



# Securitisation In Luxembourg

**A Securitisation Vehicle ("SV") assumes either directly or indirectly, present or future risks relating to claims, assets, or obligations assumed by third parties and issues securities. The value or yield of these securities is tied to the performance of the underlying portfolio of assets.**

The Securitisation Law implemented on 22 March 2004 (the "**Law of 22 March 2004**", or the "**Securitisation Law**"), modernised the statutory framework for securitisation and structured finance transactions in the jurisdiction. Luxembourg has long been regarded as a stable, investor-friendly environment. This legislation further enhanced the attractiveness of the region for securitisation and structured finance transactions by providing a broad definition of securitisation and allowing for a high degree of structuring flexibility. Since the introduction of the legislation, there has been continued steady growth in the market with currently over 1,200 active SVs established in Luxembourg.

On 9 February 2022, the Luxembourg parliament adopted Law No. 7825 (the "**Amended Law**"). The Amended Law introduces a number of amendments, further enhancing and modernising the regulatory regime initially established in the Securitisation Law, initiating greater flexibility to structuring options, whilst simultaneously enhancing legal certainty and ensuring investor protection.

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*Luxembourg has long been recognised as a very favourable environment for securitisation transactions. With the introduction of the Amended Law, the regulatory framework now offers even greater flexibility for investors. In particular, the modifications will increase the region's capacity to attract actively managed CLOs and CDOs.*

**Rodney O'Rourke,**  
**Chief Executive Officer**

# Securitisable Assets

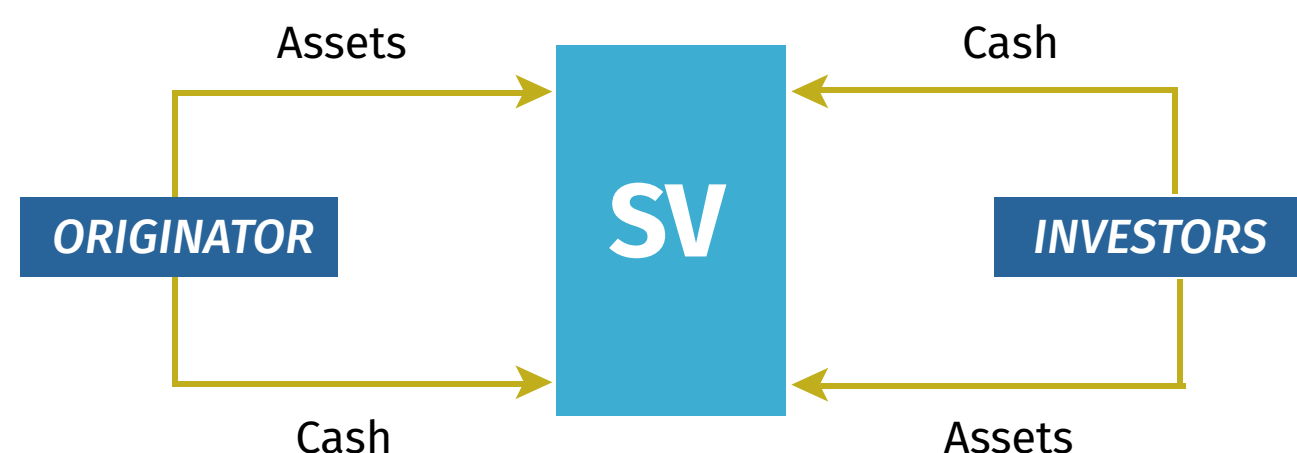
Under the Amended Law, the term “securities” has been replaced with the broader term “financial instruments” and regards financing by the issuance of financial instruments, or by entering into any form of loans; in whole or in part, a change which significantly expands the type of instruments that may be issued by a securitisation vehicle through enabling the use of financial instruments that did not previously qualify under the definition of securities.

- Shares
- Loans
- Commercial papers
- Consumer credits
- NPLs
- Commodities
- Income from operating businesses
- Bonds
- Risks relating to all types of assets
- Property, both tangible and intangible
- Risks resulting from the obligations assumed by their parties or relating to all or part of the activities of third parties
- Life assurance policies
- Equity investments
- Collateralised Loan Obligations (“**CLOs**”)
- Collateralised Debt Obligations (“**CDOs**”)
- Any other type of asset with a real value or future income

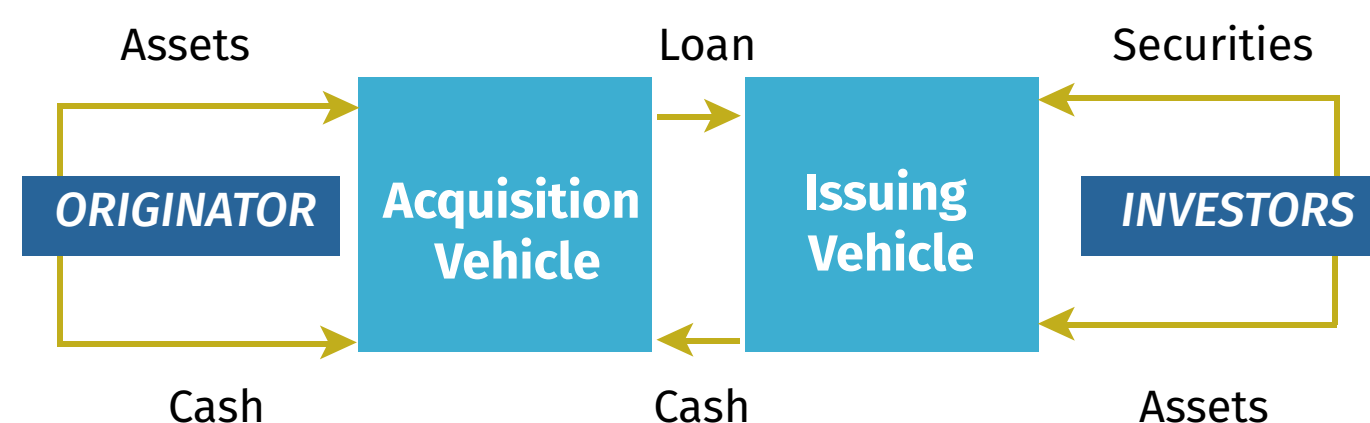
# Types of SV Structures

Securitisation may be carried out by a single-tier structure or a two-tier structure with separate entities established for acquisition of assets and the issuance of securities.

## Single Tier Structure



## Two Tier Structure



Within a two-tier structure, acquisition vehicles may be established in the country of the originator or where the assets are located, which may offer a number of tax, legal and operational advantages.

# Securitisation Company

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## A securitisation company can take the form of a:

- Public limited company (société anonyme) ("**SA**")
- Private limited company (société à responsabilité limitée) ("**S.à r.l.**")
- Partnership limited by shares (société en comandite par actions) ("**SCA**")
- Cooperative organised in the form of a public limited liability company (société cooperative organise as a société anonyme) ("**SCOOP**")
- General partnership (société en nom collectif) ("**SNC**")
- Simple limited partnership (société en commandite simple) ("**SCS**")
- Special limited partnership (société en commandite spéciale) ("**SCSp**")
- Simplified joint stock company (société par actions)

Most Luxembourg SVs are structured as companies with S.A and S.à r.l. the most commonly utilised structures. The minimum share capital for an S.A. is €30,000 and €12,000 for a S.à r.l.

Fully taxable but benefit from a specific tax regime meaning they may have a taxable basis close to nil.

Will be subject to the same applicable legislation as other commercial companies and benefit from Luxembourg's network of double tax treaties.

Where SVs opt to be established in the form of a legal partnership, such as an SNC, SCS or SCSp, the Amended Law requires the publication of annual accounts in accordance with the provisions of the law of 19 December 2002, with the Registre des Commerce et des Sociétés ("**RCS**").

## Securitisation Fund

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### Can be structured as:

- Co-ownership of assets (one or several co-ownership funds); or
- Fiduciary estate (subject to the legislation on trusts and fiduciary contracts).

### Benefits of a securitisation fund:

- Does not have a legal personality
- Tax Transparent. Not subject to subscription tax
- Management services are exempt from VAT. Represented by a management company with a registered office in Luxembourg
- Minimum share capital requirements only apply to the management company

## Securitisation Company

SVs may be internally divided by the creation of ring-fenced compartments. Compartments are created by a simple decision of the management body of the SV however, the ability to create compartments must be disclosed in the constitutional documents of the SV.

Where multiple compartments are prevalent, each compartment is treated as a separate entity, corresponding to a distinct pool of assets, rules, and securities. Investors avoid the spill-over of risks and liabilities between compartments, reducing the administrative costs and burdens relating to the set-up and management of separate entities. A compartment may be liquidated without bearing an impact on the other compartments of the SV.

Under the Amended Law, the securitisation vehicle may continue to take certain decisions at a compartment level and when provided for in the constitutional documents, the balance sheet and profit and loss accounts for a specific compartment may be approved by the shareholders of that compartment, without affecting other compartments.

Similarly, the profit and distributable reserves may also be determined on a compartment basis. The legal reserve should only be determined on a compartmental basis. This type of accounting segregation aims to protect the investors of each individual compartment.

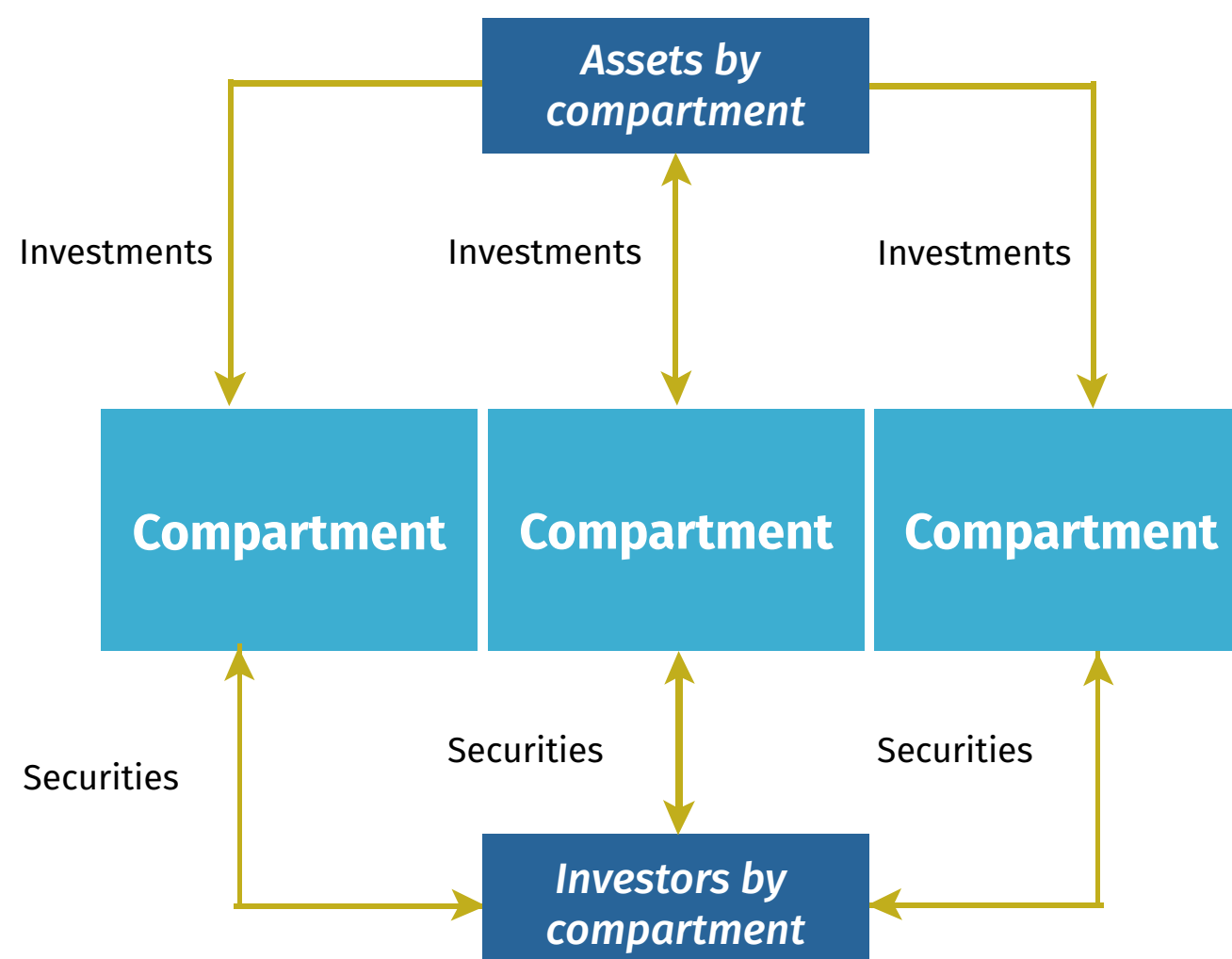
## Types of Securitisations

In Luxembourg, securitisations are categorised as “Traditional”, “Synthetic”, “Insurance-Linked” or “Other” securitisations.

### Traditional Securitisation

A traditional securitisation is evident where an asset or pool of assets, or part thereof, is transferred to an entity that is separate from the originator and is created for or serves the purpose of the transaction or scheme, either by the transfer of legal title or beneficial interest of those assets from the originator or through sub-participation. An SV acquires the legal and beneficial ownership of assets from the originator through the issuing of securities wherein the repayment is linked to the cash flows from the assets acquired.

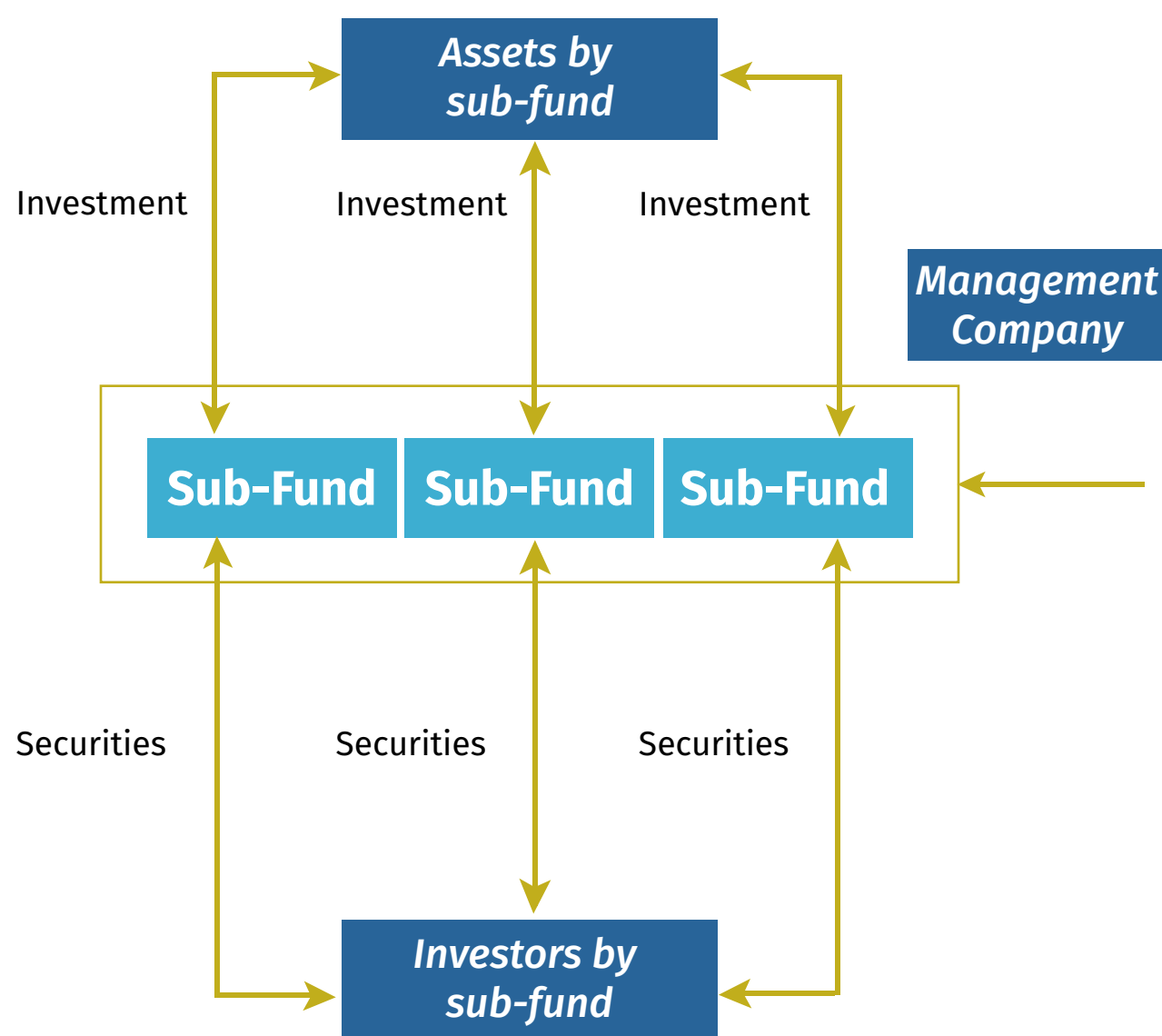
#### Securitisation Company



## Synthetic Securitisation

A synthetic securitisation constitutes the credit risk of an asset or pool of assets, or part thereof, is transferred through the use of credit derivatives, guarantees or any similar mechanism to the investors in the financing instruments issued by an entity that is separate from the originator and is created for or serves the purpose of the transactions or scheme. An SV acquires the risk associated with underlying assets in the form of derivatives or guarantees. The originator retains the legal and beneficial ownership of the assets. The amount payable by an SV to the originator is calculated with reference to the value of the underlying assets.

### Securitisation Fund



## Insurance-Linked Securitisation

An insurance-linked securitisation is classed as such when insurance risks are transferred from an insurance or reinsurance undertaking to a separate entity that is created for, or serves the purpose of the transaction or scheme, whereby the entity fully funds its exposure to such risks through the issuance of financing instruments, and the repayment rights of the investors are subordinated to the reinsurance obligations of the entity.

## Other Securitisation

Any securitisation that is not categorised within the first three categories.

## Legal Framework

The Securitisation Law provides for an “opt-in” regime, meaning that only the entities that submit themselves to its provisions in their establishment documents, management regulations or issuance documentation will benefit from the advantageous legal framework established by the Securitisation Law and the Amended Law.

## Regulated vs. Unregulated Vehicles

In principle, Luxembourg SVs are not regulated or subject to any prior authorisation or regulatory supervision. They are also not required to comply with risk spreading, diversification requirements or debt/equity ratios.

Under certain conditions, SVs may become entities regulated by the Luxembourg Financial Supervisory Authority, Commission de Surveillance de Secteur Financier, (the “**CSSF**”), namely if:

- They issue securities to the public; and
- They issue securities on a continuous basis. The threshold for issuing securities on a continuous basis is set at three or more issuances per year. In the case of SVs with multiple compartments, this is measured on a consolidated basis and not by each individual compartment.

The Amended Law provides clarification that an offer may only be considered made to the public where all of the following criteria are met:

- The securities in question have a denomination of less than €100,000;
- The securities would not be addressed to professional clients as defined in the article 1(5) of Luxembourg Law of 5 April 1993; and
- The issuance will not be conducted under a private placement arrangement.

For SVs with a cross-border structure, where an acquisition vehicle is located in Luxembourg and the issuing vehicle is located outside of the country, there is no requirement for authorisation from the CSSF.

## Transaction Parties



# AIFM

In some cases, SVs may, in addition to the regulation on securitisation, fall within the scope of the requirements for an Alternative Investment Fund Manager ("**AIFM**").

The Directive 2011/61/EU of 8 June 2011 on Alternative Investment Fund Managers, as amended ("**AIFMD**") and the Law of 12 July 2013 on alternative investment fund managers, as amended (the "**AIFM Law**") provide for the exclusion of securitisation special purpose entities ("**SSPEs**"). SSPEs are defined as entities whose sole purpose is to carry on a securitisation or securitisation within the meaning of the European Central Bank ("**ECB**") Regulation,

However, as the definition of securitisation within the ECB is not as broad as under the Securitisation Law, as amended, some SV's may not qualify as SSPEs and therefore will fall within the scope of AIFMD.

For example, securitisation vehicles issuing CLOs are considered to be engaged in a securitisation transaction and not subject to AIFMD. However, entities whose primary function is the origination of new loans are not recognised as engaged in the transaction and thus fall within the scope of AIFM.

Irrespective of whether an SV qualifies as an SSPE, they will not fall within the scope of AIFMD if they:

- Only issue debt instruments; or
- Are not managed in accordance with a 'defined investment policy'.

If an SV qualifies as an Alternative Investment Fund, then it must be managed by an appointed Alternative Investment Fund Manager.

## Financing

If an SV qualifies as an Alternative Investment Fund, then it must be managed by an appointed Alternative Investment Fund Manager.

The amendments introduced under the Amended Law allow for entirely debt financed securitisation vehicles, increasing access to investors otherwise subject to restrictions in relation to such financial products. Subject to the corporate form of the SV, securities may be issued in registered, dematerialised or bearer form. They may track a specific asset, pool of assets or compartment. SVs may issue different tranches of securities with a variety of yields and risk.

|                                |                                                                                                    |
|--------------------------------|----------------------------------------------------------------------------------------------------|
| <b>Registered Security</b>     | A security whose owner is kept on file with the issuer or a security whose transfer is restricted. |
| <b>Dematerialised Security</b> | A security with an electronic as opposed to a physical stock certificate.                          |
| <b>Bearer Security</b>         | A security that is owned by the bearer as opposed to the registered owner.                         |

Securities issued by SV's are deemed as debt securities, however, shares issued by an SV and structured as a S.à r.l. may qualify as securities. Securities may therefore be listed on the Luxembourg Stock Exchange, the Euro MTF or on other foreign stock exchanges.

Other financing options available for SVs include:

- Intra-Group Financing;
- Third Party Borrowing - Only on a temporary basis such as for the acquisition of risks or assets to be securitised or for liquidity purposes;
- Leverage Financing - Limited to the financing of the acquisition of assets; and
- Collateral and Guarantees Financing - Only in order to secure claims from investors, claims arising from commitments for the purpose of securitising these assets or connected claims of acquisition and issuing vehicles.

## Management of Securitised Risks

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As per the Amended Law, the active management of securitised risks is now permitted if the pool of assets is made up of debt securities, claims or debt financial instruments, provided they are issued by way of a private placement, thereby extending Luxembourg's capability to attract actively managed CLOs and CDOs.

The Amended Law builds on the existing offering in Luxembourg with respect to CLOs and CDOs that are not actively managed which was established under the Law of 22 March 2004.

The change introduced by the Amended Law means that securitisation vehicles for actively managed CLOs and CDOs are no longer bound to the 'buy and hold' strategy and are able to take active investment decisions with respect to the assets within the portfolio, enabling the portfolio to adapt to market developments.

## Subordination Rules

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The Amended Law clarifies the rules of subordination and priority of rights applicable in a securitisation transaction. The rules defined in the Amended Law are as follows:

- Units of a securitisation fund are subordinated to other financial instruments issued by the securitisation fund and borrowings contracted by the fund;
- Shares (actions), corporate units (parts sociales) or partnership interests (parts d'intérêt) in a securitisation company are subordinated to other financial instruments issued by such securitisation company and borrowings contracted by the securitisation company;

- Shares (actions), corporate units (parts sociales) or partnership interests (parts d'intérêt) in a securitisation company are subordinated to beneficiary shares (parts bénéficiaires) issued by the securitisation company;
- Beneficiary shares (parts bénéficiaires) issued by a securitisation company are subordinated to debt instruments issued and borrowings contracted by the securitisation company; and
- Non-fixed income debt instruments issued by a securitisation undertaking are subordinated to fixed income debt instruments issued by the securitisation undertaking.

Securitisation undertakings may derogate from the above rules either contractually or under their constitutional documents.

## Tax Regime

### Securitisation Company

Securitisation companies are treated as fully taxable entities subject to Corporate Income Tax ("**CIT**") and Municipal Business Tax ("**MBT**") on their consolidated income. However, the taxable income of a securitisation company may be reduced. Subject to certain conditions, payments to security holders are not subject to withholding tax. Securitisation companies are subject to a minimum annual Net Wealth Tax ("**NWT**") determined by the total assets of each SV compartment.

### Securitisation Fund

Securitisation funds are tax transparent vehicles, wherein the taxation of income generated occurs at the investor level rather than at the fund level. Securitisation funds are not subject to CIT, MBT, minimum annual NWT or subscription tax. In principle, a securitisation fund should not be entitled to the benefits of treaties or European Union Directives. Distributions by a securitisation fund are not subject to withholding tax.

### VAT

SVs are treated as VAT-taxable entities. However, their activities benefit from a VAT exemption. SVs are only required to register for VAT if they receive services from a foreign service provider.

Management services provided to an SV are exempt from VAT. Collateral management fees and investment advisory fees are also covered by this exemption, for so long as the services provided are considered specific and essential to the management of the SV. Fees relating to subscription, underwriting and placement may also qualify for a VAT exemption.

### Representation of Investor Interests

Similar to the treatment of bondholders, one or several persons may be designated to represent the investors'/creditors' collective interests in a securitisation transaction. Representation by an authorised fiduciary representative established in Luxembourg in charge of managing their assets is also permitted. It is possible to appoint a trustee governed by foreign law, to represent investors/creditors, once the terms of this representation are defined in the issuance documentation.

## Bankruptcy Remote

A "bankruptcy remote" entity is a term used to describe an entity established to own, develop and operate a specific transaction, while isolating financial risk and minimising bankruptcy risk.

There are a number of permitted tools which can be used in SVs to achieve a bankruptcy remote status. Most of these mechanisms are established by contractual arrangements between transaction parties. Such provisions may be outlined in the SV's issuance, or the SV's constitutional documents.

SVs are typically structured to eliminate any corporate connection between the originator to avoid any potential consolidation with respect to bankruptcy, accounting or tax legislation. As such, SV shares may be held in an "orphan vehicle".

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*Cafico International have extensive experience working with the originators of securitised assets, financial institutions, investment managers, arrangers, trustees, collateral managers and regulators across a host of financial transaction types.*

**Rodney O’Rourke,**  
**Chief Executive Officer**

## Bankruptcy Tools

|                                     |                                                                                                                                                                                                           |
|-------------------------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <b>Non seizure of assets</b>        | Investors and creditors waive their right to seize the assets of the SV.                                                                                                                                  |
| <b>Non petition clause</b>          | Investors and creditors waive their right to initiate any bankruptcy or insolvency proceeding against the SV.                                                                                             |
| <b>Subordinated clause</b>          | Investors and creditors subordinate their right of payment to the prior payment of other creditors or other investors.                                                                                    |
| <b>Limited/ Non-recourse clause</b> | Investors and creditors limit their financial recourse against an SV to the amount of proceeds received by the vehicle from the related underlying assets. This right may be waived on a temporary basis. |

# ■ Global Focus.

# ■ Local Expertise.

If you require further information regarding securitisation in Luxembourg, or if you would like to find out how Cafico International can help your business, please contact Arek Kwapien, Director of Corporate Services.



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