

THE SECURITISATION & STRUCTURED FINANCE HANDBOOK 2025



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Hong Kong as an international hub for China securitisations

By Kingsley Ong, Secretary General, APSA, and Tony Lau, Associate, CMS Hong Kong

THE CHINA SECURITISATION MARKET HAS GROWN EXPONENTIALLY IN THE LAST DECADE. IN THE LAST FEW YEARS, CHINA'S ANNUAL SECURITISATION ISSUANCE AVERAGED US\$355BN, AND THE OUTSTANDING BALANCE OF SECURITIES AT THE END OF 2022 WAS REPORTED TO BE ABOUT US\$670BN.¹ THIS MAKES CHINA THE WORLD'S SECOND LARGEST SECURITISATION MARKET AFTER THE US.

However, China's securitisation market remains largely domestic. While there are efforts to make the CNY currency more internationalised and increase participation from international investors by opening new channels for cross-border investment,² these remain restricted.³

Another potential impediment is the perceived lower level of legal certainty due to China's relatively new civil law system (which originated in 1949 after the Communist Party took over control of China).⁴

If these challenges can be overcome, China's economy and securitisation market have the potential to overtake the US and continue its exponential upward trajectory for many years to come.

This article will examine, from a legal enforcement perspective, Hong Kong's unique position to become an international securitisation hub for China and beyond.

Hong Kong's Common Law system

Hong Kong is one of the freest economies in the world.5

Following Hong Kong's return of sovereignty to China in 1997, Hong Kong became a special administrative region under the People's Republic of China ("China"). Based on the principle of "One Country, Two Systems", which is

enshrined in the Basic Law (Hong Kong's constitutional document), Hong Kong's legal system operates independently from that of Mainland China with a high degree of autonomy.





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Article 8 of the Basic Law provides that "[The] law previously in force in Hong Kong, that is, the common law, rules of equity, ordinances, subordinate legislation and customary law shall be maintained, except for any that contravenes this [Basic] Law, and subject to any amendment by the legislature of the Hong Kong Special Administrative Region."

Hong Kong is unique as the only place in China that has a common law system. Hong Kong's common law system is based on the British legal system, and inherits all the benefits of the English common law (such as predictability, creditor orientation, and insulation from change of law in debtor countries).

Asset-backed securitisation involves the pooling and isolation of various financial assets, such as mortgages, loans or receivables, and issuing of securities backed by those assets. In China cross-border securitisations, the underlying assets would be located in Mainland China, and international investors would want legal certainty that they have recourse to those assets in Mainland China in the event of distress.

For China cross-border securitisations to be appealing to international investors, there must be a robust legal framework that gives legal certainty to protect and treat international investors' rights fairly - not just in good times, but also in distress times.

The cross-border elements in international securitisation adds complexity for legal predictability. Different jurisdictions have different laws concerning the recognition and enforcement of contractual obligations, which may impact the ability of investors to recover their investments in a default situation.

Arbitration

Arbitration has become a popular dispute resolution option for international investors into China. This is because China is a member of the *United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards* ("New York Convention").⁷ This means that arbitral awards made in over 170 jurisdictions around the world (that are

members of the New York Convention) are enforceable in Mainland China.

Through China's membership of the New York Convention, the New York Convention applies to Hong Kong. Previously, some doubts were expressed over whether the New York Convention would apply between Hong Kong and Mainland China, because Hong Kong is not a separate sovereign state from Mainland China and the New York Convention only applied between sovereign states.8 To remove any uncertainty on the mutual enforcement of arbitral awards between Mainland China and Hong Kong, two arrangements were concluded, namely:

- 1. Arrangement Concerning Mutual Enforcement of Arbitral Awards between the Mainland and the Hong Kong Special Administrative Region《关于内地与香港特别行政区相互执行仲裁裁决的安排》which was entered into force on February 1, 2000; and
- Supplemental Arrangement Concerning Mutual Enforcement of Arbitral Awards between the Mainland and the Hong Kong Special Administrative Region《关 于内地与香港特别行政区相互执行仲裁裁决的补充安 排》which was entered into force on November 27, 2020 and May 19, 2021.

Nonetheless, arbitration *per se* has its limitations. For example, arbitration tribunals may not have jurisdiction to override the application of insolvency laws of Mainland China if a Mainland China originator or issuer of securitisation bonds goes insolvent.⁹ This brings us to the next highlight.

Cross-border recognition and enforcement regime between Hong Kong and Mainland China

Under Article 95 of the Basic Law, "the Hong Kong Special Administrative Region may, through consultations and in accordance with law, maintain juridical relations with the judicial organs of other parts of the country, and they may render assistance to each other."

Since 1997, Hong Kong and Mainland China have concluded several agreements to enhance mutual judicial assistance

between two jurisdictions, including three recent Arrangements that concern courts in Hong Kong and Mainland China:

- Arrangement Concerning Mutual Assistance in Court-ordered Interim Measures in Aid of Arbitral Proceedings by Courts of Mainland China and Hong Kong《关于内地与香港特别行政区法院就仲裁程序相 互协助保全的安排》which was entered into force on 1 October 2019 ("Interim Arrangement (Arbitration)");
- 2. The Record of Meeting of the Supreme People's Court and the Government of Hong Kong (concerning the mutual recognition and assistance for bankruptcy/insolvency proceedings between the courts of Mainland China and Hong Kong)《最高人民法院与香港特别行政区政府关于内地与香港特别行政区法院相互认可和协助破产程序的会谈纪要》which entered into force on May 14, 2021 ("Record of Meeting (Insolvency Recognition)"); and
- 3. Arrangement on Reciprocal Recognition and Enforcement of Judgments in Civil and Commercial Matters by the Courts of Mainland China and Hong Kong《关于内地与香港特别行政区法院相互认可和执行民商事案件判决的安排》signed on January 18, 2019 and which entered into force on January 29, 2024 ("Reciprocal Arrangement").

Interim Arrangement (Arbitration)

A groundbreaking development in 2019 enhanced Hong Kong's position as an international arbitration hub. Under the Interim Arrangement (Arbitration), which came into effect on October 1, 2019, if Hong Kong is chosen as the seat of arbitration and the arbitral proceedings is administered by a designated arbitral institution in Hong Kong, arbitration parties may apply to the Mainland China courts for interim measures to aid the arbitration proceedings. Such interim measures include property preservation, evidence preservation and conduct preservation. Hong Kong is the first and only jurisdiction in the world (outside Mainland China) to have this arrangement with Mainland China.

Pursuant to Article 3, any party to arbitral proceedings seated in Hong Kong and administered by a 'qualified arbitral/dispute resolution institution in Hong Kong' (as defined in Article 2 of the Interim Arrangement (Arbitration)) may, prior to the issuance of the arbitral award, apply to the Intermediate People's Court of the place of residence of the respondent against whom the application is made or the place where the property or evidence is situated, for interim measures in accordance with the PRC Civil Procedure Law, PRC Arbitration Law and relevant rules.¹⁰

Article 2 of the Interim Arrangement (Arbitration) stipulates the requirements for qualified institutions or permanent offices, for the purpose of considering whether it falls within the definition of "arbitral proceedings in Hong Kong":

- "(1) arbitration institutions established in the HKSAR or having their headquarters established in the HKSAR, and with their principal place of management located in the HKSAR;
- (2) dispute resolution institutions or permanent offices set up in the HKSAR by international intergovernmental organisations of which the People's Republic of China is a member; or
- (3) dispute resolution institutions or permanent offices set up in the HKSAR by other arbitral institutions and which satisfy the criteria prescribed by the HKSAR Government (such as the number of arbitration cases and the amount in dispute, etc.)"

A list of institutions and permanent offices qualified under Article 2 of the Interim Arrangement is published at the website of the Hong Kong Department of Justice.¹¹ This includes popular arbitration institutions such as The Hong Kong International Arbitration Centre (HKIAC).

Article 4 provides for the documentary requirements for an applicant applying to a People's Court in Mainland China for interim measures:

- 1. The application for interim measures;
- 2. The arbitration agreement;
- 3. Documents of identity; where the applicant is a natural

person, a copy of his/her identity card is to be submitted; where the applicant is a legal person or an organisation which is not a legal person, copies of its certificate of incorporation or registration and the identity card(s) of its legal representative(s) or responsible person(s) are to be submitted;

- 4. Where a party makes an application for interim measures after the relevant institution or permanent office has accepted the arbitration case, the request for arbitration setting out the main claim of the arbitration and the facts and justifications on which the claim is based, together with the relevant evidential materials, as well as a letter from the relevant institution or permanent office certifying its acceptance of the relevant arbitration case;
- 5. Any other materials required by the People's Court of Mainland China.

Where a document of identity is issued outside Mainland China, such document of identity needs to be certified in accordance with the provisions of the relevant laws of Mainland China.

The above Arrangement enables parties to protect assets across the border in the midst of arbitration proceedings, lowers the risks of dissipation of assets and protects the outcome of the agreed dispute resolution process.

Record of Meeting (Insolvency Recognition)

The Record of Meeting (Insolvency Recognition) was signed between the Supreme People's Court and the Hong Kong Government on May 14, 2021. In relation to the implementation of the Record of Meeting in the Mainland, the Supreme People's Court has designated Shanghai, Xiamen and Shenzhen as pilot areas.

Under the pilot scheme, a liquidator or a provisional liquidator appointed in Hong Kong may apply to the relevant Intermediate People's Court in Shanghai, Xiamen and/or Shenzhen for recognition and assistance. This pilot cross-border insolvency recognition arrangement only applies to three types of insolvency proceedings in Hong Kong, namely, compulsory winding up, creditors' voluntary

winding up and corporate debt restructuring proceedings brought by a liquidator or provisional liquidator and sanctioned by a court in Hong Kong.

The Supreme People's Court issued an "Opinion on Taking Forward a Pilot Measure in relation to the Recognition of and Assistance to Insolvency Proceedings in the Hong Kong Special Administrative Region"《最高人民法院关于开展认可和协助香港特别行政区破产程序试点工作的意见》(the "Opinion"),where the Supreme People's Court opined that the new pilot scheme applies to Hong Kong insolvency proceedings provided that Hong Kong is the centre of main interests (COMI) of the debtor for a continuous period of at least six months.

According to the Opinion, the Hong Kong provisional liquidator or liquidator should submit the following materials when applying for recognition of and assistance to the Hong Kong insolvency proceedings:

- 1. An application;
- A letter of request for recognition and assistance issued by the Hong Kong High Court;
- The relevant documents on the commencement of the Hong Kong insolvency proceedings and in relation to the appointment of the Hong Kong provisional liquidator or liquidator;
- Materials showing that the debtor's centre of main interests is in Hong Kong. Any materials issued outside Mainland China needs to be certified in accordance with the law of Mainland China;
- A copy of the judgment in respect of which the application for recognition and assistance is made;
- 6. A copy of the identity document of the Hong Kong provisional liquidator or liquidator. If such identity document was issued outside Mainland China, it needs to be certified in accordance with the laws of Mainland China:
- Evidence showing that the debtor's principal assets in Mainland China are in a pilot area, or that it has a place of business or a representative office in a pilot area.

Where a document to be submitted to a People's Court of Mainland China is not in the Chinese language, a Chinese translation shall be submitted.

Once the People's Court decides to recognise the Hong Kong insolvency proceedings, the Court shall also decide upon the application to recognise the status of the Hong Kong provisional liquidator or liquidator, and announce its decision within five days. The effect of the recognition will be that payment of debts made by the debtor to individual creditors will be invalid, any civil action or arbitration involving the debtor that has started but has not yet been concluded shall be suspended (save that such action or arbitration can resume after the Hong Kong provisional liquidator or liquidator has taken over the debtor's property and assets).

The Hong Kong provisional liquidator or liquidator may, upon application, exercise certain powers in Mainland China, including taking over property, corporate seals, accounting books, documents and other data of the debtor, investigating the financial position of the debtor, deciding on the matters of the debtor's internal management, deciding on day-to-day expenses and other necessary expenditure, managing and disposing of the debtor's property, etc, provided that such exercise of powers must not exceed the scope permitted under the PRC Enterprise Bankruptcy Law and under Hong Kong law.

The Hong Kong provisional liquidator or liquidator is also required to seek separate approval from the People's Court if certain acts of the Hong Kong provisional liquidator or liquidator involves the waiver of property rights, creation of security on property, loan, transfer of property out of Mainland China and other acts for the disposal of property which may have a major impact on the creditors' interest.

The streamlined procedures would provide better comfort and greater predictability to investors investing in securitisation products with onshore Mainland China assets, as there will be a means for the investors to pursue the onshore company and protect recovery in the event of bankruptcy through the Hong Kong courts.

Reciprocal Arrangement

The Mainland Judgments in Civil and Commercial Matters (Reciprocal Enforcement) Ordinance (Cap.645) came into force on January 29, 2024 (the "HK Ordinance"). The HK

Ordinance implements the Reciprocal Arrangement into Hong Kong law.

In Mainland China, the Reciprocal Arrangement is implemented into PRC law by judicial interpretation issued by the Supreme People's Court on January 29, 2024《法释(2024) 2 号最高人民法院关于内地与香港特别行政区法院相互认可和执行民商事案件判决的安排》("Supreme People's Court 2024 Judicial Interpretation"), which largely tracks the wording of the Reciprocal Arrangement.

Under the Reciprocal Arrangement and Supreme People's Court 2024 Judicial Interpretation, Hong Kong court judgments can be registered and enforced directly through the Mainland China courts if the following criteria are satisfied:

- The judgments are of "civil and commercial" nature under both Mainland China law and Hong Kong law. However, it is worth noting that certain matters are excluded from the scope of "civil and commercial" under the current Reciprocal Arrangement, such as:
 - a. Corporate insolvency, debt restructuring, personal bankruptcy;
 - b. Judgments on validity of an arbitration agreement and the setting aside of an arbitral award;
 - c. Judgments ruling on the recognition and enforcement of judgments and arbitral awards made by other countries or places.
- The Hong Kong judgment must be a legally effective judgment given by the following Hong Kong courts: Court of Final Appeal, Court of Appeal, Court of First Instance of the High Court, District Court, Labour Tribunal, or Lands Tribunal. A judgment includes any judgment, order, decree and allocatur, but does not include any anti-suit injunction or an order for interim relief.

Prior to making any application for recognition and enforcement of Hong Kong court judgments in Mainland China with an Intermediate People's Court of the place of residence of the applicant or respondent or where the property is located, a certified copy of the Hong Kong court judgment and the certificate certifying the Hong Kong judgment for use in Mainland China is required. This

procedure for obtaining these documents are now encoded under sections 33 and 34 of the HK Ordinance.

Conclusion

As China's economy continues to grow and develop, Hong Kong's common law system provides an amazing unique platform for China to expand its largely domestic securitisation market into a credible international offering.

In addition to Hong Kong's common law system, recent legal enhancements have significantly improved legal certainty for international securitisation investors using Hong Kong law and Hong Kong courts/arbitration as tools to invest in Mainland China.

Looking ahead, Hong Kong's unique position as the gateway to Mainland China is expected to continue to be further entrenched. Hong Kong's legal system provides greater efficiency, transparency and legal predictability, all of which will play a significant role to provide the perfect platform for China to expand and launch its international securitisation market when it is ready to do so.

Notes

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 - "Southbound Bond Connect", Jan 22, 2024. Available at: https://www.cmu.org.hk/en/bond-connect-southbound
- ³ China's strict foreign exchange controls still restrict cross-border securitisations from China. For example, there is an annual aggregate investment quota (currently set at RMB500bn) and daily investment quota set (currently set at RMB20bn) for the Southbound Bond Connect scheme.
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- Weixia Gu, "15 Years of the Handover: The Rise, Discontent, and Positive Interaction of Cross-border Arbitration in Hong Kong with Mainland China" (2013), U. Of Pennsylvania East Asia Law Review, Vol. 9, 42-98
- William Lu, "Arbitration and Insolvency Proceedings: Chinese Law Perspective", March 17, 2021. Available at https://www.jingtian. com/Content/2021/03-18/1303144238.html#:~:text=Overall%20 the%20Chinese%20insolvency%20law,impact%20upon%20the%20 arbitration%20proceedings
- Interim measures may also be sought in Hong Kong under Article 6 of the Interim Arrangements, which provides for a party to the arbitral proceedings administered by a Mainland arbitral institution to apply for interim measures in the High Court of Hong Kong.
- See: https://www.doj.gov.hk/en/community_engagement/ announcements/pdf/Interim_Measures_Arrangement_Contact_ Details_of_Arbitral_Institutions_en.pdf

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