

# Securitisation in Luxembourg

2020







## Derivatives Law Firm of the Year

Risk Magazine Awards, 2013

## Securitisation and Structured Finance Team of the Year

IFLR Europe Awards 2015

## Luxembourg Law Firm of the Year

IFLR Europe Awards 2007, 2009 and 2010

## Most Innovative Law Firm in Europe

FT Innovative Lawyers Awards 2007, 2011, 2012, 2014, 2017 and 2018

“Allen & Overy is one of the best firms in Luxembourg. At least that’s the consistent message from clients across all departments. They describe the firm as having a ‘strong brand’, ‘good knowledge through to junior levels’ and being ‘leaps and bounds above the rest’. One even goes so far as to say that ‘every lawyer was perfect’.”

IFLR1000



# Contents

Types of Luxembourg Securitisation Undertakings	4
Regulatory Supervision by the CSSF	5
Key Advantages of the Securitisation Act 2004	6
Other Benefits	7
Variety of Structuring Options	8
Certain U.S. Regulatory Issues	9
Key Contacts	10



# Types of Luxembourg Securitisation Undertakings

- A securitisation undertaking subject to the Luxembourg act dated 22 March 2004 on securitisation, as amended (the Securitisation Act 2004), may take the form of a securitisation company or a securitisation fund.
- A securitisation undertaking wishing to benefit from the favourable regime of the Securitisation Act 2004 must be located in Luxembourg.
- It is possible to set up the Luxembourg structure as
  - (i) a single tier structure or (ii) a two-tier structure comprising an issuing vehicle and an acquisition vehicle.

## 1 Securitisation company (LuxSecCo) having a corporate form

	SA <sup>1</sup>	S.à r.l. <sup>2</sup>	S.C.A. <sup>3</sup>	Scoop <sup>4</sup>
Securities may be listed on a market <sup>5</sup>	●	● <sup>6</sup>	●	–
Securities may be offered to the public	●	–	●	–
Securities may be cleared in clearing systems	●	–	●	–
“Check the box” for U.S. tax purposes	–	●	●	–
Flexibility in terms of increase or decrease of the share capital	–	–	–	●

<sup>1</sup> société anonyme – public limited liability company

<sup>2</sup> société à responsabilité limitée – private limited liability company

<sup>3</sup> société en commandite par actions – partnership limited by shares

<sup>4</sup> société coopérative sous forme de société anonyme

<sup>5</sup> regulated market or alternative market

<sup>6</sup> except for equity

## 2 Securitisation fund

- Co-ownership of assets.
- No legal personality.
- Represented by a management company vis-à-vis third parties.
- No requirement for management company to be regulated.
- No annual subscription tax (taxe d’abonnement) (as due by investment funds).

# Regulatory Supervision by the CSSF

## Regulated LuxSecCo

- Licence required if offers of securities are made to the public on a continuous basis
- Out of scope of the Banking Act 1993
- Out of scope of the AIFMD (subject to conditions)
- Securities and cash must be held with a Luxembourg custodian
- Must appoint a statutory auditor
- Full benefit of the provisions of the Securitisation Act 2004

## Non-regulated LuxSecCo

- Suitable for private placements of securities and occasional public offers of securities (ie not made on a continuous basis)
- Out of scope of the Banking Act 1993
- Out of scope of the AIFMD (subject to conditions)
- Assets (including securities and cash) may be held with a Luxembourg or foreign custodian
- Must appoint a statutory auditor
- Full benefit of the provisions of the Securitisation Act 2004

## 1 Offers of securities to the public on a continuous basis

A LuxSecCo must obtain a licence (agrément) from the CSSF (Commission de Surveillance du Secteur Financier – Luxembourg financial sector regulator) if the following conditions are met cumulatively:

### **Securities are offered to the public**

The CSSF considers that securities are offered to the public if they are (i) issued to persons that do not qualify as professional clients within the meaning of the MiFID or (ii) issued with denominations below EUR125,000, unless a private placement has been carried out (an analysis has to be carried out in this respect on a case-by-case basis).

### **Public offers are made on a continuous basis**

The CSSF considers that a LuxSecCo makes public offers on a continuous basis if it offers its securities to the public more than three times per year.

## 2 Key aspects of regulated LuxSecCos

- The approval process involves the submission of an application file and a meeting with the CSSF.
- A number of intervening parties, such as the Luxembourg custodian, the board of directors, the shareholder(s) of LuxSecCo and the statutory auditor are subject to the CSSF's approval.
- Ongoing disclosure obligations vis-à-vis the CSSF (but no need to seek the prior approval of individual transactions).

# Key Advantages of the Securitisation Act 2004

## Wide range of securitisable assets

- Residential and commercial mortgage loans, corporate loans, credit card receivables and trade receivables
- Debt and equity securities
- Rights and claims relating to financial contracts (eg derivative agreements, synthetic transactions, fully funded swaps)
- Rights and claims relating to operating businesses
- Commodities
- Assets covered by financial leases
- Real estate (subject to certain restrictions)
- IP rights

## Bankruptcy remoteness and statutory recognition of contractual arrangements

- Non-petition
- Limited recourse
- Claim subordination
- Non-seizure of assets

## Multiple ways to finance a LuxSecCo

- Through the issue of securities
- All types of debt securities (notes, bonds, certificates) in registered, bearer or dematerialised form
- Warrants
- Equity securities (ordinary equity, preference shares/ non-voting shares and tracker shares)
- Beneficiary shares
- Through loans
- To build up assets portfolio (during warehousing period only)
- To cover temporary shortfall or ongoing expenses
- As leveraged financing (on ancillary basis only) to provide higher return to investors
- Possibility to set up notes issuance facilities (NIF), where notes are booked as debt securities by the LuxSecCo and as loans by investors

## Favourable tax regime

- Direct taxes
- Considered as a fully taxable Luxembourg company
- Tax deductibility of all payments (and commitments) made in respect of securities issued by the LuxSecCo, subject to the interest deduction limitation rules which may apply depending on the assets held by the LuxSecCo (not applicable to a LuxSecCo qualifying as “securitisation special purpose entity” (SSPE) within the meaning of Regulation (EU) 2017/2402 of the European Parliament and of the Council of 12 December 2017)
- Exempt from net wealth tax
- In most cases subject only to a minimum lump sum taxation of EUR4,815
- No withholding tax applicable to payments made by the LuxSecCo to its investors except for a 20% withholding tax with regard to interest payments made by a Luxembourg paying agent to Luxembourg resident individuals
- Possibility to obtain advanced tax agreements from tax authorities
- VAT: VAT exemption for management services
- DTTs: 83 double tax treaties in effect and 20 pending

# Other Benefits

- **A LuxSecCo can create an unlimited number of segregated compartments:**

- Compartmentalisation is embedded in Luxembourg statutory law and is not merely a contractual arrangement.
- Each compartment forms an independent part of a LuxSecCo's estate; assets allocated to the compartment are segregated from those allocated to any other compartment (notwithstanding the fact that a compartment does not have a distinct legal personality).
- A decision of a LuxSecCo's board of directors is sufficient to set up a new compartment (hence low operational costs even if each individual transaction is conducted under a new compartment).
- Assets in a compartment are ring-fenced: on the one hand, only creditors whose claims have arisen in connection with the relevant compartment have access to its assets; on the other hand, such creditors have recourse only against the assets of the relevant compartment.
- Under one compartment, a LuxSecCo may issue multiple series and tranches of securities denominated in different currencies and linked to different underlying assets.
- Compartments are generally regarded as separate issuers under the U.S. Investment Company Act of 1940 and thus may rely on different exceptions under such act (Rule 3a-7, Section 3(c)(7)) simultaneously, which provides programme sponsors with flexibility in offering various securitisations under one structure. At present, it is unclear whether a multi-series issuer enjoys the same treatment with respect to the U.S. Commodity Futures Trading Commission (CFTC) or under the Volcker Rule.

- No requirement for risk diversification.
- Debt recovery exempt from Luxembourg licensing requirements.
- No requirement for arrangers, managers or agents to be based in Luxembourg.
- Enforceability of contractual set-off and close-out netting.
- Recognition by Luxembourg law of foreign law-governed trusts.
- Rating agencies are familiar and comfortable with securitisation transactions by LuxSecCos.
- Robust legal opinions can be issued on securitisation transactions.
- Luxembourg State has an AAA credit rating.



# Key Advantages of the Securitisation Act 2004

## 1 Types of securitisations

- Both true sale securitisations and synthetic securitisations (including those linked to static indices or actively managed indices) are possible.
- A LuxSecCo may itself enter into securities lending transactions, repurchase agreements and derivatives in furtherance of a securitisation transaction.
- A LuxSecCo may carry out fund repackaging (subject to restrictions in offer jurisdictions).
- Portfolio of securitised assets may be managed by an external asset manager or remain static.
- Cash may be securitised to the extent that it is used as a collateral under a swap arrangement designed to hedge a LuxSecCo's payment obligations under its securities.
- Structures subject to the Securitisation Act 2004 are increasingly used for Islamic financing purposes.

## 2 Granting of loans by a LuxSecCo

- A LuxSecCo must not use funds received from the public for purposes of granting loans for its own account (as this would constitute banking activity).
- Documentation relating to the issue of securities must contain adequate disclosure of:
  - (i) the underlying activity financed out of the issue proceeds (the Activity); (ii) the borrower(s); or (iii) the borrower selection criteria; and
- the main characteristics of the loan(s) granted or to be granted by the LuxSecCo.
- Return on Activity must be sufficient to allow the LuxSecCo to meet its obligations under the securities it has issued.
- A LuxSecCo should not directly negotiate the terms of the loans – negotiations should be conducted by a third party on a LuxSecCo's behalf or a LuxSecCo should be assisted by a third party in such negotiations.

## 3 Repackaging of assets held by an investor

- If repackaged assets/risks are not linked in any way to the investor, investors' objectives (such as rationalisation of asset management/risk management/creation of ECB eligible collateral) must be analysed in order to determine if a transaction falls within the scope of securitisation.
- If repackaged assets/risks are linked in some way to an investor, a transaction will be regarded as securitisation only if such investor becomes a minority investor of the LuxSecCo or subscribes for equity tranche.



# Certain U.S. Regulatory Issues

## 1 U.S. Investment Company Act of 1940

- Securitisations offered to U.S. investors must be exempt from the U.S. Investment Company Act of 1940.
- Static pool securitisations can generally rely on the Rule 3a-7 exemption, while receivables securitisations generally rely on the Section 3(c)(5)(a)/(B) exemptions.
- Other types of securitisations typically rely on Section 3(c)(7), which requires U.S. investors to be ‘qualified purchasers’.

## 2 U.S. Commodity Exchange Act

- Securitisations that make use of commodity interests (including commodity total return swaps, options, forwards and futures) and that have some U.S. nexus (eg, U.S. investors, a U.S. manager, among other things) must have a CFTC-registered manager and operator.
- Certain manager and operator exemptions may apply, including an exemption for securitisations that trade a minimum amount of commodity interest.

## 3 Volcker Rule

- Certain securitisations are exempt from the Volcker Rule, including loan securitisations, asset-backed commercial paper securitisations, securitisations relying on the Investment Company Act exemptions mentioned in paragraph 1, ‘public foreign fund’ securitisations offered to retail investors outside the U.S. and, with respect to certain non-U.S. bank investors and sponsors, non-U.S. fund securitisations.
- Any bank can sponsor and/or invest in an exempt securitisation; a lack of exemption significantly limits sponsoring and investing activity by a bank subject to the Volcker Rule (which would include most U.S.-based banks and their non-U.S. affiliates, and non-U.S. banks with U.S. banking affiliates).

# Key Contacts

Please do not hesitate to contact the following persons:

## On questions related to Securitisation in Luxembourg

---



**Patrick Mischo**  
Partner – Luxembourg  
Tel +352 44 44 5 5233  
patrick.mischo@allenoverly.com



**Frank Mausen**  
Partner – Luxembourg  
Tel +352 44 44 5 5257  
frank.mausen@allenoverly.com



**Henri Wagner**  
Partner – Luxembourg  
Tel +352 44 44 5 5285  
henri.wagner@allenoverly.com



**Jean Schaffner**  
Partner – Luxembourg  
Tel +352 44 44 5 5613  
jean.schaffner@allenoverly.com



**Paul Péporté**  
Partner – Luxembourg  
Tel +352 44 44 5 5257  
paul.peporte@allenoverly.com



**Pierre-Henry Maroteaux**  
Counsel – Luxembourg  
Tel +352 44 44 5 5125  
pierre-henry.maroteaux@allenoverly.com



**Evelina Palgan**  
Counsel – Luxembourg  
Tel +352 44 44 5 5403  
evelina.palgan@allenoverly.com



**Serge Zeien**  
Counsel – Luxembourg  
Tel +352 44 44 5 5134  
serge.zeien@allenoverly.com



**André Hommel**  
Counsel – Luxembourg  
Tel +352 44 44 5 5102  
andre.hommel@allenoverly.com





For more information, please contact:

## Luxembourg

Allen & Overy  
5 avenue J.F. Kennedy  
L-1855 Luxembourg  
PO Box 5017  
L-1050 Luxembourg  
Tel +352 44 44 55 1

---

## GLOBAL PRESENCE

---

Allen & Overy is an international legal practice with approximately 5,500 people, including some 550 partners, working in over 40 offices worldwide.

**Allen & Overy** means Allen & Overy LLP and/or its affiliated undertakings. Allen & Overy LLP is a limited liability partnership registered in England and Wales with registered number OC306763. Allen & Overy LLP is authorised and regulated by the Solicitors Regulation Authority of England and Wales.

The term **partner** is used to refer to a member of Allen & Overy LLP or an employee or consultant with equivalent standing and qualifications.

A list of the members of Allen & Overy LLP and of the non-members who are designated as partners is open to inspection at our registered office at One Bishops Square, London E1 6AD.