



Integrity

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E X P E C T E X C E L L E N C E

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Arthur Cox Briefing

# The National Asset Management Agency

## Function of NAMA

The National Asset Management Agency Act 2009 (the “Act”) was signed by the President on 22 November 2009 and the Minister for Finance (the “Minister”) signed a commencement order bringing the Act into force with effect from 21 December 2009 (the “Establishment Date”).

The central objective of the National Asset Management Agency (“NAMA”) is to stabilise Irish credit institutions by strengthening their balance sheets and reducing uncertainty in relation to their distressed loans, so as to facilitate lending to individuals and businesses. Whilst several governments (including the US and the UK) have announced plans to mitigate the impact of distressed assets on the balance sheets of credit institutions in their countries, NAMA is unique in terms of its mechanics.

The Government has indicated that approximately €77 billion of assets will be transferred from credit institutions and their subsidiaries participating in the NAMA scheme (the “Participating Institutions”) to NAMA.

## Participating Institutions

A credit institution can apply to the Minister to be designated as a Participating Institution within 60 days (or such longer period that the Minister prescribes by order under the Act) after the Establishment Date. A credit institution must include all of its subsidiaries in its application, although they may apply as part of the application process to become a participating institution to have particular subsidiaries excluded. The Minister has, however, complete discretion in the decision as to include or exclude subsidiaries.

The Minister will designate applicant credit institutions as Participating Institutions where he believes:

- (a) the credit institution is systemically important to the financial system; or
- (b) the acquisition of that credit institution's assets is necessary to achieve the purpose of the legislation.

*This document contains a general summary of developments and is not a complete or definitive statement of the law. Specific legal advice should be obtained where appropriate.*

It is open to the Minister to take into account:

- (a) where subsidiaries of overseas credit institutions have access to other support schemes;
- (b) the financial situation of the applicant credit institution; and
- (c) other resources available to the Minister.

### Eligible Bank Assets

Only assets that have been designated by the Minister as being eligible bank assets can be acquired by NAMA. Following the Minister's designation order, the assets that will be acquired by NAMA will include:

- (a) credit facilities to debtors made in whole or in part to purchase, exploit or develop development land;
- (b) credit facilities to debtors, the security for which is or includes development land; and
- (c) credit facilities to persons who are associated debtors of the debtors referred to above.

The foregoing are just examples of the classes of assets which have been designated and the enabling regulations are very broad. It remains open to the Minister to designate further classes should he think fit. 'Development land' is also very widely defined by the Act and means any land wherever situate in, on, over or under which works or structures were or are to be constructed or where it was intended to make a material change in the use of land where that land was intended to be sold or otherwise exploited.

### Transfer of Assets

The transfer of the largest borrowers' exposures across all Participating Institutions to NAMA is targeted to take place in the first quarter of 2010. Transfer of the remaining borrower exposures is targeted for completion by the end of July 2010<sup>1</sup>.

Participating Institutions must reply in utmost good faith to extensive questionnaires from NAMA about the assets they hold. NAMA will use the replies to these questionnaires to value the assets and prepare detailed acquisition schedules which will set out the precise assets to be acquired, the acquisition value, the date of transfer and the terms and conditions of the transfer. Once the transfer of an asset is complete, NAMA will acquire all of the Participating Institution's interests and all obligations relating to that asset specified in the acquisition schedule.

It is a matter for NAMA to decide on and identify which assets it will acquire. In the event of a dispute between NAMA and a Participating Institution in relation to eligibility of assets, the Minister can appoint an expert reviewer.

Participating Institutions are likely to be required to continue to perform "relevant services" in respect of loans transferred to NAMA unless otherwise directed. The term "relevant services" includes management, administration, restructuring and enforcement services. NAMA will reimburse Participating Institutions for the agreed cost of carrying out these "relevant services". Key credit decisions and relationship management in relation to the 100 largest borrowers (constituting 50% of the total portfolio of loans to be acquired) will be intensively managed directly by NAMA.

On acquisition, NAMA steps into the shoes of the Participating Institutions. The original borrower will continue to make payments and be liable for failure to make payments as previously agreed with the Participating Institutions and the terms and conditions of the loan remain the same. However, the end destination of these payments will now be NAMA.

### Foreign Assets

A considerable amount of the assets likely to be transferred to NAMA are situated outside of Ireland, including in the UK and the US, and are therefore governed by laws other than those of Ireland. Under the Act, if the proposed transfer of an asset to NAMA is governed by the law of a foreign country, and the law of that Jurisdiction allows the transfer to take place, the Participating Institution can be directed by NAMA to do everything necessary to effect the transfer.

If the law of a foreign jurisdiction does not permit the transfer of the asset, the Participating Institution can be directed by NAMA to do all that is permitted under such foreign law to assign to NAMA the greatest interest possible in the foreign asset. The Participating Institution will then effectively hold the asset on trust for the benefit of NAMA.

### Valuations

The expectation is that where appropriate the acquisition value of a bank asset will be its long-term economic value ("LEV"). The LEV will be determined by NAMA having regard to, *inter alia*:

- (a) the market value of the property that is the subject of security for a credit facility that is being acquired as a bank asset;
- (b) the market value of the bank asset (e.g. credit facility);
- (c) the long-term economic value of the property that is the subject of security for a credit facility; and
- (d) the LEV already determined by NAMA in respect of similar property.

<sup>1</sup> Presentation by the Managing Director of NAMA to a UCD Law Conference - 26 November 2009, available at [www.nama.ie](http://www.nama.ie).

Assets purchased by NAMA will be paid for at prices that reflect any appropriate adjustment for their LEV. This practice is in accordance with EU State Aid rules. It has been estimated that this will result in NAMA paying a €7 billion (15%) premium over the estimated current market value (“CMV”). However, this represents a 30% “haircut” or discount on the book value (“BV”) of the assets.

The NAMA (Determination of Long-Term Economic Value of Property and Bank Assets) Regulations 2009 (SI/546/2009) (the “Valuation Regulations”) signed into law by the Minister 21 December 2009 outline the various adjustments over CMV to be applied in each case to determine the LEV of land in or outside the State. These adjustment factors include the:

- (a) difference between current property yields and yields over various relevant periods; and
- (b) correlation between:
  - (i) land prices and demographic variables;
  - (ii) land prices and interest rates; and
  - (iii) land prices and GDP.

For example, NAMA may determine in respect of a particular parcel of land that a 0% adjustment factor is appropriate, for land which, in NAMA’s view, has no prospect of development and for incomplete developments which have limited sale prospects. NAMA may refuse to acquire certain assets.

Valuation is subject to certain overall limitations. For example the Valuation Regulations provide that the LEV of a particular parcel of land will not exceed its CMV by more than 25% and the maximum aggregate adjustment upwards per Participating Institution on total property collateral acquired will be 20%.

NAMA will value each loan separately and the actual amount of the discount applied will depend on the quality of the underlying property and other collateral. This means there will not be a uniform discount across all the loans of the Participating Institutions. For example, a loan valued for transfer with a BV of €10 million which is secured on two acres of rural greenfield is likely to be acquired by NAMA at a far greater discount than a BV loan of €10 million secured on a fully built but tenantless city centre office block.

Valuation appeals from Participating Institutions are restricted under the Act.

## Financing

NAMA will purchase eligible assets from the Participating Institutions by issuing Government backed bonds as consideration, with a floating rate of interest payable to the Participating Institutions.

These bonds can be used by Participating Institutions as collateral to raise cash, in the form of loans, from the ECB or from inter-bank repo markets.

The consideration for eligible bank assets can also be comprised in part (up to 5% of the aggregate total portfolio acquisition value) of subordinated debt securities issued by NAMA or a NAMA group entity. In this way Participating Institutions will share some risk based on the future financial performance of the assets acquired by NAMA. This is considered further in section “*Risk Sharing*” below.

## Establishment of Special Purpose Vehicles

The Act allows NAMA to establish Special Purpose Vehicles (“SPVs”) (referred to in the Act as NAMA group entities) for the purpose of acquiring, managing and disposing of bank assets as well as the issuing of bonds as consideration to Participating Institutions. NAMA has indicated that it will delegate the purchase and management of the loans to be acquired to a master SPV with a subscribed share capital of €100 million. This master SPV will be 51% owned by private investors on an investment of €51 million, with NAMA owning the remaining 49% equity.<sup>2</sup> This master SPV may in turn own other SPVs established to deal with each Participating Institution. While the master SPV will be a separate entity to NAMA and will have its own board, its board will include representatives of NAMA and NAMA will have a veto over all of the decisions of the board of the master SPV.

Establishing a master SPV will mean the Government can exclude NAMA’s estimated €50 billion-plus liability from the national debt. This will avoid a serious breach of the EU’s stability and growth pact, which limits the amount that euro-zone states can borrow relative to the size of their economies. The EU Commission and its statistics agency, Eurostat, have issued guidelines that allow member states take liabilities related to schemes to rescue their banks off their balance sheets. Eurostat have provisionally confirmed that the mechanism proposed by the Government complies with the EU guidelines.

The Minister has indicated that if the master SPV is ultimately profitable, the private investors will be repaid their capital plus 10% (if available) on the winding up of the master SPV. This means that the private backers will be repaid their €51 million, plus €5.1 million, plus any annual performance linked dividends received during the lifetime of the master SPV. Any further profits over and above these amounts will be returned to the exchequer. However, the master SPV is not ultimately profitable, the private investors will lose their €51 million. Further details on the operation of the master SPV and the role of private investors will be set out in regulations issued by the Minister in due course.

<sup>2</sup> Central Statistics Office “ESA95 accounting treatment of the National Asset Management Agency (NAMA) and related majority privately owned SPVs”, September 2009.

## Risk Sharing

Provisions providing for risk-sharing by Participating Institutions are built into the Act.

### Subordinated Debt

NAMA will use subordinated debt to pay for part of the assets to be acquired, up to a maximum of 5% of the value of each asset. NAMA can withhold payments to the Participating Institutions if it cannot realise the full value of properties underlying the loans because this is a lower class of debt. By partly paying the Participating Institutions in subordinated debt and withholding payments due on that debt in the event NAMA makes a loss, the Participating Institutions are still partly bearing the risk of any loss. This provision has the aim of reducing risk to the taxpayer.

### Tax Surcharge

The Act provides for the imposition of a surcharge on the profits of Participating Institutions if NAMA ultimately incurs a loss. Where the Minister is of the opinion that such underlying loss is unlikely to be otherwise made good, then legislation may be enacted providing for the imposition of a special tax by way of surcharge on the profits (if any) of the Participating Institutions. Such surcharge will not become payable until:

- (a) 10 years after the passing of the Act;
- (b) NAMA is dissolved or restructured; or
- (c) there is a material alteration of NAMA's functions, whichever last occurs.

## Powers

NAMA will have all the necessary commercial powers of a financial asset management company to establish subsidiaries, to operate through agents, to buy and sell assets, to manage loans and work with borrowers, and to take full and determined action in relation to debts owed. NAMA will have wide-ranging and unique powers to allow it to fulfil its functions. These powers include:

- » Appointment of a Statutory Receiver - where the conditions of a loan enabling appointment of a receiver or the sale of the security are triggered by an appropriate default, NAMA will be able to appoint a receiver by operation of statute in order to realise the security on the loan. The appointment of a statutory receiver cannot be displaced by the appointment of an examiner or liquidator. This is a significant departure from the current situation under the Companies Acts.
- » Dealings with Liquidators - where the borrower is a company there is no absolute prohibition on the appointment of a liquidator. Creditors remain entitled to petition a court to have the company wound up. However, the Act amends the Companies Acts so that a court will be prevented from appointing a liquidator to a company whose loans are acquired by NAMA, unless the winding-up petition has been served on NAMA and the court has heard the views of NAMA on the petition.
- » Work Outs - a statutory receiver has the same obligation to exercise all reasonable care to obtain the best price reasonably obtainable at the time of sale as an ordinary receiver. However, a statutory receiver is not obliged to sell a property asset. This will enable NAMA to work-out/develop the property over the medium term to enhance the return to the taxpayer, rather than requiring the sale of such assets in the short term. The Minister has indicated he intends to issue guidelines governing NAMA's interaction with borrowers in the completion of properties acquired by NAMA.
- » Foreclosure and Vesting Orders - NAMA will have the power to obtain a vesting order from the High Court in respect of land charged in its favour. NAMA will be able to apply to the High Court for such a vesting order if it has acquired a credit facility that is secured by a charge over land, once its power of sale has become exercisable and once NAMA forms the view that it is unlikely that the sum secured by the charge can be recovered by a sale within a reasonable period.
- » Equitable Interests in Subsequent Mortgages Extinguished - NAMA will have the ability to convey land that has been mortgaged in its favour so as to extinguish any equitable interest or the interest that any other person holding a mortgage or charge on the land has/may have - other than a charge which has priority or ranks *pari passu* to the interest of NAMA. Where the interest of a chargee or mortgagee or the holder of a beneficial interest is extinguished, their interest attaches in the same order of priority to the proceeds of sale received by NAMA. The Act explicitly states that such provision applies to land that is or includes a person's principal private residence.
- » Compulsory Acquisition - Subject to complying with certain prescribed preconditions, compulsory acquisition powers are exercisable by NAMA on application to the High Court in respect of any land or easement which in NAMA's opinion is necessary to facilitate the sale or development of land charged to NAMA.
- » Power to Avoid/Set Aside Transactions - NAMA will have the ability to apply to the High Court to seek a declaration that a disposition of any asset of a borrower, associated borrower or guarantor is void if it can show that the effect of the disposition was to defeat, delay or hinder the acquisition by NAMA of an "eligible bank asset" or any associated rights.
- » NAMA Defaulters Cannot Acquire NAMA Assets - the Act provides that a person who is the debtor, an associated debtor or a person for whom a debtor or associated debtor act as nominee, in relation to an acquired bank asset, cannot if any of them is in default in relation to any acquired bank asset, acquire from NAMA or a NAMA group entity, any interest in property comprised in the security forming part of any acquired bank asset in relation to which the default has occurred.

- » Statutory Exemptions - asset transfers to NAMA will benefit from a range of statutory exemptions from certain rules of law which might otherwise invalidate or delay such transfers of the eligible bank assets.
- » Tax Exemptions - certain tax liabilities that would normally accrue when NAMA acquired a loan and related assets from one of the Participating Institutions are set aside by the bill.
- » Litigation - the Act provides for limits on the power of the courts to grant injunctive relief, limits on applications for judicial review and limits on certain rights of appeal to the Supreme Court.

### Guidelines Regarding Lending Practices

The Act allows the Minister to issue guidelines setting out lending practices and procedures to facilitate the availability of credit to classes of borrowers or potential borrowers, including small and medium sized enterprises, which Participating Institutions will be required to comply with. Guidelines may also be issued allowing for the review of decisions of Participating Institutions to refuse credit facilities.

### Accountability

Every three months NAMA will be required to provide the Minister with a report on the activities of NAMA and each NAMA group entity. These quarterly reports will be laid before each house of the Oireachtas (the Irish Parliament) and an Oireachtas committee which will be established to examine matters relating to NAMA. In these quarterly reports, NAMA will be required to report on its compliance with any guidelines or directions issued by the Minister. Quarterly reports will also include, *inter alia*, the following information for the relevant quarter:

- (a) the number of all loans outstanding and the condition of those loans, categorised as between performing and non-performing loans;
- (b) non-performing loans categorised as to the degree of default, distinguishing where default has occurred on capital payment as well as interest payments;
- (c) the number of loans being foreclosed or otherwise enforced during the relevant quarter;
- (d) the number of cases where liquidators and receivers have been appointed in the relevant quarter;
- (e) a schedule of any finance raised by NAMA and each NAMA group entity in the relevant quarter;
- (f) sums recovered from property sales in the relevant quarter; and
- (g) an abridged balance sheet of the assets and liabilities of NAMA and each NAMA group entity.

The CEO of NAMA will be accountable to the Public Accounts Committee ("PAC") and will be required to give evidence to the PAC whenever required to do so by the Oireachtas committee set up to examine matters relating to NAMA.

### Tax on Windfalls from Rezoning

The Act amends the Taxes Consolidation Act 1997 to provide for the imposition of a capital gains tax at a rate of 80% on gains arising from the disposal of land relating to an increase in the market value which is attributable to rezoning.

The Act also introduces an 80% rate of income tax on profits of taxpayers who deal in or develop land in the course of their business, where such profits are derived from rezoning.

### Codes of Practice

The Act requires that, within three months after the establishment of NAMA, codes of practice will be prepared in relation to the following matters:

- (a) the conduct of officers of NAMA;
- (b) servicing standards for acquired bank assets;
- (c) risk management, including with regard to debtors;
- (d) disposals of bank assets; and
- (e) the manner in which NAMA is to take account of the commercial interests of credit institutions that are not Participating Institutions.

These codes of practice will set out, *inter alia*, what constitutes misconduct in office, the procedures for the investigation of an officer of NAMA suspected of misconduct, and the procedures for the suspension of such an officer from his or her duties for misconduct in office. These codes of practice are required to be published on NAMA's website.

### Role of the Financial Regulator

The Financial Regulator, may, with the approval of the Minister, give directions to Participating Institutions in order to achieve the purposes of the Act, including directions to:

- (a) restrict balance sheet growth;
- (b) restrict the Participating Institutions' ability to take over other credit institutions;
- (c) reduce balance sheets; or
- (d) restrict or require consolidation and merger of Participating Institutions.

### Secondary Legislation

The Act provides that a range of matters relating to the operation of NAMA are to be implemented by way of secondary legislation. In this regard the following statutory instruments have been signed into law by the Minister:

- » National Asset Management Agency Act 2009 (Commencement) Order 2009 (SI/2009/545) which commenced the Act with effect from 21 December 2009.

- » National Asset Management Agency (Determination of Long-Term Economic Value of Property and Bank Assets) Regulations 2009 (SI/2009/546) which outline the various adjustments to be applied in each case to determine the long term economic value of land in or out of the State.
- » National Asset Management Agency Act 2009 (Establishment Day) Order 2009 (SI/2009/547) which designated 21 December 2009 as the establishment day for the purposes of the Act.
- » National Asset Management Agency (Designation of Eligible Bank Assets) Regulations 2009 (SI/2009/568) which outlines the classes of bank assets which are to be prescribed as classes of eligible bank assets for the purposes of the Act.

### Links

<http://www.nama.ie>

<http://www.oireachtas.ie>

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