Securitisation of African assets through the UAE

Sakshi Puri - Partner - Banking and Finance
s.puri@tamimi.com - Dubai International Financial Centre

Murtaza Hussain - Associate - Banking and Finance
- Dubai International Financial Centre

Introduction

During a liquidity crisis, such as the one faced currently due to the COVID-19 pandemic, companies in developing countries increasingly need innovative ways to raise finance. This article focuses on one such mechanism, i.e. asset-backed securitisation of future-flow receivables generated by African operating companies (commonly referred to as 'originators') using the UAE as a conduit jurisdiction. This type of mechanism provides a means of securing credit by utilising a special purpose vehicle structure provided by the financial free zones of the UAE and thereby reducing the cost of funding. In recent times we have seen an increasing interest among foreign investors and borrowers in using this structure in the UAE for securitising receivables originating in Africa.

Common UAE structure and benefits

Generally, a future cash flow securitisation structure entails a borrowing entity selling its future product (i.e. the receivable) directly or indirectly to an offshore Special Purpose Vehicle ('SPV'). The SPV obtains borrowing to be able to purchase the receivable or issues debt instruments. Designated international customers are directed to act as collection agents and pay for the exports from the originating entity directly to an offshore collection account managed by a trustee. The collection agent makes principal and interest payments to the investors and directs excess collections to the originator.

The innovative structuring of these transactions has allowed many investment grade borrowers in developing countries to obtain financing at significantly lower interest costs and for a longer duration. In addition to future flow. securitisations also attract a much wider class of investors because of their potential investment grade rating possibilities. Furthermore, by establishing a credit history for the borrower, these deals enhance the ability to and reduce the costs of accessing capital markets in future.

In the past, we have discussed (here) how the financial free zones in the UAE i.e. the Abu Dhabi Global Market ('ADGM') and Dubai International Financial Centre ('DIFC') have played a pivotal role in attracting interest in using the UAE as a base to launch a securitisation transaction by providing the option of a flexible, robust, simple and efficient SPV regime that is well suited as a legal entity for securitising a portfolio of assets. Since then, we have seen a steady increase in the appetite of local and foreign investors to use DIFC and ADGM vehicles as a centre piece to drive their securitisation transactions globally.

Under the laws applicable onshore in the UAE, the restrictions on foreign shareholding and filing requirements often make it difficult for foreign investors to set up an onshore SPV and implement a securitisation transaction. Also, UAE law does not recognise the notion of a trust removing the availability of a critical structuring tool employed in securitisation. However, the basis of the ADGM and DIFC legal frameworks is English common law which means that trust structures can be used in connection with its

SPV regime.

Trailblazing deal

We have recently acted for a multi-national group in converting their illiquid assets from eleven African subsidiaries to liquid cash flow under a securitisation structure ('Africa Securitisation'). In this transaction, the receivables were purchased through an orphan special purpose vehicle that facilitated an off-balance sheet securitisation structure. We worked closely with the counsel in Ghana, Ivory Coast, Kenya, Nigeria, Senegal, Tanzania, Uganda and Zambia to ensure the Africa Securitisation was fully aligned with local laws. In particular, we engaged with local counsel to ensure that the securitisation was perfected in each jurisdiction to satisfy the requirements for completing a "true sale". The Africa Securitisation was well received in the banking and finance industry and has boosted UAE investor confidence in African securitisation transactions that are routed through the UAE from a recognition and overall viability perspective. In terms of recognition in Africa, we have received a vote of confidence from the local counsel in the jurisdictions mentioned above on the recognition and enforceability of such transactions at the originator level.

Key takeaways

Like all transactions, various facets need to all work in perfect harmony for a securitisation to not only provide a watertight enforcement mechanism for the investors but also to effectively meet the commercial objectives of the borrower. Some key takeaways for us from the Africa Securitisation are set out below. These have become some the key guiding principles to bear in mind when securitising assets through the UAE:

1. **Collateral**: By design, SPVs are incorporated for two key purposes, (i) holding assets sought to be transferred by the originator and such assets, once transferred, are ring fenced for the benefit of the beneficiaries of the SPV; and (ii) the issuance of financial instruments by the SPV, providing exposure to the underlying assets transferred to the SPV. Therefore, transactions that are structured through SPVs are heavily driven by the value of the underlying assets and the ability of the investors to establish control over the financial instruments issued by the SPV and eventually, the securitised assets. We believe this is a critical consideration when creating a collateral package in a securitisation.
2. **Taxation**: The ability of the borrowing SPV and the underlying originator to meet its payment obligation under a securitised transaction is greatly dependent on the applicability of taxation legislation to (i) the amounts paid to the originator as a consequence of the securitisation; (ii) the amounts payable by the originator (as collection agents) to the borrowing SPV once the future recievables have been recovered from the end customers. Any deductions in payments could impact the commercial viability of the transaction if they affect the amounts that the investors would realise from the SPV.
3. **End customers**: Given the source of payment to the investors in securitised transactions are the end customers, it is important for the investors or the collateral agent to have some degree of a contractual relationship with the end customers. This ensures that in an enforcement scenario, the investors have the ability to obligate customers to pay directly to the investors. These step-in rights of the investors can be built into the collateral package of the transaction. Depending on the laws of the jurisdiction where the receivables are originating the end customers would need to either be notified or consent to such step-in rights of the investors or their collateral agent.

Closing thoughts

It has been noted in a report published by the World Bank on development financing and securitisation of future receivables that it is essential for countries where the borrowing SPV are located to provide certain institutional and legal protections to investors in a securitised transaction. In general, it is difficult to structure securitised transactions in countries that have limited legislation. Typically, this results in greater doubt and uncertainty which makes it more difficult to structure a deal. Bankruptcy law, in particular, is crucial for securitised transactions. In this regard, the DIFC and ADGM provide certain key advantages in the context of such transactions such as: (a) an independent courts' system; (b) clear and robust bankruptcy protocol; and (c) a generally investor friendly business infrastructure (for example, an efficient process for set-up, no restriction on the number of shareholders of a SPV, a fully digital registration process, no attestation requirement for corporate documents, etc). All of these factors have incentivised investors to use SPVs incorporated in the DIFC and ADGM for their securitisations.

We regularly advise clients, comprised of both local and international investors and borrowers, in the automobile, healthcare and petroleum sectors in structuring securitisations and financing transactions. We have also assisted in incorporating SPVs to act as a conduit between the assets and the ultimate investors, making the holders of the securities the ultimate beneficiaries of the underlying asset.

For further information, please contact Mamoon Khan (m.khan@tamimi.com), Sakshi Puri (s.puri@tamimi.com) or Murtaza Hussain (m.hussain@tamimi.com).