HALSEY GROUP Sàrl

PROFESSIONAL SERVICES FOR COMPANIES

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SECURITIZATION

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Scope and legal regime

The Luxembourg securitization undertakings are subject to the amended law dated 22 March 2004 on securitization ("Securitization Law"). The Securitization Law defines securitization as the transaction by which a securitization undertaking acquires or assumes, directly or 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 whose value or yield depends on such risks.

The Securitization Law expressly foresees the possibility to create securitization undertaking under the corporate form (which is considered from a Luxembourg tax perspective as a Luxembourg resident fully-taxable company) or under the form of an unincorporated (contractual) fund not subject to any income taxes.

Article 5 of the Securitization Law allows the creation of undertakings (whether as a securitization company or securitization fund) with multiple compartments (umbrella structures) where each compartments will correspond to separate assets and liabilities and where each compartment will be segregated from the other compartments of the same undertaking as regards investors' and creditors' rights, effectively "ring-fencing" each compartment. This "ring-fencing" will also apply in case of liquidation, as a compartment can be liquidated without affecting the other compartments.

Pursuant to article 19 of the Securitization Law, securitization undertakings which issue securities to the public on a continuous basis must be authorized by the CSSF to exercise their activities, in which case they shall, in principle, remain regulated by the CSSF until their liquidation.

The regulated status is thus mandatory when both criteria ("issue securities to the public" and "on a continuous basis") are cumulatively met. A securitization undertaking may not, however, voluntarily opt for the regulated status if it does not meet cumulatively these two criteria.

The securitization undertaking must determine by itself if, in its particular case, it is to be considered as issuing securities to the public on a continuous basis, and such assessment does not need to be submitted for validation by the CSSF.

The Securitization Law does not provide strict definitions nor criteria to assess if these two conditions are met, but the CSSF has provided the following guidelines:

(I) the criterion of issue "on a continuous basis" is assumed to be fulfilled when the securitization undertaking makes more than three issues per year to the public. In the case of an umbrella structure, the number of issues to consider is determined by the total number of issues of all compartments of the securitization undertaking. In addition, the setting-up of an issuance program cannot be considered as equivalent to one single issue. In order to determine the number of annual issues of a securitization undertaking issuing securities under a program, the nature of the program and of the different series of issues must be analyzed in order to assess whether the characteristics of these issues allow considering that they constitute one single issue and not several separate issues.

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(II) the criterion relating to the issuance of securities "to the public" shall be assessed on the following basis:

- issues to professional clients within the meaning of Annex II to Directive 2004/39/EC (MiFID) are not issues to the public;
- issues whose denominations equal or exceed EUR 125,000 are assumed not to be placed with the public;
- the listing of an issue on a regulated or alternative market does not ipso facto entail that the issue is deemed to be placed with the public;
- issues distributed as private placements, whatever their denomination, are not considered as issues to the public. The CSSF assesses whether the issue is to be considered as a private placement on a case-by-case basis according to the communication means and the technique used to distribute the securities. However, the subscription of securities by an institutional investor or financial intermediary for a subsequent placement of such securities with the public constitutes a placement with the public.
- If the management of the securitization undertaking is of the opinion that it is about to fall within the scope of the Securitization Law, it must file an application for CSSF authorization, and abstain, from that moment, from initiating issues of securities which would make such prior authorization mandatory until it has obtained such authorization. It appears however from our contacts with the regulator that no such application for a conversion of an existing, non-regulated, undertaking into a regulated undertaking has yet been submitted to the CSSF.

Once authorized, the securitization undertaking shall in principle remain under the supervision of the CSSF until its liquidation. However, if, at one point, the securitization undertaking does not issue new securities on a continuous basis to the public, and on the condition that all the securities that the securitization undertaking has issued to the public during the time it was subject to supervision have matured and been refunded, the securitization undertaking may request to be withdrawn from the official list of authorized securitization undertakings.

Tax aspects

As opposed to securitization undertaking under the corporate form (which are considered from a Luxembourg tax perspective as a Luxembourg resident fully-taxable company), a securitization undertaking under the form of an unincorporated (contractual) fund is not subject to any income taxes. The tax regime of securitization undertakings under the form of an unincorporated fund is aligned on the tax regime applicable to ordinary Luxembourg investment funds.

The developments below only relate to securitization undertakings under the corporate form.

As a rule, according to the provisions of article 89 of the Securitization Law, any commitments of a securitization company towards its investors and/or other creditors are tax deductible business expenses in the meaning of article 97 (1) 5 ITL. As a consequence, a securitization company generally does not realize any taxable profits and hence will not actually pay income tax as any income or gain is normally offset by a tax deductible expense. In addition, distributions and other proceeds allotted to the investors and/or creditors, whatever the form they adopt (dividends or interests) are considered as interests from a Luxembourg tax perspective, which, whether fixed or variable, are fully deductible for the purpose of Luxembourg taxation at the level of the securitization company (article 46, paragraph 14 ITL) under the accounting/tax year to which they relate, even if their payment is delayed.

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Under Luxembourg tax law, a securitization company is a fully-taxable resident company which benefits from specific deductibility features and, as such, has access to Luxembourg tax treaties enabling it to benefit from reduced withholding taxes in the source countries of its investments.

In this respect, and absent any specific provision in the Securitization Law, a securitization company cannot be excluded from the benefit of the Luxembourg participation exemption as foreseen under article 166 ITL. In order to qualify for the participation exemption on dividends and/or capital gains, the following conditions must be met:

- The parent company must hold a direct participation in the share capital of an eligible entity, i.e. a company covered by article 2 of the EU parent-subsidiary directive (directive 2011/96/EU) or a non-resident company limited by share capital (société de capitaux) liable to a tax corresponding to Luxembourg corporate income tax;
- At the time the income is made available, the parent company must have held, or must commit itself to hold, the participation in the eligible entity for an uninterrupted period of at least 12 months and during this whole period, either the level of participation must not fall below the threshold of 10% or the acquisition price must not fall below EUR 1.2 million (6 million in case of capital gains).

The participation exemption regime contains however some rules intended to avoid a double benefit (exemption of income and deduction of expenses). If the acquisition of a participation is financed through an interest-bearing debt, such interest has an impact for the application of the participation exemption. Indeed, pursuant to article 166 (5) ITL, to the extent that received dividends are exempt, interests in direct economic relationship with these dividend incomes are not deductible (up to the related exempt income, the excess being deductible). Similarly, when a participation is disposed of, the capital gain exemption does not apply to the extent of the algebraic sum of the related expenses (for example, interest exceeding the exempt dividend income) that have decreased the tax result of the current and preceding years (so-called "recapture rule").

However, the securitization company cannot use concurrently for the same assets the participation exemption regime and the specific tax regime as provided for in the Securitization Law. If the participation exemption regime is applied towards income derived from participations qualifying for the dividends and capital gains exemption, interest paid in the context of financing the acquisition of such qualifying participations shall not be deductible (for the sake of clarity, dividends are generally not considered as tax deductible, except in the securitization regime).

As a consequence, within the context of a securitization company, it is not possible to receive exempt dividends under the participation exemption regime and deduct interests (or dividends qualifying as interest under that regime) payable under the securitization regime.

Finally, a securitization company is subject to a minimum NWT of EUR 4,815 if it holds fixed financial assets, receivables, transferable securities and cash at bank which exceed 90% of its total gross assets and EUR 350,000.

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Accounting aspects

The annual accounts of a corporate securitization vehicle are subject to the same accounting rules applicable to Luxembourg commercial companies. Annual accounts of a securitization fund are subject to similar accounting rules to those provided for an investment fund.

The accounts of all securitization vehicles must be audited by one or more independent auditors designated by the board of the securitization company, or by the management company in case of a securitization fund.

For a regulated vehicle, the auditor must be authorized by the CSSF.

Regulated and unregulated securitization vehicles, qualified as financial vehicle corporations engaged in securitization transactions, have to comply with quarterly reporting obligations imposed by the :

- Circulars of the Luxembourg Central Bank on statistical data collection for securitization vehicles ;
- Regulation of the European Central Bank in relation to statistics on the assets and liabilities of financial vehicle corporations engaged in securitization transactions.

The Luxembourg Central Bank may grant derogations to certain reporting obligations.

Services offers by Halsey Group

HALSEY has been established in Luxembourg for more than 20 years and has licenses from the "Commission de Surveillance du Secteur Financier" (CSSF), the Luxembourg Regulator, to provide domiciliation, fund administration and other corporate services. We provide a fast and reliable service to many private investors, leading institutions, major international corporations and private equity firms.

HALSEY offers its clients an extensive range of high quality services in connection with Luxembourg financial companies both at the time of incorporation and throughout the life of the company:

- Company formation
- Administrative and accounting
- Corporate secretarial
- Fund administration
- Company management
- Assistance in setting-up own offices & management of client staff

The objective of this fact sheet is to provide the reader with a general view of relevant aspects relating to the SECURIZATION. No action shall be taken without prior consultation with Halsey Group, as this document alone cannot cover all aspects relating to the incorporation and administration of the SECURIZATION. Finally, please note that this document is provided for information purposes only and should not be understood as legal or fiscal advice.