

## PROFESSIONAL PAYMENT GUARANTEES – A NEW TOOL FOR RISK TRANSFERS UNDER LUXEMBOURG LAW

Historically, guarantees in Luxembourg law have taken either the form of an accessory suretyship (*cautionnement*) or an autonomous first demand guarantee (*garantie autonome*). Each of these has presented its own issues in commercial contexts, including synthetic securitisations, that have sometimes required complex structuring to deal with. A new law has now introduced a third type of guarantee, the "professional payment guarantee", that should avoid most of these issues and thereby permit simpler structures. In this briefing, we review the historic issues with the use of guarantees in Luxembourg, describe how the new professional payment guarantee can be used and how it will help address those historic issues.

A Luxembourg law dated 10 July 2020 has introduced a new guarantee instrument named "professional payment guarantee". This instrument is described in the law as an undertaking by which the guarantor commits to pay, at the request of the beneficiary (or of an agreed third party), a sum determined according to the terms agreed, in relation to one or more claims or the risks related to such claims. The main aim of the law is to create an instrument parties can use freely, according to agreed terms, to guarantee any kind of claims or their associated risks. As a result, this instrument is of interest to those structuring securitisation transactions, especially in the field of synthetic risk transfer transactions.

While those accustomed to English law guarantees will not be surprised by the features of this type of guarantee (and may wonder why a legislative intervention was necessary), readers familiar with Luxembourg law (and other civil law systems, including French law) will be aware of the historic distinction between the accessory suretyship (*cautionnement*) and the autonomous first demand guarantee (*garantie autonome*), the difference being mostly around the ability to reference the underlying obligations combined with the potential (or absence thereof) to waive defences arising from the underlying obligations. This historic distinction created certain challenges in the structuring and documentation of guarantees especially for the purpose of risk transfers in the

### Key issues

- The professional payment guarantee is a new type of guarantee introduced in July 2020
- It is simple and flexible to use, requiring only that the parties clearly specify the desired terms of the guarantee in writing and that it references the new professional payment guarantees law

context of securitisation transactions and portfolio guarantees. This is because there was a risk, where the criteria of an autonomous guarantee were not fulfilled, that it would be recharacterised as an accessory guarantee – leading to full application of the consequences of this accessory nature.

While this issue could be overcome in the past, this sometimes required complex structuring. By contrast, the professional payment guarantee law now expressly allows transaction parties to combine elements of accessory and autonomous instruments to create "hybrid" guarantees, which are fully adapted to the commercial requirements of the specific transaction.

As an example, parties are free to waive all defences or only some of them, to make reference to the underlying obligations while still maintaining a full waiver of defences, and to determine as they wish the terms and modalities of payment and call events under the professional payment guarantee.

There is no express restriction on the scope of use for professional payment guarantees, although in light of the name of the instrument this tool is intended to be used in the context of professional transactions. Nor are there burdensome formal requirements, as the law only requires parties to be able to evidence the guarantee in writing (which can be achieved through electronic documentation) and to indicate expressly that the guarantee is subject to the new law. Indeed, the law does not abolish any of the other already existing guarantee instruments - it is therefore necessary for legal certainty that parties expressly agree to the application of the law and thereby characterise their instrument as a professional payment guarantee.

Other notable features of the professional payment guarantee include clarification of the existence of rights of recourse and subrogation (which can be waived by the parties) and confirmation of the continued effectiveness of the guarantee in case of insolvency proceedings affecting the debtor of the underlying obligations, except where the law specifically provides otherwise (which is the case in Luxembourg for the overindebtedness regime for private individuals).

Finally, the law also clarifies that such professional payment guarantees can be granted to intermediaries such as agents or trustees acting on behalf or for the benefit of the creditors, which is clearly relevant and helpful for securitisation transactions.

The professional payment guarantee is necessarily governed by Luxembourg law. The usual rules (Rome I Regulation) will determine the conditions for the recognition of the choice of governing law in international transactions.

In summary, the law seeks to ensure that parties are free to contractually determine the terms of their guarantee tool in light of the requirements of their transaction, without running the risk that their arrangements will be recharacterised such that they no longer reflect the commercial purposes for which they were entered into.

The law therefore provides an interesting structuring tool for securitisation transactions which parties wish to have governed by an EU civil law system. It may also be used in the context of the well-known 2004 Luxembourg law on securitisation, in particular the provisions which expressly contemplate the use of guarantees as a risk transfer mechanism.

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