Briefing

12 September 2016

Finance and secured lending in Romania

1. Trends and regulatory climate

1.1 Trends

What is the current state of the lending market in your jurisdiction and have any new trends emerged over the last 12 months?

The lending market picked up during the second quarter of 2016, following a slowdown at the end of 2015.

Bank debt continued to be the most common form of lending. International banks and multilateral development banks have been active alongside local banks, which have increasingly been cleaning their balance sheets (including through several deals involving large non-performing loan portfolios) following the recommendations of the National Bank of Romania and in preparation for expected growth in lending. There is generally high liquidity in the Romanian banking sector.

There has been limited lending through the capital markets (ie, by issuing bonds), but alternative lenders – including mezzanine funds, private debt funds, business development companies, insurers, asset managers and finance companies – are scouting the market and have already concluded deals.

The main sectors with significant secured lending include real estate (in particular, shopping malls, office buildings and logistics centres), agriculture, pharmaceuticals, production, retail and technology.

On the regulatory side, since May 2016 legal developments in consumer banking have kept local banks busy with impact assessments and new processes and procedures in relation to a new law regarding the transfer of mortgaged real estate in lieu of payment by consumers. Further, in late 2016 a new law on the insolvency of natural persons is expected to enter into force – the first of its kind in Romania. These developments have unfortunately shifted the focus from business development.

1.2 Regulatory activity

Is secured lending a regulated activity in your jurisdiction?

Lending is a regulated activity in Romania and may be carried out on a professional basis only by credit institutions and non-bank financial institutions licensed by the National Bank of Romania. EU licensed credit institutions may also provide lending in Romania on a professional basis by establishing a branch or being directly subject to passporting.

Lending on a professional basis without holding a proper licence constitutes a criminal offence.

Are there any specific regulatory issues which a prospective borrower should consider when arranging or entering into a secured loan facility?

As for any transaction, a prospective borrower should ensure that it has all necessary corporate approvals. The approval level should be set out under the borrower's articles of association; in practice, this is either a

shareholders' resolution or a board decision. In case of joint stock companies, a shareholders' resolution is mandatory if the facility exceeds:

- 50% of the book value of the assets for closed joint stock companies; or
- 20% of the total immobilised assets less receivables for listed joint stock companies

Are there any specific regulatory issues which a prospective lender should consider when arranging or entering into a secured loan facility?

Lenders that also intend to take the role of agent in connection with a facility should ensure that such business is covered by their licence.

Are there plans or proposals for reform or significant changes to the regulatory landscape in this area?

No.

2. Structuring a lending transaction

2.1 General

Who are the active providers of secured finance in your jurisdiction (eg, international banks, local banks or non-bank financial institutions)?

The usual mix of lenders is present in Romania. While international and multilateral development banks generally look for larger tickets, local banks aim to cover all segments of the market. Non-bank financial institutions are also active in secured finance and there are limited alternative lenders as well.

Is well-established market-standard facility documentation used in your jurisdiction for secured lending transactions?

There is no generally recognised Romanian law standard facility documentation (eg, similar to Loan Market Association (LMA) standards). Depending on the size and type of the transaction, lenders usually prefer either internally developed standard documents for bilateral loans and small deals or LMA-style facility agreements for syndicated or club loans.

2.2 Syndication

Are syndicated secured loan facilities typical in your jurisdiction?

Large Romanian companies have access to syndicated facilities (or club loans). However, in view of the usual size of Romanian companies, syndicated facilities are not as common as in developed or emerging markets.

How are syndicated facilities normally structured? Does the law in your jurisdiction allow a facility agent to be appointed to act on behalf of other banking syndicate members?

For syndicated facilities, the usual agency structure is used to appoint the facility agent. With regard to the security agent, several structures are used in practice, including:

- the joint creditorship between lenders structure, which enables the lender that is designated as security agent to enforce all claims of the syndicate against the borrower and the other obligors;
- the agency structure, under which the syndicate appoints the security agent to act as its attorney in fact in relation to the guarantees and security interests (this structure in particular is recognised by Romanian law for moveable mortgage agreements); and
- the parallel debt structure for foreign law-governed facility agreements, under which the borrower and the other obligors undertake towards the security agent to make all payments due to all lenders, but without affecting the rights of the lenders (although this has sometimes been assimilated to joint creditorship in relation to Romanian law guarantees and security interests).

Does the law in your jurisdiction allow security and guarantees to be held on trust by a security trustee for the benefit of the banking syndicate?

Romanian law recently recognised a concept similar to a trust – the fiducia. Unfortunately, the creation of a fiducia is onerous (involving special forms and various registrations and raising certain tax issues) and, as such, it has rarely been used in practice for taking security. Thus, in syndicated facilities security agents are more common than security trustees.

2.3 Special purpose vehicle financing

Is it common in secured finance transactions for special purpose vehicles (SPVs) to be used to hold the assets being financed? Would security generally be given over the shares in the SPV or would lenders require direct asset security?

For real estate and project finance transactions, it is common for financed assets to be held by SPVs. Security is generally taken over the shares in the SPV and the assets being financed, together with all other assets of the SPV (eg, immoveable assets, bank accounts and receivables).

For a standard acquisition financing structure, in the first stage there is a security interest over all shares in the target, created by the SPV holding the target, and a security interest over all present and future moveable assets of the same holding SPV; following a debt pushdown (by way of merger between the target and its holding SPV), there are additional security interests over all moveable and immoveable assets of the merged target and holding SPV.

2.4 Interest

Is interest most commonly calculated by reference to a bank base rate or a market standard variable reference rate (eg, LIBOR, EURIBOR or HIBOR)? If the latter, which is the most commonly used reference rate in your jurisdiction?

The interest rate is generally calculated by reference to:

- the Romanian Interbank Offer Rate for leu-denominated facilities;
- EURIBOR for euro-denominated facilities; and
- LIBOR for US dollar-denominated facilities

Are there any regulatory restrictions on the rate of interest that can be charged on bank loans?

In general, there are no regulatory restrictions. However, with regard to default interest, a law intended to combat late payments in commercial transactions provides that abusive clauses – for example, whereby the parties establish a default interest lower than the legal default interest (ie, the legal interest set by the National Bank of Romania plus eight percentage points) – are penalised with absolute nullity.

2.5 Use and creation of guarantees

Are guarantees used in your jurisdiction?

Yes, guarantees are generally used in Romania.

What is the procedure for their creation?

Guarantees may be granted by means of a private deed or included in the facility agreement. No registration is necessary (with the exception of applicable corporate approvals).

Do any laws affect or restrict the granting or enforceability of guarantees in your jurisdiction (eg, upstream guarantees)?

Under Romanian law, there are several limitations that a lender should bear in mind when structuring guarantees granted by other members of the borrower's group (and even third parties). These also apply to security interests.

First, as in other jurisdictions, financial assistance is prohibited in Romania. While the prohibition appears to be aimed at joint stock companies, it has been contended that it should also apply to limited liability companies.

Second, a guarantor should have a certain corporate benefit in relation to any guarantee granted to support liabilities of third parties. While there are no specific legal provisions setting out what constitutes an adequate corporate benefit for a company, the assessment should be undertaken by the management of the guarantor on a standalone basis, but may take into account the entire transaction and even the group relationship (although Romanian law does not recognise group benefit). In practice, a guarantee fee is often payable to the guarantor in order to mitigate corporate benefit concerns in relation to upstream or cross-guarantees to a certain extent.

Additional general company law limitations apply, including:

- a prohibition against distribution of dividends in advance (if a guarantee would be deemed as such);
- a prohibition against misuse of the guarantor's assets; and
- in relation to guarantees granted by joint stock companies, a prohibition against guaranteeing loans of directors or companies where such persons (or their spouses or relatives up to the fourth degree) are directors or shareholders of more than 20% of the share capital.

Breach of these rules will render the guarantee null and void and may even trigger criminal liability in certain conditions.

Finally, under Romanian law a guarantor should hold and maintain sufficient assets in Romania to cover the secured liabilities. However, there is a carve-out to this requirement – in particular, if the lender requests that a specific person act as guarantor (which is the rule in practice).

2.6 Subordination and priority

Describe the most common methods of structuring the priority of debts and security.

Romanian law provides for both the structural priority of liabilities (secured versus unsecured) and contractual priority, which is usually established by means of a subordination or intercreditor agreement.

2.7 Documentary taxes and stamp duty

Are any taxes, stamp duty or other fees payable on the granting of a loan, guarantee or security interest, or on its enforcement?

No stamp duty, registration duty or similar charge in connection with the granting and enforcement of finance documents is payable under Romanian law, with the exception of:

- court and enforcement fees for proceedings in relation to the finance documents;
- fees payable to the Electronic Archive (including the operator of the Electronic Archive) and any other public register for registration of the security documents;
- fees payable for the authentication by a notary public of an immoveable mortgage agreement;
- fees payable to the relevant land books for registration of an immoveable mortgage agreement; and
- fees payable to a certified translator and notary public in connection with notarised translations into Romanian of the finance documents, if applicable.

3. Cross-border lending

3.1 Governing law

Is it more common for local law to govern the terms of the facility documentation or is the law of another jurisdiction often elected by the parties (eg, English law or New York law)?

For cross-border lending, English law commonly governs facility agreements (particularly for large financings). Austrian banks typically use Austrian law-governed facility agreements for deals in Romania. However, Romanian law has been increasingly used of late.

3.2 Restrictions

Are there any restrictions on the making of loans by foreign lenders or the granting of security or guarantees to foreign lenders?

Romanian-resident borrowers should notify the National Bank of Romania for statistical purposes in relation to mid and long-term cross-border loans.

With regard to the enforcement of security interests by foreign lenders, certain limitations apply to enforcement by means of appropriation of the assets subject to the security interest (eg, in relation to immoveable assets).

Are there any exchange controls that restrict payments to a foreign lender under a security document, guarantee or loan agreement?

In principle, no. However, in theory, pursuant to the foreign exchange regulations the National Bank of Romania may impose certain foreign exchange control restrictions as safeguarding measures, which may restrict the

borrower's ability to make payments due under a facility agreement or the foreign lender's ability to exercise its rights against a borrower or remit the proceeds of enforcement. These restrictions may include:

- a requirement to notify the National Bank of Romania at least 10 days before performing short-term capital foreign exchange operations;
- thresholds and other limitations on short-term capital foreign exchange operations which trigger capital inflows and outflows;
- fees or commission on foreign exchange transactions on the interbank market for the purpose of performing capital operations which envisage the purchase or sale of foreign currency;
- restrictions on the repayment term of certain short-term capital foreign exchange operations; and
- restrictions on initiating new short-term capital foreign exchange operations).

4. Security – general

4.1 Security agreements

Is it possible to create a security interest over all assets of an entity? If so, would a single security agreement suffice or is a separate agreement required for each type of asset?

In general, three security interest agreements are available in relation to a secured lending transaction:

- a general moveable mortgage agreement, under which most types of asset can be covered (eg, bank accounts, stocks, inventory, receivables, intellectual property, intangible assets and universalities) – such an agreement can be split into various agreements for each type of asset;
- an immoveable mortgage agreement, under which all real estate of the borrower is mortgaged (depending on the deal, together with rent and insurance in relation to the real estate); and
- a share mortgage agreement, under which the shareholders of the borrower mortgage their shares in the borrower.

Depending on the actual financed assets, other arrangements may be available (eg, for aircraft, ships or financial collateral).

4.2 Release of security

What are the formalities for releasing security over the most common forms of assets?

The release of the security interests is generally straightforward: the secured lender issues a statement on the discharge of liabilities (in notarial form for immoveable mortgages), which is followed by deregistration from the relevant registers (eg, the Electronic Archive for moveable assets, the land book for real estate and the shareholders' register for shares).

5. Asset classes used as collateral for security

5.1 Real estate

Can security be granted over real estate? If so, what are the most common forms of security granted over real estate and what is the procedure?

Security interests may be created in relation to real estate by means of immoveable mortgage agreements authenticated by a notary public. The mortgage should be registered with the land book where the real estate is registered and, in the case of moveable assets attached to the real estate, with the Electronic Archive.

An immoveable mortgage is generally created by signing the mortgage agreement. However, with regard to real estate registered in land books for plots of land in locations where all cadastral works are finalised, registration of the mortgage agreement in the relevant land book actually creates the mortgage over the real estate (in practice, this scenario is uncommon).

From a practical perspective, the signatories of a secured lender should be appointed by means of a special power of attorney signed as a notarial deed (ie, the most solemn form of document in the jurisdiction where that power of attorney is signed).

5.2 Machinery and equipment

Can security be granted over machinery and equipment? If so, what are the most common forms of security granted over this kind of property and what is the procedure?

The moveable mortgage is the most common form of security over moveable assets such as machinery and equipment.

A moveable mortgage is validly created by means of a moveable mortgage agreement signed as a private deed (no notarisation is necessary). The mortgaged assets should be described precisely enough under the mortgage agreement to enable reasonable identification of the actual assets. This description can be made by:

- setting out lists of assets;
- stipulating specific classes of asset; or
- indicating criteria such as quantity or other specific formulas to this end.

In the case of universalities, the description should include the content and nature of the assets therein. A generic description of the mortgaged assets, such as "all moveable property" or "all present and future moveable property of the mortgagor", is no longer sufficient under the new security interests regime in force since 2011.

The enforcement of a moveable mortgage is subject to its perfection – that is, when:

- the mortgage becomes effective (ie, once the secured obligation is born and the mortgagor owns the mortgaged assets); and
- all publicity formalities are completed. For moveable mortgages in relation to machinery and equipment, such publicity is completed on registration with the Electronic Archive.

The ranking of a moveable mortgage is generally determined by reference to the time that the publicity formalities are performed (ie, registration with the Electronic Archive), irrespective of the time that the secured obligations are born. The registration with the Electronic Archive maintains its priority for five years and should be renewed before expiry of this period, if needed.

5.3 Receivables

Can security be granted over receivables? If so, what are the most common forms of security granted over this kind of property and what is the procedure?

Receivables may be subject to security under Romanian law, the most common type being a moveable mortgage. In practice, assignments for security purposes are also made (albeit increasingly less commonly) as an alternative to mortgages (such assignments are in any case assimilated to the legal regime governing moveable mortgages for most of their elements and characteristics).

Mortgages over receivables may be subject to additional perfection formalities, such as registration with the land book for real estate if they relate to relevant rent or insurance or notification to the mortgaged/assigned debtors if collection is transferred to the secured lender.

5.4 Financial instruments and cash

Can security be granted over financial instruments? If so, what are the most common forms of security granted over this kind of property and what is the procedure?

In general, security may be created in relation to shares in a Romanian company by means of a moveable mortgage. Mortgages over shares should be registered with the company shareholders' register, which is maintained by the company's directors or, in the case of listed companies, the Romanian Central Securities Depository.

For securities and collateral takers and creators that meet the eligibility criteria under the EU Financial Collateral Directive, as implemented in Romania, security over such securities (including shares in listed companies) may be taken in the form of financial collateral; however, this is rarely used in practice.

Can security be granted over cash deposits? If so, what are the most common forms of security granted over this kind of property and what is the procedure?

The most common form of security over cash is the moveable mortgage over bank accounts. For validity purposes, the bank account should be specifically set out under the moveable mortgage agreement. With regard to perfection of a mortgage over a bank account, the secured lender should hold control over the mortgaged bank account to ensure priority – such control is deemed to be held if:

- the secured lender is the account bank;
- the borrower, the account bank and the secured lender agree that the account bank will comply with the instructions of the secured lender regarding any amounts in the mortgaged bank accounts without the consent of the borrower; or
- the secured lender becomes the bank account holder or co-holder.

5.5 Intellectual property

Can security be granted over intellectual property? If so, what are the most common forms of security granted over this kind of property and what is the procedure?

IP rights may be subject to moveable mortgages. Mortgages over registered IP rights (eg, patents, trademarks and designs) should be registered with the Romanian State Office for Inventions and Trademarks.

6. Enforcement

6.1 Criteria for enforcement

What are the common enforcement triggers for loans, guarantees and security documents?

Following an event of default (and after expiry of any applicable cure period), a secured lender may in theory accelerate the entire outstanding loan and commence enforcement. In practice, lenders mainly use non-payment events of default as triggers for enforcement. There is little or no jurisprudence on acceleration and enforcement based on events of default such as failure to meet financial covenants, breach of representations and general undertakings and material adverse changes, among others.

6.2 Process for enforcement

What are the most common procedures for enforcement? Are there any specific requirements with which lenders must comply?

As a general principle, enforcement is subject to:

- the secured obligation being certain, liquid and payable;
- to holding of writs of execution; and
- the procedures set out under the Civil Code or the Civil Procedure Code (including authorisations by relevant courts and enforcement officers, registration of the commencement of enforcement with the Electronic Archive and notices to other creditors, if applicable).

Depending on the assets subject to the security interests, common methods of enforcement include:

- sale by public tender (with the price for the first tender being determined by a valuator, but with some price flexibility for subsequent tenders);
- sale of the mortgaged assets in a 'commercially reasonable' manner;
- appropriation of the mortgaged assets on account of the outstanding debt, with the consent of the borrower (and assuming no opposition by any other affected parties);
- a mere request addressed to the account bank to transfer to the secured lender any amounts existing in mortgaged bank accounts; and
- as a new but not tested method, taking over the mortgaged asset for administration purposes.

6.3 Ranking in insolvency

In what order do creditors rank in case of the insolvency of a borrower?

As a preliminary aspect, under Romanian law the opening of insolvency proceedings against a company generally suspends any enforcement against the company and its assets; enforcement can continue or re-commence only in limited cases (which are rarely seen in practice).

If an insolvent company is declared bankrupt and its assets liquidated, the secured lenders will have a general priority to the proceeds obtained from the sale of their duly perfected collateral, provided that such proceeds first satisfy:

- taxes, fees, costs and expenses arising from the sale of the assets (including operation and maintenance costs, expenses in connection with these assets that are incurred after the opening of the insolvency proceedings and judicial administrator fees); and
- claims of secured creditors which arise after the opening of the insolvency procedure (including the principal, interests and ancillary rights).

In theory, the secured lenders may even benefit from distributions performed before the sale of their collateral (such distributions being deducted from the amounts obtained following the sale of their collateral).

If the secured lenders are not fully satisfied following the sale of their collateral, the outstanding amounts will be deemed to be unsecured claims – which, as a rule, are paid in the following order:

- taxes, fees, costs and expenses of the insolvency procedure (including operation and maintenance costs and expenses, salaries for the necessary personnel and judicial administrator fees);
- claims under financings made available to the company during the insolvency proceedings;
- claims of employees;
- claims arising during the insolvency proceedings for carrying out the operations of the insolvent company, claims regarding damages for the termination of contracts during the insolvency and claims of good-faith third parties that have returned the assets subject to clawback or their value;
- budgetary claims;
- claims of third parties relating to alimony, minors' allocation or other regular subsistence payments;
- claims arising under bank loans or the supply of products, services or works, rent, or leasing arrangements and bonds (other than such claims of the insolvent company's group members);
- other unsecured claims (other than such claims of the insolvent company's group members); and
- subordinated claims, in the following order of priority:
  - claims of bad-faith third parties that have not returned the assets subject to clawback or their value and claims under shareholder loans if that creditor holds at least 10% of the insolvent company's share capital or voting rights in the general meetings of shareholders; and
  - claims under free-of-charge acts.