



IN THIS EDITION

Luxembourg Securitisation Vehicles

The law of March 22, 2004 on securitisation (the **Securitisation Law**) and the law of August 10, 1915 on commercial companies, as amended (the **1915 Law**) govern Luxembourg securitisation vehicles (the **SVs**).

Definition and types of SVs

“*Securitisation*” is defined as the transaction by which a securitisation undertaking acquires or assumes, directly or indirectly through another undertaking, risks relating to claims, other assets, or obligations assumed by third parties or inherent to all or part of the activities of third parties, and issues securities (*valeurs mobilières*), the value or yield of which depends on such risks.

There are three types of SVs:

- (i) securitisation undertakings, which carry out the securitisation in full (i.e. they acquire the securitised risks and issue the securities),
- (ii) undertakings, which participate in the securitisation transaction by assuming all or part of the securitised risks - the **acquisition vehicles**,
- (iii) undertakings, which participate in the securitisation transaction by issuing securities to ensure the financing thereof - the **issuing vehicles**.

The SV’s articles of association, management regulations or issue documentation have to provide for specific submission to the Securitisation Law.

Available forms

An SV can be structured as a company or as a fund.

An SV company may be set up as a public limited liability company (*société anonyme*) (S.A.), a corporate partnership limited by shares (*société en commandite par actions*), a private limited liability company (*société à responsabilité limitée*) (S.à r.l.) or a co-operative company organised as a public limited liability company.

Definition and types of SVs	1
Available forms	1
Compartmentalisation	2
Supervision	2
Financing	2
Securitisable risks	3
Acquisition of securitised risks	4
Management of assets	4
Taxation	4
Conclusion	5

The minimum share capital for an S.A. is EUR 31,000.- and for an S.à r.l. - EUR 12,500.-.

An SV may also be formed as a co-ownership of assets (without legal personality), a so-called securitisation fund, to be managed by a Luxembourg-based management company in accordance with its management regulations. The securitisation fund may also be set up under a fiduciary arrangement, whereby the assets are being held by a fiduciary for the account of the investors.

Compartmentalisation

An SV may be compartmentalised, meaning that each compartment represents a distinct part of the assets and liabilities of the SV. The compartmentalisation allows for the segregation of the assets and liabilities between various compartments, whereby assets are ringfenced on a compartment by compartment basis in the case of insolvency of the SV. The rights of recourse of the investors and creditors are limited to the assets of the SV. Where such rights relate to a specific compartment or have arisen in connection with the creation, the operation or the liquidation of a specific compartment, the recourse is limited to the assets of the relevant compartment. Between investors, each compartment is treated as a separate entity, unless otherwise provided for in the constitutional documents of the SV.

The constitutional documents of an SV may authorise the management body of the SV to create one or more compartments.

Supervision

Luxembourg SVs are in principle unregulated entities and are not subject to any authorisation or prudential supervision, unless the SV issues securities to the public on a continuous basis. In the latter case, the SV must be approved by the Luxembourg Supervisory Commission for the Financial Sector (the **CSSF**). An SV issues securities on a continuous basis, if it makes more than three issues to the public per year (CSSF 2007 Annual Report (the **2007 Report**)).

The issue of securities to professional clients as defined in Annex II of Directive 2004/39/EC of April 21, 2004 on markets in financial instruments (the **MiFid Directive**) is not considered by the CSSF as an issue to the public for the purpose of the Securitisation Law. Securities issued with a nominal value of at least EUR 125,000 each, are presumed as not being issued to the public (this is different from the definition used in the Prospectus Directive). Private placements do not constitute an issuance to the public. However, the characterisation of private placement is assessed on a case-by-case basis by the CSSF and, for instance, the subscription of securities by an institutional investor or financial intermediary with a view to a subsequent placement of such securities with the public does constitute a placement with the public for the purpose of the Securitisation Law.

Whereas unregulated SVs are not required to appoint a custodian bank, regulated SVs have to entrust the custody of their liquid assets and securities to a credit institution established or having its registered office in Luxembourg.

The annual accounts and financial statements of both regulated and unregulated SVs have to be audited by one or more independent auditors (*réviseurs d'entreprises*).

Reporting obligations

Both regulated and unregulated SVs, which qualify as financial vehicle corporations engaged in securitisation transactions have to comply with the reporting obligations laid down in (i) the Regulation (EC) Nr 24/2009 of the European Central Bank of December 19, 2008 concerning statistics on the assets and liabilities of financial vehicle corporations engaged in securitisation transactions (the **ECB Regulation**) and (ii) the circular BCL 2009/224 of the Luxembourg Central Bank dated June 8, 2009 on statistical data collection for securitisation vehicles (notably notifying the Luxembourg Central Bank of its existence and reporting certain data on a quarterly basis). The Luxembourg Central Bank may grant derogations to certain obligations in the circumstances specified in the ECB Regulation.

Financing

The acquisition of the securised risks by an SV has to be financed through the issuance of securities (*valeurs mobilières*), the value or yield of which is linked to such risks. There is no definition of securities (*valeurs mobilières*) in the Securitisation Law. However, (i) instruments, which are considered as securities under their governing law (*lex contractus*), and (ii) financial instruments, which are negotiated on the capital markets and transferable, will be recognised as securities for the purpose of the Securitisation Law (2007 Report). By derogation to the 1915 Law, shares (*parts sociales*) issued by an SV organised as a private limited liability company (*société à responsabilité limitée*) will also be considered as securities (despite the fact that they are not freely transferable).

An SV may issue equity and debt securities in bearer or registered form (subject to the limitations set forth by the 1915 Law). There is a high degree of contractual flexibility and, accordingly, an SV may issue securities the value or yield of which is linked to specific compartments, assets or risks, or the repayment of which is subject to the repayment of other instruments, certain claims or certain categories of shares. Insolvency remoteness can be achieved through the use of limited recourse, non-petition and subordination provisions in the issuance or constitution documentation of the SV.

The possibility for SVs to use leverage by borrowing funds from third parties is accepted by the CSSF, provided the SVs are substantially financed through the issuance of securities (2007 report). An SV may borrow (i) during the warehousing phase on a temporary basis (taking into account market conditions), or (ii) for liquidity (matching) purposes to cover temporary shortfalls. In each case, the issuance documentation has to disclose the additional risks for investors generated by such leverage.

SVs do not have to comply with any debt/equity ratios.

Securitisable risks

Risks relating to the holding of assets, whether movable or immovable, tangible or intangible, as well as risks resulting from the obligations assumed by third parties or relating to all or part of the activities of third parties, may be securitised. During the last years, the securitisation transactions in Luxembourg involved diverse assets, such as commercial loans, mortgage loans, car lease receivables, consumer credits, non-performing loans, deferred purchase receivables, commodities, operating businesses, etc.

The CSSF has loosened certain of its previous positions in this respect. In its 2007 Report, the CSSF thus clarified the legal environment applying to SVs, by accepting:

- the possibility to securitise loans not yet fully drawn down or revolving loans: such loans must contain a pre-determined framework and the SV cannot have any discretion regarding the choice of borrowers or the terms of the loans;
- the possibility to securitise commodities: provided that the acquisition by the SV is designed to provide financing, and the commodities constitute a collateral securing the repayment of the obligations of the entity to whom the financing is provided and generate cash flows in favour of the investors;



- the possibility to securitise and repackage shares or units in UCIs, hedge funds, limited partnerships or other companies holding the securitised risks: provided that the SV is not actively involved in the management of the entities in which it has a participation (direct or indirect), and the SV does not provide services of any nature to such entities; and
- the possibility to securitise intra-group loans: provided that the risk assumed by the SV is effectively transferred by a separate entity of the group and that a substantial part of the securities issued by the SV are subscribed by third party investors.

Acquisition of securitised risks

The SV may assume the securitised risks by acquiring the underlying assets, by using credit derivatives or by committing itself in any other way. Securitisation transactions (notably transactions involving the use of credit derivatives) do not constitute insurance activities subject to the Luxembourg law of December 6, 1991 on the insurance sector.

The assignment of an existing claim to, or by, an SV becomes effective between the parties and against third parties as from the moment the assignment is agreed upon, unless otherwise agreed. A future claim may also be assigned. The assignment of a claim to, or by, an SV entails the transfer of the underlying guarantees and security interests securing such claims, and its effectiveness against third parties by operation of law, without any further formalities.

Management of assets

An SV must have a passive attitude when managing its assets. It cannot engage in commercial activities or any other activities pursuant to which it would act as entrepreneur or merchant and generate any personal risk as a result of such activities.

An SV may entrust the assignor or a third party with the collection of the securitised receivables, as well as other management tasks, without such persons having to apply for a licence under the Luxembourg law on the financial sector.

An SV cannot assign its assets, except in accordance with the provisions set forth in its constitutional documents. It may only grant security interests over its assets in order to secure the obligations it has assumed for their securitisation or in favour of its investors. Security interests and guarantees created in violation of this restriction are void by operation of law.

Taxation

One of the main reasons in selecting a Luxembourg SV is its tax efficiency and neutrality. A corporate type SV is subject to Luxembourg corporate income tax and municipal business tax. It will thus be regarded by the Luxembourg tax authorities as Luxembourg tax resident, and should also be covered by the Parent-Subsidiary Directive. The SV is exempt from the annual net wealth tax of 0.5%. Obligations (*engagements*) vis-à-vis its investors and other creditors ((future) dividends, interest, etc.) are considered to be deductible "interest payments" for income tax purposes. If properly structured, the taxable income of an SV can in that case be minimal. The distributions are not subject to withholding tax. A non-resident investor owning or having owned a participation of more than 10% in the share capital of an SV may be subject to Luxembourg income tax in case shares are transferred within six months following their acquisition, unless treaty protection is available for such investor.

A common fund type SV is transparent for tax purposes, hence it will not be subject to corporate income tax, trade tax or net wealth tax. Distribution of profits is not subject to Luxembourg withholding tax.

No capital duty tax is due upon incorporation of an SV or an increase of its share capital. Only a nominal registration fee of EUR 75 is due upon such occasions.

Payments of dividends or interest by an SV to an individual investor or certain so called residual entities resident in an EU Member State or certain associated territories may be subject to a 20% withholding tax under the EC Savings Directive (35% as per July 1, 2011), unless the name and address of the beneficiary and the amount of income received is disclosed to the Luxembourg tax authorities.

Management services rendered to an SV are exempt from VAT.

Conclusion

The Securitisation Law, with its flexible, lightly regulated and tax efficient regime, provides a wide range of vehicles for securitisation and structured finance transactions. The success of the Securitisation Law is confirmed by the significant number of SVs incorporated in Luxembourg over the last years, as well as the diversity in terms of structures and eligible assets.



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