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# SECURITIZATION IN POLAND AS AN INNOVATIVE SOLUTION IN THE CAPITAL MARKETS

**Summary:** The development of international financial markets depends on financial innovations. For those markets the securitization of assets may be regarded as one of such innovations. Since 1997 some securitization programmes have been executed in Poland too. This study is an attempt to answer, in the light of theories on financial innovation, whether domestic securitization is a new financial instrument. A positive answer to this question may also point to a general trend of the securitization market in Poland.

**Keywords:** securitization, capital markets, innovation.

## 1. Introduction

The dynamic growth of the global capital markets was based on development of new financial instruments. Some of them called "financial innovations" affected further evolution of that branch of the economy in a remarkable way. The issue of innovation in the capital markets has been finally encapsulated in a number of scientific theories that seek to elucidate the circumstances of its origination. Since the beginning of the nineties of the last century, the Polish market has been also encompassed by that general trend, which in our country translates mainly into the implementation of the already developed solutions and, if needed, their adjustment to domestic institutions. An example of such operations may comprise securitization issues that have taken place in Poland since 1997. The recent twenty years of development of securitization services in Poland make it legitimate to advance a hypothesis that off-balance sheet securitization of assets may be regarded as a financial innovation in the domestic capital market.

In order to provide for the falsification of this thesis, this study presents the actual theories on innovation in the financial sector and within such an established frame it reviews the securitization issues in Poland.

## 2. Theories on financial innovation – outline

The lack of single theory implies that the issue of financial innovations is complex. The difficulties to determine that concept in a clear-cut way result also from the varied development of areas of the international capital market (e.g. the United States and Western Europe)[1]. The so-far arisen notions may be grouped as follows: demand-oriented group, supply-oriented group, mixed (demand and supply-oriented) group, a group based on the capital market theory as well as institutional economy theory[2]. The grouping criterion is hinged on the structure of elements that impact the development of an innovation. Each of those theories attempts to find a specific condition that directly affects the development of a new financial instrument. Individual theories, along with their authors and recognition clues, are presented in Table 1.

**Table 1.** Theories on financial innovation

| Theory type | Representative | Conditions substantiating development of innovation |
|---|---|---|
| 1. Demand-oriented | S.I. Greenbaum, C.F. Haywood | Income and substitution effects in capital market |
| 2. Supply-oriented | W.L. Silber | Competitiveness |
| | E.J. Kane, W.L. Silber and M. Ben-Horim | Legal restrictions |
| | C.R. Dunham, | Interest rates and risk |
| 3. Based on capital market theory | J.C. Van Horne | Increase in effectiveness and aiming at market completeness / cohesion |
| 4. Based on institutional economy | G.Dufey, I.H. Giddy | Institution malfunctioning |

Source: own study based on H. Hastenpflug, *Das Securitizationsphänomen*, Wiesbaden 1991, p. 45.

In the supply-oriented theory, the income and substitution effects in the capital market are construed as a function that interconnects the demand for financial instruments with the growing income or movements in interest rates, taking account of the available (alternative) products[3]. Advancing those hypotheses, S.I. Greenbaum and C.F. Haywood pointed to a significant correlation between an increasing value of assets subject to investment in the capital markets and the costs of their diversification[4]. In relation with the theory by H.M. Markowitz, in which a greater portfolio diversification results in risk diminishing, the investors

[1] Ch. Franzen, *Finanzinnovation – was ist das ?*, „Die Bank" 1988, No. 1, p. 18-20.

[2] H. Hastenpflug, *Das Securitizationsphänomen*, Wiesbaden 1991, p. 43-44.

[3] J.G. Gurley, E.S. Shaw, *Financial Intermediaries and the Saving-Investment Process*, „Journal of Finance" 1956, Vol. 11, p. 532.

[4] S.I. Greenbaum, C.F. Haywood, *Secular Change in the Financial Services Industry*, „Journal of Money, Credit, and Banking" 1971, Vol. 3, No. 2, p. 573.

endeavour to generate the highest possible rate of return at the given risk level. At the same time, the costs related to the portfolio management, including portfolio diversification costs, originate. Those costs are on increase if the value of the portfolio is growing. According to the theory, the demand for a financial innovation arises when the costs of the portfolio management begin to exceed the gains on those assets. The disappearing benefits trigger a search for alternative solutions in the capital market in order to downsize those costs or increase the income. The latter element is manifested in the substitution effect that regards interest as remuneration for the use of the capital.

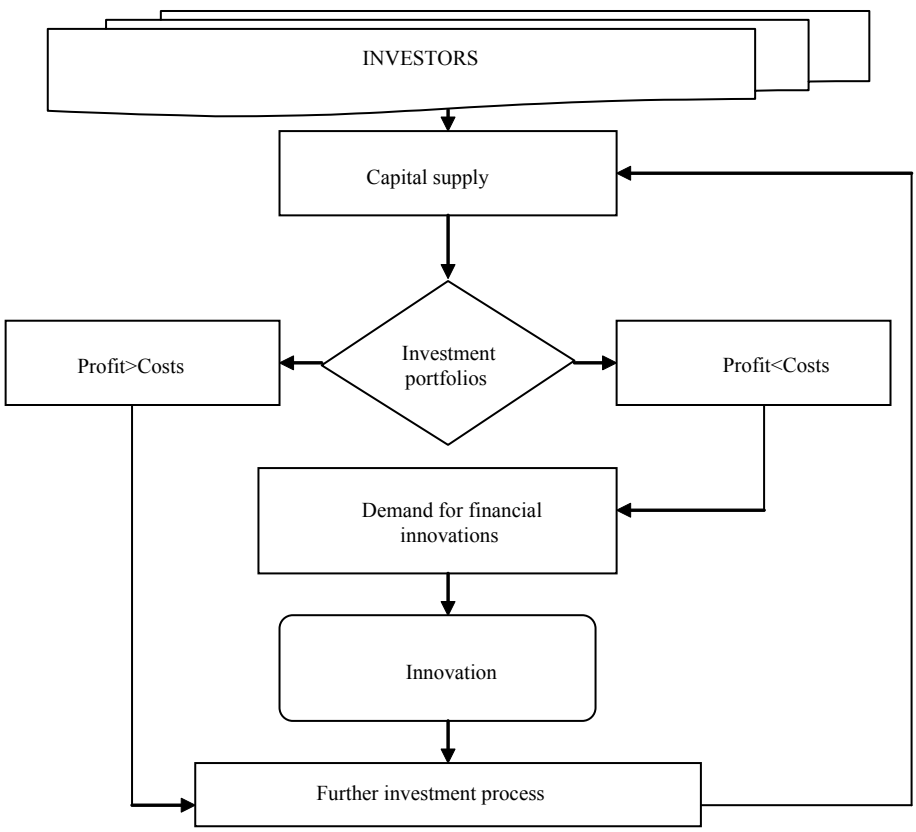


**Figure 1.** Conditions of innovation development according to the demand-oriented theory

Source: own study based on S.I. Greenbaum, C.F. Haywood, *Secular Change in the Financial Services Industry*, „Journal of Money, Credit, and Banking" 1971, Vol. 3, No. 2.

Every financial service may be perceived as an n-element vector, which may be described with the use of specified attributes such as time, risk, liquidity etc. Potentially, there exists an unlimited number of different combinations of those

attributes, which translate into an unlimited number of financial services. Under this theory, an innovation shall be a product that combines those elements in an innovative way and develops an instrument unknown before. At the same time, it provides for a response to demand occurring on the part of the capital market participants.

The development of an innovation may be schematised in the following way (Fig. 1).

As opposed to the demand-oriented theory, supply-oriented concepts may be split into a few trends, each of which highlights a different aspect of an innovation development. A model by E.J. Kane, named also as *regulatory dialectic*, recognizes innovations as a reply to a legal regulation that limits the freedom of action. The theory is based on an assumption of cyclical changes and adjustment of two opposing trends: political interventionism in the economy, which is manifested in establishing legal regulations, and pursuance of business processes to evade those regulations. The struggle between those drives may be compared with an interaction of visible and invisible forces, in which the first one is represented by the actual transactions in the market, and the second mirrors the introduced regulations[5]. The temporarily reached equilibrium is thrown off balance due to an action of one of the parties and the whole process starts anew. Such a speculative presentation of the entire change process, to which the theory owes the name "dialectic", has been confirmed in the course of actual financial market operation. An example may include statutory restrictions, introduced as early as in the 30s of the last century in the United States, with respect to determination of the maximum interest rates for deposits. The growing inflation in the 60s resulted in opening new possibilities of depositing, which enabled the evasion of the then existing regulations[6].

The sequential approach to the innovation process by E.J. Kane is based on a premise of *innovation and regulatory lags* that arise from the calculation of the costs of innovation. An introduction of a given regulation makes an innovation arise only if the probable profit from the innovation is greater than the cost of such an introduction. The lag may be a consequence of "accumulation" of factors, which will determine profitability of its introduction. If the influence of the regulation is immaterial for the increase in the costs of the market operation, then an innovation does not arise immediately. It may originate in the future if the costs of its introduction become reduced. This may be affected with external changes such as the higher inflation rate in the already presented example of deposits, or technological changes. Then, while the profit remains constant, the costs of implementation may be downsized to such an extent that the development of an innovation will turn profitable. If, however, a regulation impacts profitability of the market transaction in a vital way, it may encounter a relatively prompt response in the form of a new financial service aimed at evasion of those unfavourable regulations. The same may be applied in the other

[5] E.J. Kane, *Impact of Regulation on Economic Behaviour. Accelerating Inflation, Technological Innovation, and the Decreasing Effectiveness of Banking Regulation*, "Journal of Finance" 1981, Vol. 36, No. 2, p. 358.

[6] E. Głogowski, M. Münch, *Nowe usługi finansowe*, PWN, Warszawa 1996, p. 253-254.

way round, where the significance of the innovation is reviewed from the legislator's perspective.

Figure 2 presents the innovation process described above.

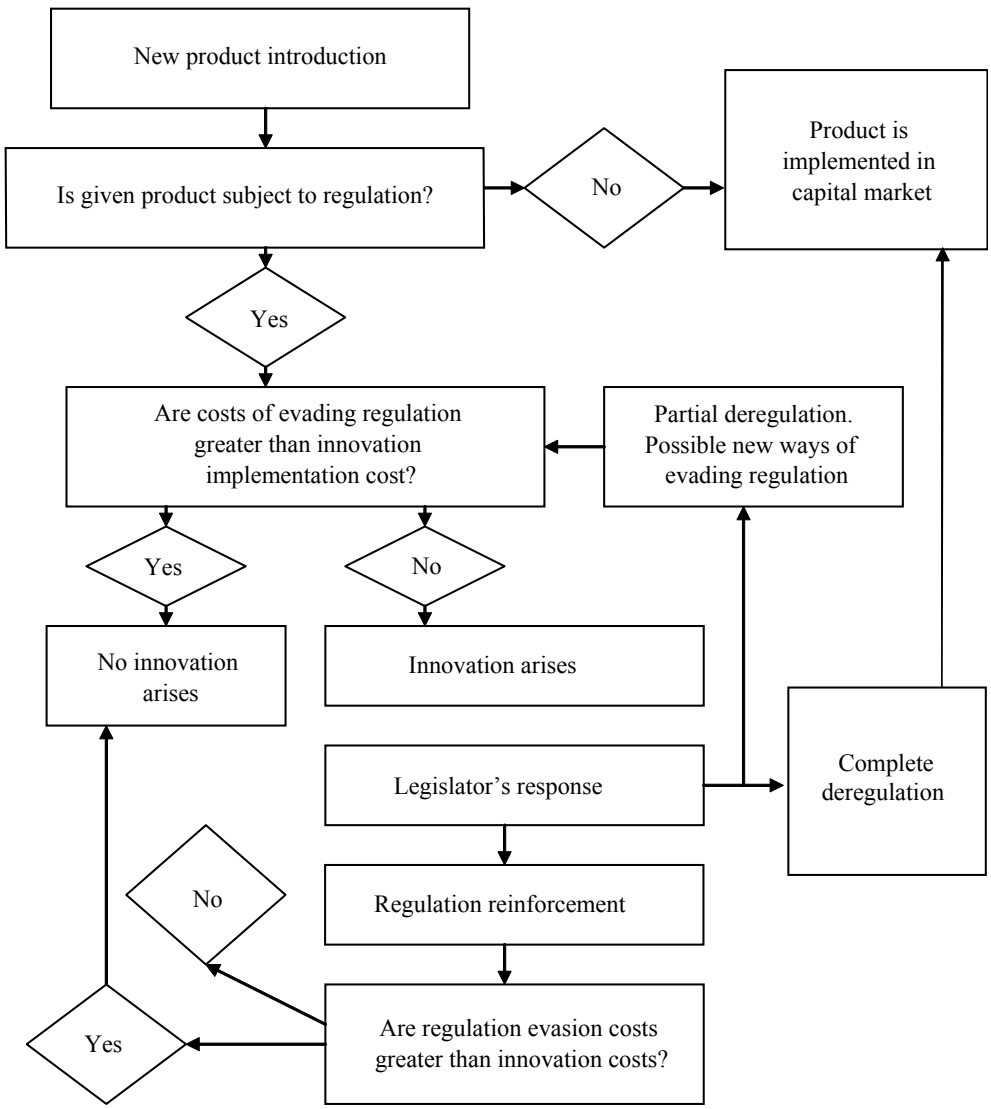


**Figure 2.** Development of innovation according to the regulatory dialectic theory by E.J. Kane

Source: study based on P Bofinger P., *Geldpolitische Regulierungen und Finanzinnovationen*, Aussenwirtschaft, Vol. 2/3, 1987.

In his theory, W.L. Silber deepens the understanding of the restrictions that trigger innovations. In addition to the legal regulations as external factors, he also takes into account internal restrictions occurring in a given market (e.g. demand for given products), or the ones imposed by the entities themselves (e.g. mutual deposit securities). The source of innovation development is sought in two aspects[7]. The first one involves dropping profits from operations of financial institutions in given markets. As a consequence of external changes, such as decreasing demand for credit, banks are forced to introduce new products or search for new market segments at the expense of the developing security market that provides for immediate financing. The second one involves the costs related to the existing and implemented regulations. Those alterative costs derive from the fulfilment of certain conditions, both external (legal regulations), and internal, which require additional expenditures to be incurred in order to track the changes, modifications and adjustments accordingly. An innovation arises when the profit from given services is on decrease or the costs of operation under certain regulations are too extensive. The chart below schematises the development of an innovation.

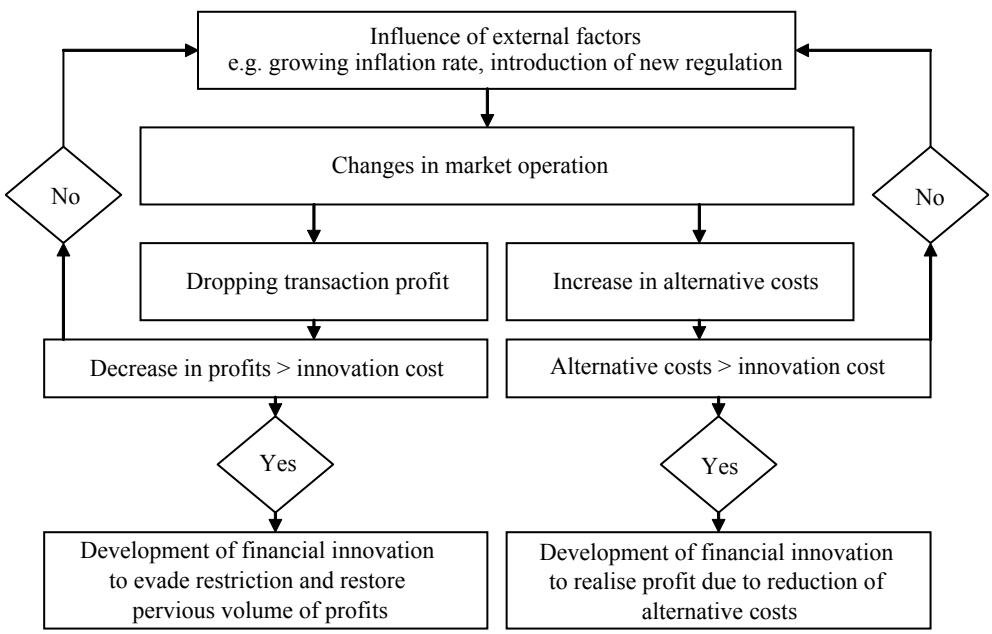


**Figure 3.** Development of innovation according to the theory by W.L. Silber

Source: study based on H. Hastenpflug, op. cit. p. 63.

The last theory in the supply-based group belongs to C.R. Dunham, who assumes that every financial intermediary operates within the frame determined by

[7] W.L. Silber, *Towards a Theory of Financial Innovation*, Lexington 1975, p. 65-66.

the correlation of risk and interest rates, in which they are compelled to offer their services all the time. This means the assumption of both active as well as passive role towards the market in such a way so as to enable demand to balance in those areas. An innovation arises in a situation when the existing demand and supply structure is subject to transformation in the financial service market as a result of changes in the structure of risk and interest rates[8]. The factors of two kinds may trigger the development of those changes. The first group involves transformations of the very structure of risk and interest rates. The co-existence of the capital markets and the commodity and service markets leads to establishing certain equilibrium in which demand for tangible investment financing equals the financial service supply. Changes on either part (e.g. increase in investment expenditures) strike the whole system off balance and a process of adjustment is set off. During such a period, financial entities strive to re-adjust to new market conditions, which may bring about the development of an innovation. The second group of conditions involves diversity in risk approaching assumed by the participants in the transaction. Similarly to the previous case, the changes result in a need to adjust to new conditions and, therefore, bring about the development of an innovation.

The theory may find it difficult to determine the factors that substantiate the changes within the operating structure of the market. It is hard to define them, and in particular the weight of their influence, in a clear-cut way.

The theory by J.C. Van Horne is founded on two bases: reaching for operating effectiveness of capital markets and making them total, more complete[9]. The notion of operating effectiveness assumes that the costs of capital flow between the entities should be as low as possible. An innovation provides, therefore, for reduction in paid commissions, interest etc., and enables more efficient and immediate allocation of the existing funds. Totality does not imply here any struggle for total (weighty) market effectiveness in the meaning of asset valuation models[10], but it rather involves the occurrence of such financial instruments as there are in correspondence with that given point in time and that specific economic situation. It is, hence, possible to conclude a transaction with the use of securities or their combination, to provide for inclusion of any future event. An innovation is an instrument that is introduced to cover the existing gap, as there has been no possibility so far to conclude a transaction in view of a given period or with respect to a given event. An example of such an innovation may be creation of a product that will secure the transaction in the forex market for a period longer than it is possible with the existing instruments.

According to that theory, a financial innovation would not occur in a market of complete effectiveness, where all information was reflected in the price of the assets. As markets are not effective in the above sense, there are incentives that may trigger

[8] C.R. Dunham, *Financial Innovations*, Stanford University, Palo Alto 1980, p. 56.

[9] J.C. Van Horne, *Financial Innovations and Excess*, "Journal of Finance" 1985, Vol. 41, p. 621.

[10] J. Czekaj, M. Woś, J. Żarnowski, *Efektywność giełdowego rynku akcji w Polsce*, PWN, Warszawa 2001, p. 32.

the development of innovations. C. Van Horne listed variability of economic ratios (inflation, interest rate), impact of legal regulations as well as technical and social progress among such incentives.

According to the theory by G. Dufey and I.H. Giddy functioning of social structures is defined as institutions substantiates development of an innovation. Within the frame of the institutional economy, in order to function properly the society requires to minimize the so-called transaction costs that constitute a material aspect of made agreements[11]. If no relevant protection of competition and property rights (including intellectual property rights) exists, the incentives to trigger an innovation are on decrease[12]. A paradox in this theory may be the fact that the actual capital market development since the 80s of the last century has denied the necessity to protect patents for the introduced innovations, and their imitations became the drivers of the global financial market development.

The authors of this theory split the financial innovations into two types. The first one is called *aggressive innovation*, which is a result of a search carried out by companies that specialise in the generation of products of this kind. Potential buyers will be more willing to acquire new instruments from known and reckoned companies, as that involves less risk. On the other hand, such solutions are more expensive than the future imitations, as the price of these solutions includes an additional cost related to both research of the innovation as well as a possible risk to fall in disrepute in case a faulty solution is introduced. We may even speak about a peculiar monopoly on introducing innovations, which is held by reckoned financial institutions. The second group comprises the so-called *defensive innovations* that address the changes in regulatory laws or asset interest rates and risk. The notion of this kind refers explicitly to earlier theories by E.J. Kane and W.L. Silber (legal regulations) as well as by C.R. Dunham (interest rates and risk).

## 3. Initial period of asset securitization in Poland

The first off-balance sheet issue of asset securitization was carried out in 1997 by Urtica S.A, a company located in Wrocław. Naturally, transactions secured against assets had been concluded from the beginning of the nineties[13]. However, they were exclusively syndicated credits and the assets were not formally excluded from the balance sheet.

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[11] O.E. Williamson, *Ekonomiczne instytucje kapitalizmu*, Warszawa 1998, p. 390.

[12] G. Dufey, I.H. Giddy, *The Evolution of Instruments and Techniques in International Financial Market*, Société Universitaire Européenne de Recherches Financières, 1981, p. 2.

[13] D. Strojewski, S*ekurytyzacja aktywów w Polsce*, [in:] *Sekurytyzacja aktywów ze szczególnym uwzględnieniem wierzytelności hipotecznych*, Fundacja na Rzecz Kredytu Hipotecznego, Vol. 16, Warszawa 2003, p. 20-21.

Till the beginning of 2003, securitization issues had been of relatively low value. In autumn 2003 a securitization which was initiated by DTC Real Estate S.A. for the amount of EUR 74 million, turned up a breakthrough. Paradoxically, the Polish capital market was not ready for such a voluminous issue and its significant portion came to the markets of Western Europe. Table 2 presents a list of the securitization issues carried out in Poland till that time.

**Table 2.** Securitization issues in Poland till 2003

| First issue date | Initiator | Issuer | Value of issue |
|---|---|---|---|
| 1997* | Urtica S.A. | Urtica Finanse S.A. | PLN 50m. |
| 2000 | PKO Leasing S.A. | PKO Leasing Sekurytyzacja Sp. z o.o. | PLN 4.3m.** |
| 2001 | Greenhouse Capital Management S.A. | Greenhouse Finance | PLN 12m. |
| 2001 | Pharmag S.A. | Pharmag-HM Sp. z o.o. | PLN 38m. |
| 2003 | DTC Real Estate S.A. | Polish Retail Properties Finance Plc | EUR 74m.*** |

*In 1997 it was the first 3-year issue, which was later on rolled over for the subsequent periods.
** The low value of issue is a consequence of the forerunning nature of the leasing assets under securitization.
*** At the average exchange rate published by the NBP, the issue value in autumn 2003 was ca. PLN 340m.
Source: own study based on J. Zombirt, I. Styn, *Transakcje sekurytyzacyjne na świecie i w Polsce*, Rynek Terminowy No. 14 (4) 2001, p. 19.

Both the issue of Urtica S.A., as well as all the issues in 2001, as presented in Table 2, were made based on receivable debts in the health care sector. If the immediate issues of bonds of hospitals[14], which transformed the outstanding debt into its securitised form, are added to the same, then we may generally state that the majority of issues in Poland involve receivable debts of the public health care institutions against suppliers.

When juxtaposing that branch of the economy with the presented theories on innovation, the following elements may be indicated to help to prove that securitization of those receivable debts was a financial innovation:
– transfer of liquidity-related risk by the suppliers to securing parties and purchasers of securities;
– reduction of debt-handling costs by the health care institutions;
– lack of efficiently operating institutions that make up the public health care system in Poland.

Both the risk transfer and the change in the capital acquisition cost refer to the theory by C.R. Dunham. The occurring indebtness of public health care institutions

[14] *Zamiast długów obligacje,* "Rzeczpospolita", 6 August 2003.

(hereinafter: the HCI), when their income is one-sidedly shaped by the National Health Fund (as from January 2004; hereinafter: the NHF) is often structural in nature. This is a consequence of maladjustment of the service supply financed by the NHF against the arising demand. The thus resultant shortages need to be made up for by way of incurring debts against e.g. suppliers. Inability to source additional funds from the NHF brings about an increase in debt-related costs that comprise first of all statutory interest on overdue payables. Moreover, if legal vindication of receivable debts from debtors is pursued, the public health care institutions are additionally charged with the costs of legal proceedings and collection. At present (legislation at force as in September 2009) those costs amount respectively to: 12.25 % - statutory interest, 8-5% (degressive scale) – legal costs, 18-3% (degressive scale) – costs of legal representation and 15% – debt enforcement costs.[15] Within the public health care system established under the administrative reform of 1999, the public HCIs depend on the units of territorial self-government (the UTSG), as their establishing bodies, which is evident in imposing accountability for the debts of the taken over entities on the UTSG. Bearing in mind the fact that it is impossible to declare bankruptcy with respect to the units of territorial self-government, there has arisen a peculiar structure of the public health care system, where one entity is the financing party (NHF), another is liable for the existing debts (UTSG), and the unit being the service provider is formally solvent, even if there is no cash. Furthermore, any cash supplies from the financing party are appropriated for handling the current indebtness, which means that the cost of such handling solely takes a relatively high per cent. Securitization enabled downsizing those values as additional expenditures related to the legal and collection proceedings were avoided and at the same time legal guarantees for creditors were introduced. Therefore, larger amounts may be used to immediately handle the incurred debts, which results in more flexible and swift repayment. This means an effective search for a relatively cheap source of financing even if the level of the already existing indebtness is high.

The risk of poor liquidity of suppliers arises out of irregular payments for the delivered goods and the so-called order of appropriating the cash funds received by the HCIs. If court enforcement proceedings are instituted, then, pursuant to Art. 1025 of the Code of Civil Proceedings[16], the court enforcement officer is obliged, in the first place, to cover the costs of legal and enforcement proceedings, subsequently public

[15] Those values result directly from: Ordinance of the Council of Ministers of 18 September 2003 on determining statutory interest rates ("Journal of Laws" No. 166, item 1613); Ordinance of the Minister of Justice of 17 December 1996 on determining court fees in civil cases ("Journal of Laws" No. 154 item 753, as amended), Ordinance of the Minister of Justice of 28 September 2002 concerning fees for attorneys' activities and incurring by the State Treasury the costs of unpaid ex officio legal aid ("Journal of Laws" No. 163 item 1349) and Act of 29 August 1997 on Court Enforcement Officers and Debt Enforcement Proceedings ("Journal of Laws" No. 133 item 882, as amended).

[16] Act on the Code of Civil Proceedings of 17 November 1964 ("Journal of Laws" No. 43 item 296, as amended).

law liabilities, and finally transfer the remaining financial funds to the creditor. Such a procedure, as combined with the *modus operandi* of the whole system of the public health care financing, may lead to insolvency, and, as a consequence, to bankruptcy of the supplier. Therefore, securitization provides for a source of cash in lieu of issued securities, which are secured against the receivable debts of the public HCIs. It may be appropriated for further operation of that entity, including repayment of the liabilities incurred against its contracting parties.

The last element to be considered with respect to medical service sector are the clear-cut, coherent and transparent rules of operation of the health care system, which are missing in Poland. The new shape of the system, which was introduced in spring 2003, established institutions, which have been unable to accomplish the assignments vested in them[17]. Securitization may be perceived in this case as an innovation, which due to the shortage of legible solutions in financial management, provides for the entity's further operation. This may be regarded as aggressive innovation in the light of the theory by G. Dufey and I.H. Giddy, which is based on institutional economy. At the same time, the lack of precisely determined property rights, which in this case implies vaguely defined rights and obligations of the premium payers and the NHF, triggers innovations. This is a confirmation of the already discussed paradox of this theory.

Securitization of receivable debts due to lease, as made in 2000, was a test-run issue of an entity belonging to the banking sector in its broad sense. The thus gained practical experience was to be employed in the future while issuing securities based also on other receivable debts. Nevertheless, securitization of debts against banks started to grow dynamically as late as on the moment of introduction of special legal regulations in the form of amendments to investment fund regulations.

## 4. Prescriptive regulation of securitization

The Investment Fund Act (the IFA)[18] has launched new solutions for asset securitization markets that were intended to increase the volume of transactions of this kind. First of all, a new kind of investment fund was introduced in order to issue certificates for the purpose of raising financial funds to acquire receivable debts (Art. 183 item 1 of the IFA). In this way, the fund will play the function of an SPV, which has so far been reserved exclusively for commercial companies holding legal personality, and established each time for the purpose of a given transaction.

Referring to the introduced legislative solutions as a whole, it should be mentioned that they provide for the application of the latest solutions for asset securitization.

[17] K. Piotrowska-Marczak, B. Mikołajczyk, *Perspektywy reform ochrony zdrowia w Polsce*, [in:] *Koncepcje zmian z Samodzielnym Publicznym Zakładzie Opieki Zdrowotnej*, ed. M. Węgrzyn, D. Wasilewski, Wrocław 2004, p. 31-34.

[18] Investment Funds Act of 27 May 2004 ("Journal of Laws" No. 146 item 1546, as amended).

This is because they enable either securitization in a form of assignment or with the use of sub-participation (Art. 183 item 4 of the IFA). A securitization fund may issue either *pass-through* as well as *pay-through* certificates (Art. 189 item 1 of the IFA). There is also a possibility to arrange for the issue of subordinated securities (Art. 190 of the IFA). Moreover, amending the banking law, this Act introduced the possibility for the bank, as the initiator, to acquire that part of receivable debt that would not be paid by the original debtors - no more, however, than up to 10% of the debt total value (Art. 92a item 6 of the Banking Law Act)[19]. Furthermore, the Act has introduced two crucial changes: a possibility to process the debtors' personal data by the fund (Art. 193 item 5 of the IFA) as well as a lump-sum fee for an amendment to the record in the land and mortgage register, while securitizing the debts collaterised against mortgage (Art. 195 item 5 of the IFA). The solutions existing so far significantly hindered transactions of this kind, whereas it should be remembered that those conveniences relate only to securitization transactions, where the receivable debts are acquired and securities (certificates) are issued by the investment fund.

Some negative aspects of this Act need to be, however, highlighted. They are related to the issue of securitization of receivable debts against banks, as the entire regulation seems to favour, to a large extend, transactions of this kind. The legislator has introduced two types of securitization funds: standardized and non-standardized. The first one may have sub-funds opened only if the financial funds, as sourced from the issued certificates, are used for the acquisition of receivable debts against banks (Art. 185 item 5 of the IFA). On other instances, that fund may operate exclusively as a single fund, which makes it similar to the non-standardized fund (Art. 187 item 1 of the IFA). The second securitization fund, having the possibility to acquire various receivable debts, may issue its certificates only to legal persons as well as organisational units that have no legal personality (Art. 187 item 4 of the IFA), which narrows down the group of potential investors. While amending the pension fund regulations[20], the Investment Fund Act introduced a limitation according to which only 5% of assets of those entities may be covered by securities issued by the securitization funds (Art. 142 item 2a of the Pension Funds Act). It may be, however, much surprising as from the essence of the assets subject to securitization it may be concluded that they are a secure form of long-term capital investment.

In addition to some civil law aspects of securitization, the amendments binding as from 2004 introduced material changes to the provisions of tax regulations. The binding regulations provide for special rules of taxation of bank receivable debts, where the value of the credits and loans advanced, except for the capitalised interest,

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[19] Banking Law Act of 29 August 1997 ("Journal of Laws" No. 140 item 939, as amended, consolidated text: "Journal of Laws" of 2002 No. 72 item 665, as amended).

[20] Act on Organization and Functioning of the Pension Funds of 28 August 1997 ("Journal of Laws" No. 139 item 934, as amended), hereinafter: the PFA.

is not an income. This situation is different to cases in which enterprises are obliged to recognise the accrued income at the time of the sale. Therefore, the operation of granting a credit by a bank is neutral from the tax perspective and does not result in cost recognition by the borrower, except from the interest amount (Art. 16 item 1 sub-item 10a of the CIT Act[21] and Art. 23 item 1 sub-item 8a of the PIT Act[22]), the amount being simultaneously the bank's income. The bank can make provisions, recognised as tax-deductible costs (revenue earning costs), for the credits and loans advanced (Art. 15 item 1h of the CIT Act), and if collectability of those assets is doubtful, the bank may also make special provisions (Art. 16 item 1 sub-item 26 of the CIT Act), the value of which should be reduced by guarantees and collaterals for those receivable debts (Art. 16 item 2a of the CIT Act). In line with the introduction of amendments to the CIT Act, the Investment Funds Act stipulated that if bank assets under advanced credits are sold to a securitization fund, then the outstanding part of the assigned receivable debts under those credits and loans are not recognized by the bank as income (Art. 12 item 4 sub-item 15c of the CIT Act). However, the income shall be the interest along with the capitalized interest (Art. 12 item 4e of the CIT Act). The cost, as in the cases of non-bank receivable debts, shall be the loss from the disposal of the securitized receivable debts, and only up to the amount of the provisions made for them and previously recognised as tax-deductible costs less the value of the securities made for the credit (Art. 15 item 1h sub-item 2 of the CIT Act). In this way, the new regulations provide for booking higher tax-deductible costs with banks while securitizing receivable debts with the use of an investment fund, as opposed to selling the debts to other entities in the market.

The introduced legislation amendments, including in particular tax-related ones, triggered vital growth of asset securitization market, which covers exclusively overdue receivable debts against banks. At present, two development paths for that instrument may be observed in Poland. The first one involves securitization transactions concluded by the banks for overdue credits, where the value of the assets under securitization is high enough to find it profitable to establish a separate investment fund only to handle that transaction. The second path involves establishing, most frequently with a solid support of a debt collection company, a securitization fund, which would subsequently cover partial receivable debts and issue securities based on the receivable debts total. Table 3 presents the initial period of development concerning the securitization transaction and fund market.

The chronological presentation of establishing securitization funds shows that debt collection companies strongly participated in its initial phase, and while pursuing exploitation of the potential and experience held in debt handling, they

[21] Corporate Income Tax Act of 15 February 1992 ("Journal of Laws" No. 21 item 86, consolidated text: "Journal of Laws" of 2000 No. 54 item 654, as amended).

[22] Personal Income Tax Act of 26 July 1991 ("Journal of Laws" No. 80 item 350, consolidated text: "Journal of Laws" of 2000 No. 14 item 176, as amended).

endeavoured to encourage potential creditors to sell their receivable debts. Legal regulations, especially tax-related ones, narrowed down the circle of initiators to banks exclusively.

**Table 3.** Transactions of asset securitization in Poland upon amendments to the IFA

| No. | Transaction date | Transferor | Receivable debt type | Value of receivable debt transferred | Society managing investment fund | Debt collection company handling securitized receivable debts |
|---|---|---|---|---|---|---|
| 1. | Summer 2005 | No data | Partial receivable debts and credits of Kredyt Bank S.A. | No data | TFI Copernicus Capital | Best S.A. |
| 2. | Autumn 2005 | Bank PKO BP S.A. | Overdue credits | PLN 735m. | PKO/Credit Suisse | P.R.E.S.C.O. |
| 3. | November 2005 | No data | Partial receivable debts | No data | BPH TFI | Kruk |
| 4. | February 2006 | Dominet Bank | Credits of entrepreneurs | Up to PLN 600m. | Polish Assets SPV | – |
| 5. | March 2006 | Raiffeisen Bank Polska | Receivable debts due to lease | EUR 270m. | Bank KfW | – |
| 6. | June 2006 | BGŻ | Overdue credits | ca. PLN 700m. | Selected by Lehman Brothers | Selected by Lehman Brothers |

Source: own study based on: E. Więcław, *Złe długi na sprzedaż*, "Rzeczpospolita", 2 September 2005, appendix: Ekonomia; E. Więcław, *Ponad 6 miliardów złotych do odzyskania*, "Rzeczpospolita", 12 October 2005, appendix: Ekonomia, Sz. Karpiński, *Zakupy długów w modzie*, "Rzeczpospolita", 23 June 2005, appendix: Ekonomia; A. Krakowiak, *Niespłacone pożyczki trafiły do nowego właściciela*, "Rzeczpospolita", 7 June 2006, appendix: Ekonomia.

Attention should be as well paid to the securitization of assets under lease, as carried out by Raiffeisen Bank Polska. This is a joint securitization of Polish and Czech (Raiffeisenbank a.s.) banks, which belong to Raiffeisen International Bank-Holding AG. The exceptionality of this transaction results from the fact that this has been the first joint asset securitization at this scale. Its initiators were Dresdner Kleinwort Wasserstein and Raiffeisen Zentralbank Österreich AG, whereas the European Investment Fund took part in that transaction as an investor. The mechanism of this securitization is based on transfer of risk of insolvency from the Polish and Czech banks to German bank KfW by way of credit default swap. The procedure exploits KfW "Promise" securitization platform, on which the bank brings together the risk related to the portfolio of both banks and secures it by way of a synthetic transaction. This securitization provides for the supplementation of the transactions

that reached their maturity with new ones during 5 years, whereas the estimated time limit for swap maturity is 7 years.

During the subsequent stages of development, the securitization market was limited in Poland to bank receivable debts. Currently, no transactions involving other receivable debts are concluded, and the sale of bank assets is based exclusively on securitization funds that handle, in co-operation with large debt collection companies, the repayment of receivable debts by the debtors to the funds with respect to subsequent pools of the receivable debts received.

Analysing bank asset securitization in the light of the described theories on innovation, a reference should be made to the primary (i.e. before the discussed regulations were introduced) limits and benefits of securitization of assets in Poland. The first group may include legal as well as organisational and technical barriers:

- impossibility to transfer assets based on credits incurred by consumers without their consent;
- tax burdens related to off-balance sheet securitization;
- difficulties with transfer of receivable debts under mortgage credit;
- difficulties with transfer of receivable debts collaterised with registered pledge;
- difficulty in credit rating of bank assets.

The first four aspects refer to legal and technical limitations as they entail the consent of the consumers to replace the creditor, or require relevant adjustments to be made with national registers (land and mortgage register, pledge register), which in the case of large pool of receivable debts makes their securitization impossible[23]. At the same time, every change in the register brings about additional costs. Ambiguously regulated burdens under the public law also expose the participants of this transaction to a greater risk, which, as a consequence, directly affects the transaction profitability. Nevertheless, due to amending the Investment Funds Act, the first and third limit was completely abolished, and as a result of making the transaction tax treatment detailed, the public law costs of the transactions were determined in a clear-cut way. Those changes, however, relate only to bank receivable debts and impinge on the development of the entire market in an obvious way.

Moreover, it should be pointed out that the difficulty to rate the assets under securitization results from a relatively short period of operation of the Polish banking system under the market economy. No statistical data exists to provide for a correct evaluation of repayment of such receivable debts, which is, in particular, valid for the assets to be repaid on a long-term basis (e.g. mortgage loans). Nevertheless, it should be underlined that those limitations as well are to a large extent temporary in nature and possible to be eliminated in a long run. Therefore, in the light of the theory by E.J. Kane, no regulatory circumstances occur to enable securitization to be regarded as a financial innovation. At the same time, neither are the costs of

[23] A. Pędzich, *Problemy przelewu wierzytelności banku z umowy kredytowej*, [in:] *Perspektywy rozwoju sekurytyzacji w Polsce*, Warszawski Instytut Bankowowści, Warszawa 1999, p. 82-84.

alternative regulations present, or if present, they do not exceed the cost of a potential securitization transaction (a theory by W.L. Silber), which does not provide for any incentive to introduce such an innovation either.

Similar conclusions may be reached in the course of analysis of potential advantages of bank asset securitization. The list may include[24]:

- gaining a cheaper source of financing;
- augmenting return on assets and owners' equity in case of off-balance sheet securitization;
- financing source diversification;
- unleashing the regulatory capital;
- adjusting the financing structure to asset maturity schedule.

Taking into account the ownership structure of the Polish banking system, where over 60% of the share is held by large international financing groups, Polish banks are not at present interested in gaining cheap financing, as it may be sourced immediately from their foreign shareholders. Neither are there incentives to diversify the sources of financing. The structural excessive liquidity in the banking sector in Poland does not prompt to gain financial funds either, but rather to search for lucrative investment projects. The competitive pressure in Poland is too weak to provide for a spur to introduce asset securitization. At present, the sole argument to be considered in favour of such a transaction is to make the return on assets increase. Such an increase has been so far forced by way of cost restructuring. In the future such a trend may trigger the need to conclude off-balance sheet securitization, which makes such ratios grow automatically as a result of excluding some of the assets from the balance sheet (i.e. making the balance sheet "shorter"). However, in such a case, the increase in return on assets is purely superficial.

## 5. Conclusions

It is difficult to falsify the first hereinabove hypothesis in a clear-cut way, which may be attributed to the multiplicity of theories, some of which have been briefly characterised herein, as well as to the diversity of the entities on the initiators' part of the whole process. Nevertheless, some conclusions may be presented to indicate the trends for developing such innovations as securitization in Poland:

a) innovations arise in those branches of the economy where no clear-cut rules of operation of public and private institutions exist;

b) an essential reason for developing an innovation is an attempt to downsize the statutory costs of transaction, as attributed to assertion of the ownership title;

c) the entities that have the base to introduce innovations (banks), follow this path exclusively upon the implementation of individual tax solutions, which enable them to ease the burdens under the public law;

[24] A. Grubman, *Sekurytyzacja aktywów w procesie zasilania finansowego przedsiębiorstw*, "Bank i Kredyt" No. 2, 2002, p. 66.

d) deficient, and also resultant from the prescriptive regulations, supply of capital in the financial market.

The first two conclusions are derived from the branch of the Polish health care system, which for fourteen years of functioning under the market economy has not lived up to a coherent model of operation. Therefore, such innovations as securitization become an attempt to solve comprehensive problems, which does not, however, translate into the improvement of the condition of the whole sector. It should be added as well that in this very case, securitization *de facto* postpones only the repayment of debts, possibly by way of instalments and with reduced costs of their handling. Due to the failure to the simultaneous restructuring, the main problem, i.e. the very debt itself, remains in general unsolved.

The failure to develop innovations independently by financial institutions is also worth considering. As already mentioned above, bank assets are securitized only after tax preferences have been introduced for that group of initiators. In view of the capital supply, regulatory and factual solutions reduce the actual volume of supply. Taking into account also the large structural demand on the part of the State Treasury, as realized by way of standardized instruments (treasury bills and bonds), a narrow market strip has been left for enterprises. In conjunction with minor values of potential issues, the costs of introducing innovations go up whereas no sufficient supply of financial means can be found for large transactions.

In order to summarize, it needs to be stated that although perceived as an innovative solution, securitization in the Polish market should not be approached as an innovation in the meaning of the theories valid for finance studies. This is true, in particular, for bank receivable debt securitizations, which are a consequence of the introduced legal regulations, and not of independent creation of new solutions by financial institutions.

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## SEKURYTYZACJA W POLSCE JAKO INNOWACJA NA RYNKU KAPITAŁOWYM

**Streszczenie:** Przedmiotem opracowania są polskie emisje sekurytyzacyjne w perspektywie wypracowanych na świecie teorii innowacji. Problematyka innowacyjności na rynkach kapitałowych doczekała się szeregu teorii naukowych, próbujących wyjaśnić ich przyczyny. Polski rynek kapitałowy od początku lat dziewięćdziesiątych ubiegłego wieku został także włączony w ten ogólny trend, który związany jest głównie z implementacją stworzonych już rozwiązań. Przykładem takich działań mogą być emisje sekurytyzacyjne, które mają miejsce w Polsce od 1997 roku. Celem niniejszego artykułu jest falsyfikacja hipotezy związanej z innowacyjnością transkacji sekurytyzacyjnych w Polsce.