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Amendments to the Luxembourg Financial Collateral Law

On 24 July 2022, the Luxembourg law of 20 July 2022 (the “Law”) entered into force amending, among others, the law of 5 August 2005 on financial collateral arrangement. It promotes the attractiveness of Luxembourg as a creditor-friendly jurisdiction and emphasises contractual freedom and legal security.

The Law aims to clarify and consolidate market practices regarding financial collateral arrangements governed by Luxembourg law. These amendments aim to reinforce, among other aspects, the provisions relating to the enforcement of financial collateral arrangements.

The main amendments introduced by the Law are as follows:

1. Clarification of enforcement event

The legislator amended the definition of “enforcement event” by clarifying that any event (“whatsoever”) that has been agreed upon by the parties in connection with a financial collateral arrangement can be used as an enforcement event.

This confirms and clarifies that occurrences other than payment defaults may serve as an enforcement event (i.e. violations of financial ratios or other specific aspects of the transaction, etc.).

2. Enforcement event where financial obligations are not due and payable

In case there is an enforcement event where the underlying financial obligations are not due and payable, the proceeds of the realisation shall be applied to discharge such financial obligations unless the parties have agreed otherwise. This clarifies how proceeds of the enforcement are to be used in such a scenario but also reinforces the autonomy of financial collateral arrangements by giving total freedom to the involved parties to organise things differently.

3. Public auctions

The Financial Collateral Law originally stated that if the involved parties agreed that the enforcement of a financial collateral arrangement had to be done by means of a public auction, the auction would be performed in the Luxembourg Stock Exchange. The new Law establishes that public auctions will now be conducted by a bailiff or by a notary following a detailed new procedure. This will permit effective recourse to this enforcement procedure which was previously not used in practice given the practical difficulties.

4. Sale of pledged assets admitted to trading

In connection with enforcement by way of selling pledged assets admitted to trading, the legislator has replaced the reference to “sale on a stock exchange” with “sale on a trading platform”. This change aims to extend the types of platforms on which a sale of the financial instruments can occur insofar as these financial instruments are admitted to trading on such a platform. This includes financial instruments

admitted to trading on a regulated market but also on Multilateral Trading Facilities or on an Organised Trading Facility in Luxembourg, Europe or in a third country.

5. Insurance contracts

The Law expressly authorises granting pledges over insurance contracts. The collateral taker may enforce such financial collateral by exercising all the rights arising under the collateralised insurance contract, including, in the case of life insurance, the right to surrender the contract or to demand payment from the insurance company of any sums due under it.

However, a pledge over a Luxembourg life insurance contract would still need to comply with Articles 116 and 117 of the Luxembourg law of 27 July 1997 on insurance contracts. These articles establish that life insurance contracts may only be pledged by an endorsement signed by the policyholder, the collateral taker and the insurer and, where the benefit of a life insurance contract has already been accepted, with the consent of the beneficiary.

6. Collective investment undertakings

The legislator introduced an additional enforcement method regarding collateralised units or shares in a collective investment undertaking. If the units or shares are admitted on a trading platform, they can be appropriated at their market price. If they are not admitted on a trading platform the redemption price is determined in accordance with the constitutional documents of the relevant collective investment undertaking.

7. Inapplicability of sequestration in enforcement of financial collateral arrangements

Finally, the Law strengthens the enforcement of a financial collateral arrangement by means of adding "sequestration" to the existing measures (i.e. civil, criminal or judicial, or penal confiscation) which do not apply to collateral arrangements governed by the Financial Collateral Law. Sequestration does not therefore prevent enforcement.

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