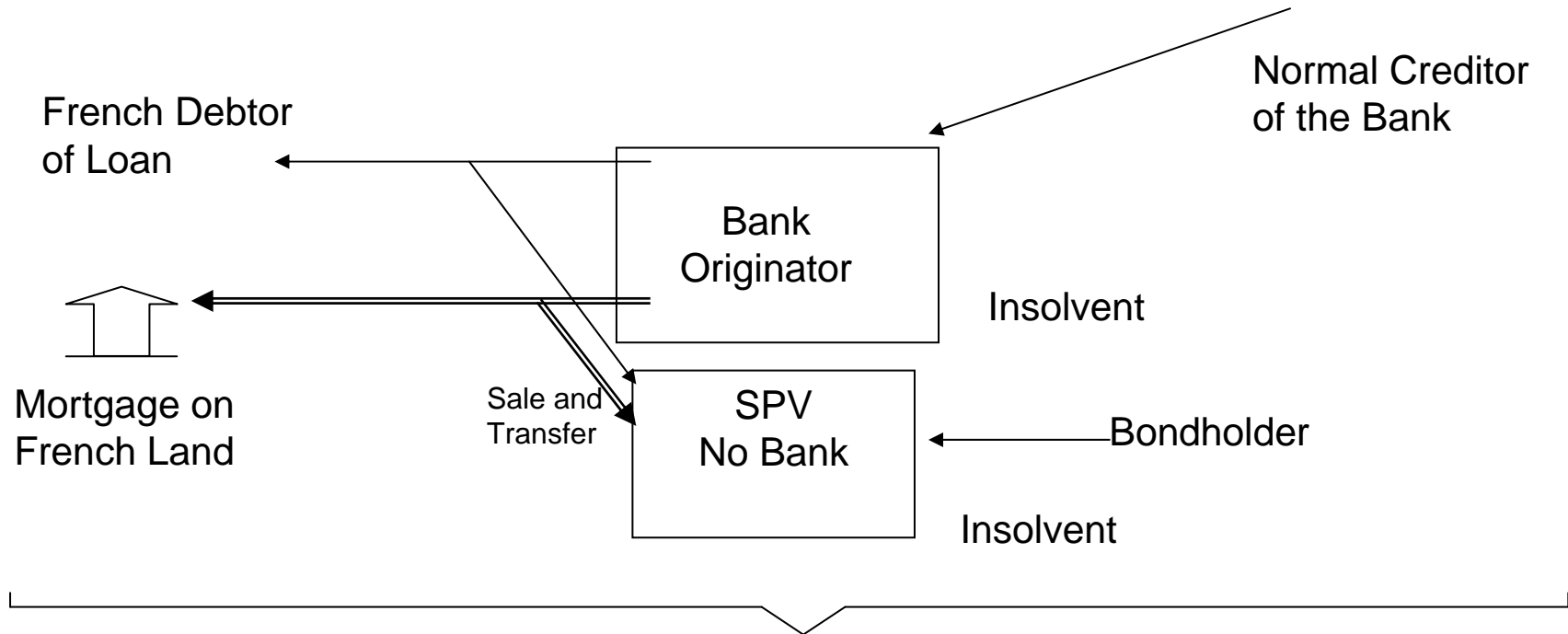


## True Sale Model and Cover Assets in Countries of the European Union



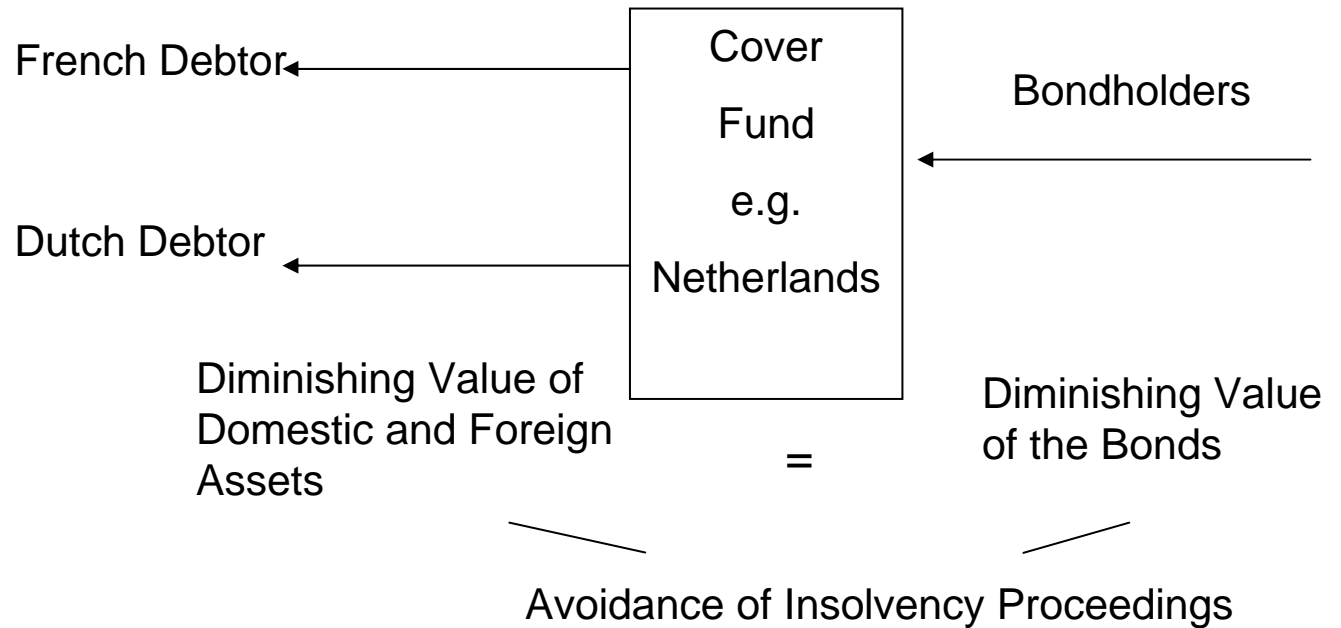
1. Theory: Foreign French Assets unaffected by the bank's insolvency as it is the case with domestic assets
2. Potential non-recognition of the contractual separation (recourse of the SPV against the bank, rights of the bank to surplus, retroactive price adjustment, degree of administration by the originator etc.) or consolidated insolvency
3. Consequence: priority rights of the bondholders only – then governed by French law with many unclear Issues.

## True Sale Model Cover Assets in Member State and Insolvent SPV



1. German Main Insolvency Proceedings
2. Secondary Insolvency Proceedings in European Countries where Cover Assets are located
3. No Secondary Insolvency Proceeding, if fund owned by the Originating Bank (German solution and – in part – French solution)

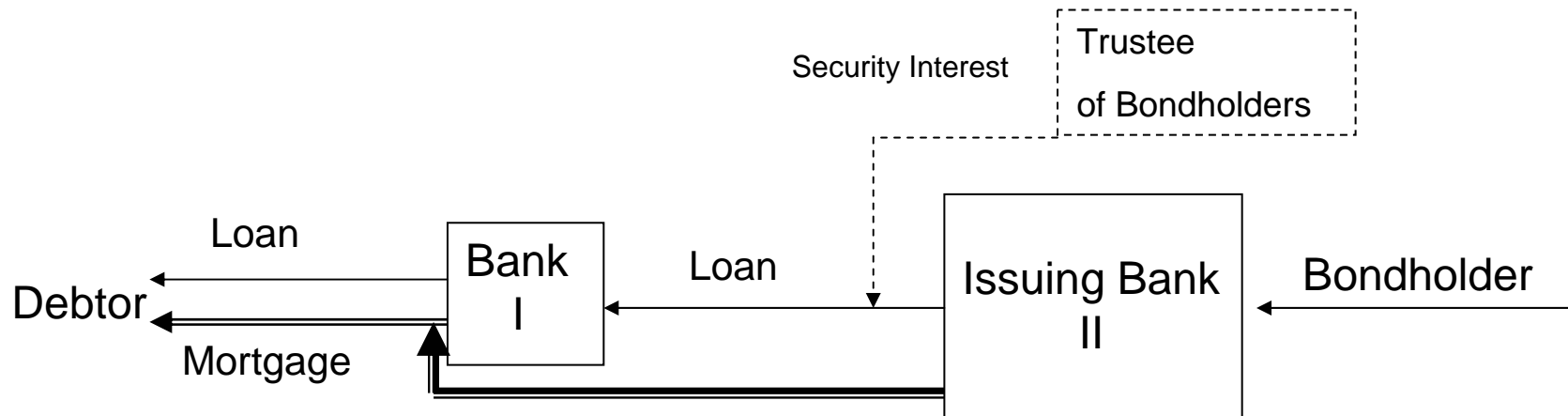
## Hybrid Covered Bonds Avoidance of Insolvency of Cover Funds



Preliminary Contractual Insolvency Arrangement

1. Admissibility under German Law questionable
2. Lower Rating?

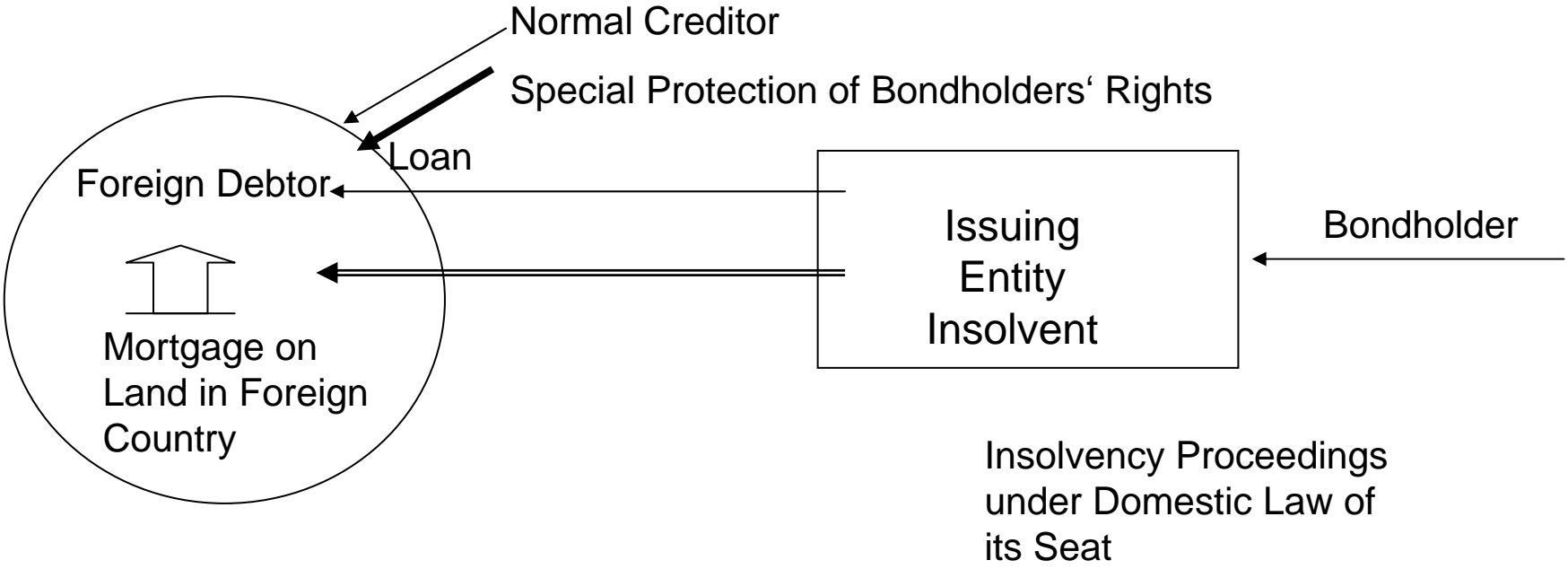
## Pledge Model with Two Tiers and Cross Border Cover Assets



Pledge under the European Directive on financial collateral arrangements (interbank security interests)

1. Insolvency of the issuing bank II:  
Danger for priority of bondholders' claims realistically excluded if other bank business not permitted
2. Insolvency of the bank I:  
Security interests of the issuing bank not affected (European Directive)
3. Third Party Effect of Security Interests in Foreign Cover Assets only in case of Security Interests under Foreign Law

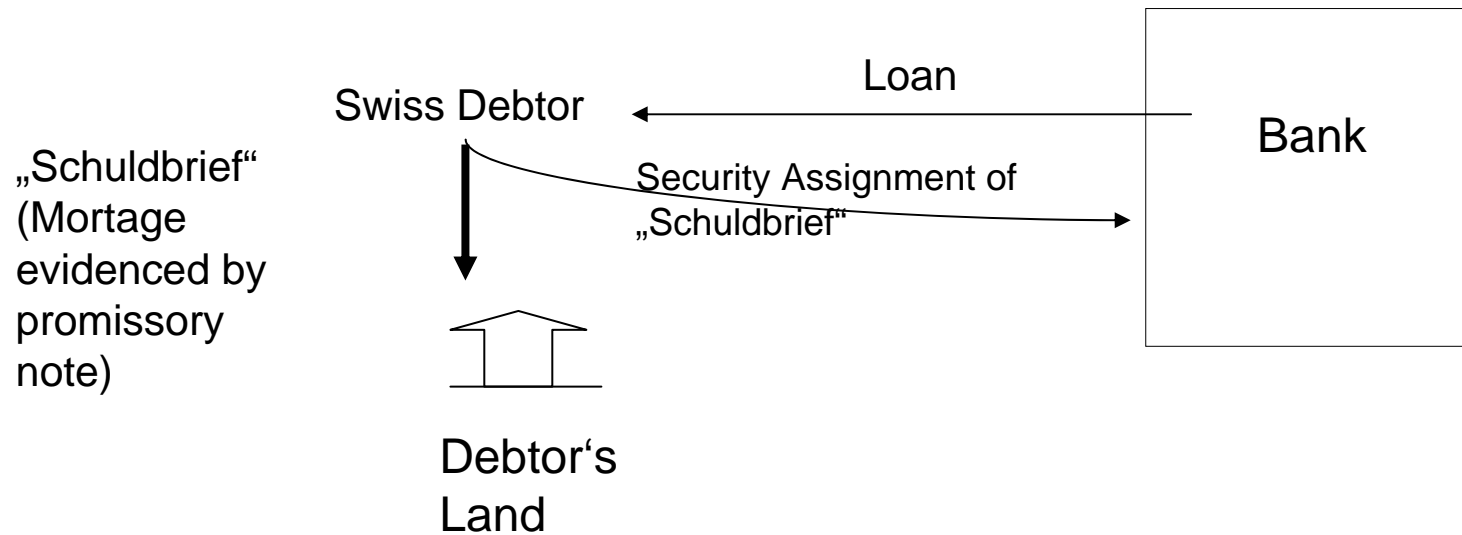
# Cross Border Cover Assets in Non-Member Countries Principle



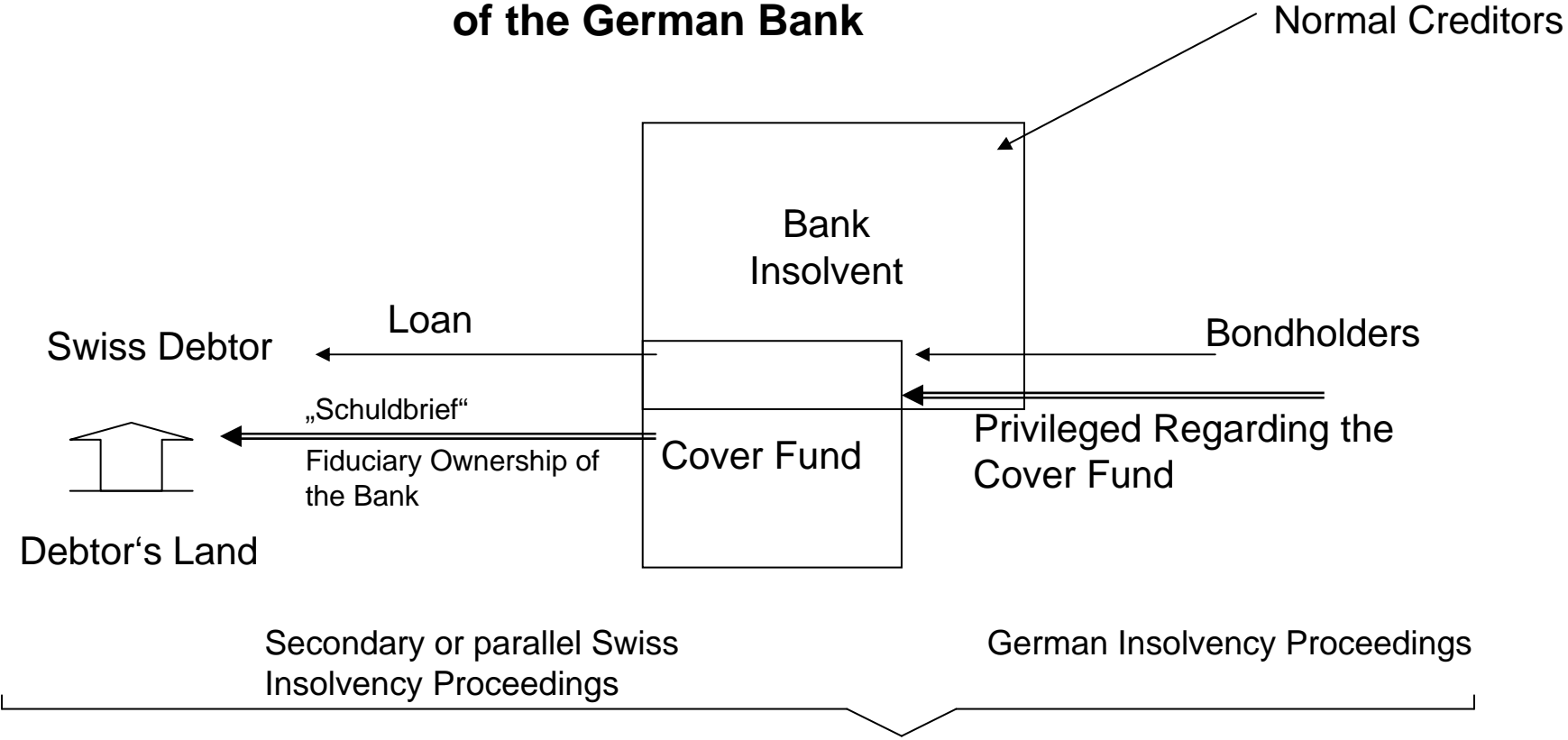
Secondary or Parallel  
Insolvency under Foreign Law

Legal Instrumentalities of  
Foreign Law for the Protection  
of Bondholders' Priority Rights

## Loans and Security Rights in Real Property under Swiss Law

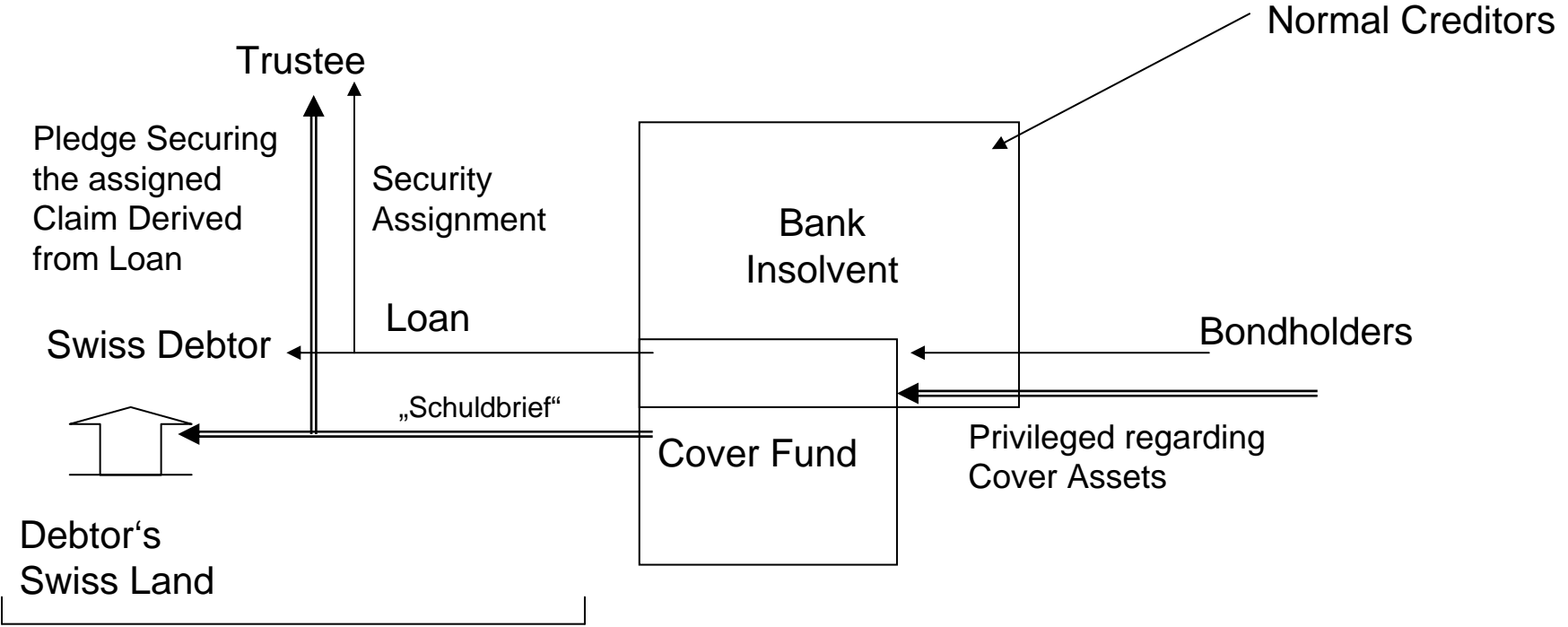


# Protection of Swiss Assets and Insolvency of the German Bank



1. Seizure of Loans Before Recognition of German Insolvency by Normal Creditors
2. Recognition of German Priority Rights in Swiss Insolvency Proceedings Questionable

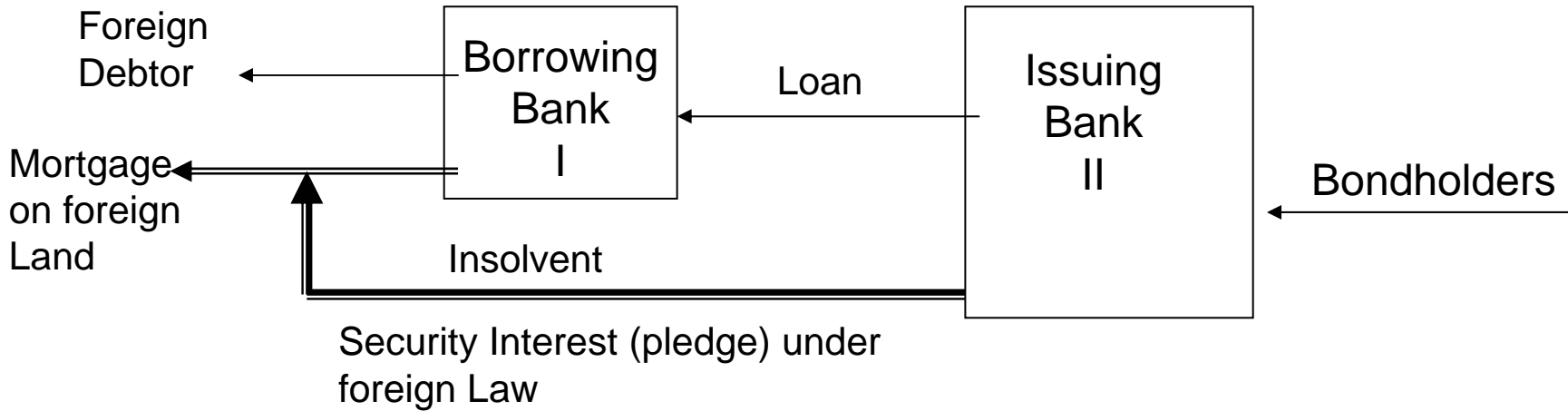
# Special Swiss Security Interest for Bondholders' Protection



1. Protection against execution in Swiss assets through Trustee's security interests
2. Assigned claims derived from loans not included in Swiss secondary or parallel insolvency proceedings

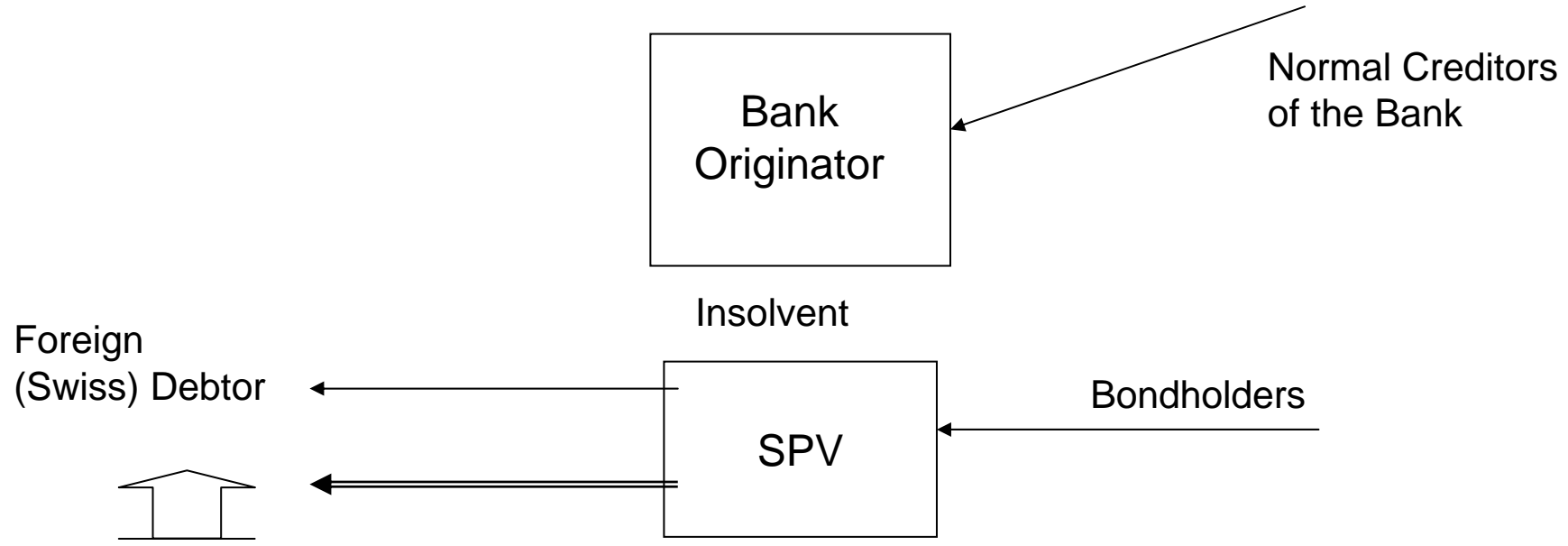


## Pledge Model with Two Tiers and Cover Assets in Non-Member Countries



No Remarkable Difference to the Case of  
Assets in European Member States

# True Sale Model and Cover Assets in Non-Member Countries



Mortgage („Schuldbrief“) on Foreign („Swiss“) Land

No Remarkable Difference to the Case of Assets in European Member States

1. Danger of non-recognition of separation of assets
2. Lack of security interests under foreign (Swiss) law for the protection in Swiss insolvency and execution procedures in case of collapsing contractual structure

## **Conclusion**

Preference for Legal Models Combined with  
Standardized Security Interests

Adequately Calculated Overcollateralization  
Recommendable When Using Cross Border  
Cover Assets

In Part Obligatory under German Covered Bond  
Law