

Subscription-secured financings: enforcements vs perfection - Luxembourg

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Subscription-secured financings in Luxembourg: enforcement vs. perfection

This article formed part of a report originally produced with Haynes and Boone LLP titled Subscription-Secured Financings: Enforcement vs Perfection (European Deals Edition). You can see links to Ogier's other chapters below and find the original report [here](#).

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Perfection and enforcement under the laws of the Grand Duchy of Luxembourg

Like in the UK, the security package granted by the fund in a subscription credit facility will generally include:

- a pledge over the rights of the general partner to call the uncalled capital commitments of the investors and to enforce any associated rights; and
- a bank account pledge over the deposit account into which the investors deposit the proceeds of the capital calls.

Perfection of security

The pledge of the right to call capital from investors in respect of their uncalled capital commitments is perfected under Luxembourg law by the mere conclusion of the pledge agreement listing the pledged capital commitments between the fund and the security agent. However, an investor may nevertheless validly discharge his payment obligation under the subscription agreement as long as he has no notice of the security interest. Notification of the pledge is therefore highly recommended, and market standard, even if not strictly required for security perfection purposes. The notice should be provided by the fund on the date of closing or as soon as possible thereafter to ensure the priority of the security interest. To perfect the bank account security under Luxembourg law, the account bank must be notified of the pledge and asked to relinquish any rights of set off, combination of accounts or first ranking pledge in the respect of the account collateral which would otherwise apply in standard account bank terms and conditions. When the account bank is the lender itself, the perfection requirements can be dealt with in the security agreement directly.

Enforcement of security

Under Luxembourg law, enforcement may be carried out by the lender as a secured party by way of private action, without requiring any court order or the involvement of any public or judicial officer or notary.

Upon enforcement, the secured party will be able to deliver drawdown notices to the investors in lieu and place of the fund's general partner (or manager, depending on the fund documents).

In addition to the right to call capital, a secured party will also be granted the right to enforce the obligations of the investors to fund the capital commitments.

Finally, the secured party will be able to take control of the collection account pursuant to the bank account pledge agreement.

To facilitate the enforcement process, the Luxembourg law of 5 August 2005 on financial collateral arrangements (the 2005 Law) disapplies the Luxembourg civil law requirement for a formal default notice (*mise en demeure*) to be served prior to enforcement, although the contractual facility agreement terms will often entail a notice of acceleration and demand in any event. Certainty is further enhanced by the 2005 Law's disapplication of the laws of both Luxembourg and other jurisdictions relating to bankruptcy, liquidation, reorganisation or similar measures and from any civil, criminal or other judicial attachment or confiscation court order. All legal risks of nullity of the security or unenforceability against third parties, arising from such matters, are thus disapplied except in relation to civil liability for conspiracy to defraud and in relation to an insolvency cause of action pursuant to a fraud on creditors. Accordingly, in the absence of fraud, the relevant Luxembourg security and its enforcement provisions are binding on any insolvency office-holders and the secured assets fall outside the bankruptcy estate of the grantor, and is enforceable by private action of the secured party despite the opening of any bankruptcy

proceedings against the grantor, and, importantly, is not vulnerable to being set aside by reason of any hardening period (période suspecte). The result is an attractive, secure legal framework that strongly benefits the secured finance parties in transactions involving Luxembourg entities granting security, and consequently, fund promoters seeking investment financing solutions.

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