



## NEW FRENCH LEGAL FRAMEWORK ON COVERED BONDS

The French Parliament adopted on October 11, 2010, the law on banking and financial regulation (*'loi de regulation bancaire et financière'*) which (i) creates a new type of covered bond issuer, the *Société de Financement de l'Habitat* (the '**SFH**') to exist beside the existing *Sociétés de Crédit Foncier* (the '**SCF**') and (ii) improves liquidity management for both categories of covered bond issuers. This law has been published on October 22, 2010.

The SFH will exist alongside the other current issuance entities: SCF (*Société Crédit Foncier*) and CRH (*Caisse de Refinancement de l'Habitat*). SFH will be a credit institution licensed and supervised by the French regulator (*Autorité de Contrôle Prudentiel*, '**ACP**').

A new category of French legislative covered bonds is now created under the name of '*Obligations à l'Habitat*' ('**OH**') to be issued by SFH.

The recent legislative changes are primarily based on the rules governing German *Pfandbriefe* and will soon be codified under Articles L.515-13 *et seq.* of the French Monetary and Financial Code for the SCF, with a new Section 5 of Chapter V of Book 5 of the French Monetary and Financial Code created for the SFH).

### Background

Created for the first time in December 2006 by BNP Paribas, structured covered bonds in France are based on the general French legal framework and use the collateral directive for the transfer of legal title on the home loans to the issuer of the covered bonds. This structure prevents any operational issues linked to the true sale of the underlying home loans.

The main reason for the current French legislative reform is to allow the general French law-based covered bonds to become legislative covered bonds and, therefore, fully compliant with the UCITS-directive.

The existing 'structured' covered bonds issued by various French retail banks to refinance French home loans are all expected to be converted into OH after the implementation of the recently approved legislation. This conversion must be notified to the ACP within 12 months following the law's publication.

From now on, under French law, SCF and SFH will both be considered as issuing legislative covered bonds and will satisfy the requirements of Article 22 (4) of the UCITS Directive of December 20, 1985. This will allow certain investors to increase the amount of assets they can invest in OH from the current 5% limit to 25% (UCITS) or 40% (insurers).

These law changes are expected to further improve the already strong perception of French covered bonds in the market.



## Key points of the reform

### IMPROVEMENTS OF LIQUIDITY MANAGEMENT

Various improvements are implemented in the law and will be valid for both SCF and SFH. This includes improving liquidity instruments such as:

- ◆ a requirement to cover all liquidity needs for next 180-day period on an ongoing basis;
- ◆ a minimum 2% level of over collateralization; and
- ◆ possibility for issuers to use up to 10% of covered bonds issued for ECB repo operations.

### CREATION OF THE SFH LEGAL FRAMEWORK

As is already the case with the SCF, the future SFH will be licensed and supervised credit institutions. Unlike the SCF legislation which limits the percentage of guaranteed home loans (currently 35% of total assets), the SFH legislation has been drafted to reflect the development of the French home loan market and will not limit the percentage of guaranteed home loans in the issuer's assets.

Once the law enters into force existing issuers will have a 12-month period to apply for a license as an SFH and convert their existing covered bonds into OH. One of the key requirements for this legal status conversion is that each SFH must appoint a specific controller to replace the existing asset monitor.

SFH will be subject to the same strict criteria in terms of asset eligibility, supervision, control and license requirements as already existed in the 1999 French covered bond law. The control over cover pool assets and guarantors will be further tightened under the SFH regime with the appointment of the specific controller.

Investors in OH issued by SFH will benefit from the same statutory privilege (*'legal privilège'*) regarding the assets that investors in OFs already have over assets of the SCF.

The main differences between SFH and SCF will be that:

- ◆ only residential home loans are eligible for cover pool assets of SFH while SCF can also refinance public sector exposures, alongside residential home loans (with a limit of 35% for guaranteed home loans);
- ◆ the transfer of legal title to the SFH will be based on the EU Collateral Directive, as opposed to transfer by true sale or securitization law used in SCFs; and
- ◆ the risk weighting under the CRD standard approach of OHs will remain at 20% (vs. 10% for OFs) as SFH will not be compliant with the current CRD due to the level of guaranteed home loans.



## The new framework at a glance

MAIN FEATURES	Structured Covered Bonds Issuers	SFH	SCF
	<b>NEW LEGAL FRAMEWORK</b>		
Legal form	specialized credit institution with an exclusive purpose		
	licensed as financial company	licensed as ' <i>société de financement de l'habitat</i> '	licensed as ' <i>société de crédit foncier</i> '
Supervision	supervised by the ACP; controls by an asset monitor; reviews by external auditors	supervised by the ACP; controls by a specific controller; reviews by external auditors	
Composition of the asset pool	Only residential home loans, without limitation for guaranteed home loans		Residential home loans and commercial real estate loans (with 35% limitation on guaranteed loans) and public entity exposures
Transfer of the assets to the issuer	collateralized loan agreements, home loans are granted as financial collateral security to secure the loans (securitisation and true sale also possible)		(i) true sale or securitization and (ii) possibility of collateralized loan agreements for public entity exposures only
Ring fencing	contractual ring fencing mechanism non recourse – non petition clauses	legal ring fencing mechanism expressly stating that the opening of insolvency proceedings against a company holding shares in an SCF/SFH may not be extended to the issuer.	
Priority of payments	common pledge	legal privilege (senior ranking priority) over all of the assets of the issuer to the benefit of the covered bond holders and swap counterparties on a pari passu basis	
Risk weighting	20%		10%
UCITS compliance	No	Yes	
Liquidity	contractual requirements	(i) legal requirement to cover all liquidity needs for next 180-day period on an ongoing basis – (ii) minimum 2% level of over-collateralization – (iii) possibility for issuers, if need be, to use ECB repo facilities	
Issuance program	AAA rated EMTN issuance programs		



## Further regulations pending

Attention is also drawn to the fact that a forthcoming decree and regulations are expected in the near future.

## Contacts

Please do not hesitate to contact us should you have any questions or require any additional information:

**Boudewijn Dierick**, Head of Covered Bond Structuring, BNP Paribas  
[boudewijn.dierick@bnpparibas.com](mailto:boudewijn.dierick@bnpparibas.com)

**Alexis Latour**, Head of CIB Legal Funding and Securitisation team, BNP Paribas  
[alexis.latour@bnpparibas.com](mailto:alexis.latour@bnpparibas.com)

**Diane Jammaron**, Legal Counsel, CIB Legal Funding and Securitisation, BNP Paribas  
[diane.jammaron@bnpparibas.com](mailto:diane.jammaron@bnpparibas.com)

*By reading this document, you agree to be bound by the limitations herein. This presentation is being supplied to you solely for your information. This document is intended to provide non-exhaustive, general legal information. This document is not intended to be and should not be construed as providing legal advice. This presentation, and the information disclosed herein, is provided on a confidential basis and may not be further copied, distributed or passed on to any other person or published or reproduced directly or indirectly, in whole or in part, by any medium or in any form for any purpose. BNP Paribas Home Loan Covered Bonds and BNP Paribas take no responsibility for the use of these materials by any person.*

*Some information contained herein and other information or material may include forward-looking statements based on current beliefs and expectations about future events. Any forward-looking statement contained in this document speaks as of the date of this document. BNP Paribas undertakes, does not have any obligation, to publicly revise or update any forward-looking statements in light of new information or future events.*

*The information contained in this document as it relates to parties other than BNP Paribas Home Loan Covered Bonds or BNP Paribas has not been independently verified and no representation or warranty expressed or implied is made as to, and no reliance should be placed on the fairness, accuracy, completeness or correctness of, the information or opinions contained herein. None of BNP Paribas Home Loan Covered Bonds, BNP Paribas or their advisors or their representatives shall have any liability whatsoever in negligence or otherwise for any loss however arising from any use of this document or its contents or otherwise arising in connection with this document or any other information or material discussed.*