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Amendments to the law of 5 August 2005 on financial collateral arrangements

On 24 July 2002, the Law of 20 July 2022 (published in *Mémorial* A 371, with corrigendum published in *Mémorial* A 402) entered into force.

In particular, the Law of 20 July 2022 has amended a number of provisions of the Law of 5 August 2005 on financial collateral arrangements, as amended from time to time ("**2005 Law**"), which implemented Directive 2002/47/EC on financial collateral arrangements, as amended.

In most cases, the amendments introduced by the Law of 20 July 2022 clarify or consolidate practices developed by practitioners in relation to security interests governed by the 2005 Law.

Among the changes made to the 2005 Law, we set out below a list of those that are particularly relevant to the structuring of security interests governed by the 2005 Law:

1) Clarification of beneficiaries for transfers of title by way of security:

The definition of "financial sector professional" now expressly includes any payment institution or any electronic money institution.

2) Exercise of rights attached to claims over insurance contracts:

The 2005 Law applies to financial collateral arrangements over financial instruments and claims.

As a reminder, the Law of 20 May 2011 (which first amended the 2005 Law by implementing Directive 2009/44/EC of the European Parliament and Council dated 6 May 2009) introduced a paragraph (4) in Article 5(b) of the 2005 Law, pursuant to which "[…] The pledge of a claim implies the right for the pledgee to exercise the rights of the collateral provider linked to the pledged claim."

The Law of 20 July 2022 has introduced a paragraph (g) in Article 11 of the 2005 Law (article on means of enforcement) which allows the pledgee in the event of an enforcement event "[to] exercise all the rights arising under the pledged insurance contract, including, in

the case of a life insurance contract or a capital redemption operation, the right to surrender, or request the insurance undertaking to pay any amounts due pursuant to the insurance contract".

The addition of this paragraph enshrines the exercise of the rights attached to the claim against the insurer.

3) Terms and conditions of enforcement:

- The definition of "enforcement event" now expressly refers to an event of default or any other event whatsoever as agreed between the parties. The addition of the word "whatsoever" emphasises that the parties are entirely free to determine by agreement the events the occurrence of which may trigger the enforcement of the collateral without the financial obligations having to become necessarily due and payable.

  The parliamentary work on the Law of 20 July 2002 cites examples such as non-compliance with certain financial ratios (which had been confirmed by the Courtepaille judgment) or other factors relating to particular aspects of a transaction.

- The Law of 20 July 2022 has introduced a new paragraph 5 in Article 11 of the 2005 Law (as copied below) : "Where the relevant financial obligations are not due at the time the pledge is realised following an event agreed between parties as constituting an enforcement event, the proceeds of the realisation shall be, unless otherwise agreed, applied to satisfy the relevant financial obligations."

  This new paragraph is directly related to the definition of "enforcement event", which allows the pledgee to realise its security following a default or any other event whatsoever as agreed between the parties while the financial obligations are not necessarily due and payable.

4) Means of enforcement: Article 11 of the 2005 Law has been amended to modernise the means of enforcement

- A new definition of "trading venue" has been inserted and includes a regulated market, a multilateral trading facility or an organised trading facility. This definition is used in Article 11 of the 2005 Law.
- Article 11 has been substantially amended to modernise certain means of enforcement:
  - in the event of an assignment by the pledgee of the pledged collateral, the pledgee can assign or cause the pledged collateral to be assigned on the trading venue on which it is admitted to trading. This assignment method complements the existing assignment methods, i.e. by private sale in a commercially reasonable manner or by public auction;
  - regarding the pledged financial instruments, the pledgee can appropriate them or have them appropriated by a third party:
    (i) at the market price, where such instruments are admitted to trading on a trading venue;
    (ii) where they are units or shares of an undertaking for collective investment, at the price referred to in point (i) or at the price of the last net asset value published by or for this undertaking for collective investment, provided that the last

publication of the net asset value does not exceed one year;

- the pledgee may request the redemption of the pledged units or shares of an undertaking for collective investment at the redemption price in accordance with the instruments of incorporation of this undertaking for collective investment.

- In the event of a public auction of the pledged collateral, the *Bourse de Luxembourg* no longer has any imposed role (the 2005 Law provided for the intervention of the *Bourse de Luxembourg* unless otherwise agreed by the parties). Unless otherwise agreed by the parties, the pledgee can now appoint an auctioneer in charge of operating the public auction among sworn notaries or bailiffs (*huissiers*). The Law of 20 July 2022 provides in detail for the terms and conditions of a public auction.

5) Sequestration expressly becomes a measure that does not apply to collateral financial arrangements and netting agreements:

Article 19 (b) of the 2005 Law adds sequestration to the existing measures (attachment whether civil, criminal or judicial, or penal confiscation) which do not apply to financial collateral arrangements governed by the 2005 Law and cannot impede their enforcement.

The *Conseil d'État* had noted in its advice to the bill of the Law of 20 July 2022 that this provision goes against the case law of the Court of Cassation which ruled that according to Article 20 (4) of the 2005 Law, such provision " [...] does not prevent the president of the district court, when seized upon unilateral application or sitting in summary proceedings, from ordering a provisional measure aimed at preserving the rights of the pledgor in the event of allegation of fraud or abuse of rights in the enforcement event." Accordingly a sequestration measure was the only conservatory measure which would have the effect to stop the enforcement of a financial collateral arrangement in the event of allegation of fraud or abuse of rights in the enforcement event.

However the parliamentary work to the Law of 20 July 2022 specifies that this addition is in line with the general spirit of the 2005 Law, which aims at ensuring a swift and smooth enforcement of a financial collateral arrangement.

For the consolidated version of the Law of 5 August 2005 on financial collateral arrangements, please see **here**.