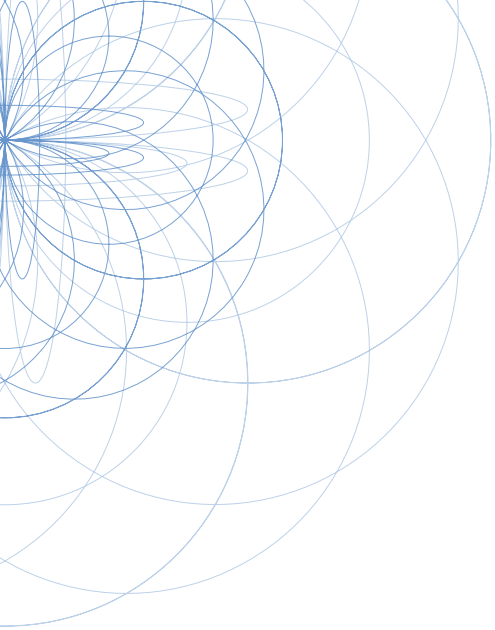
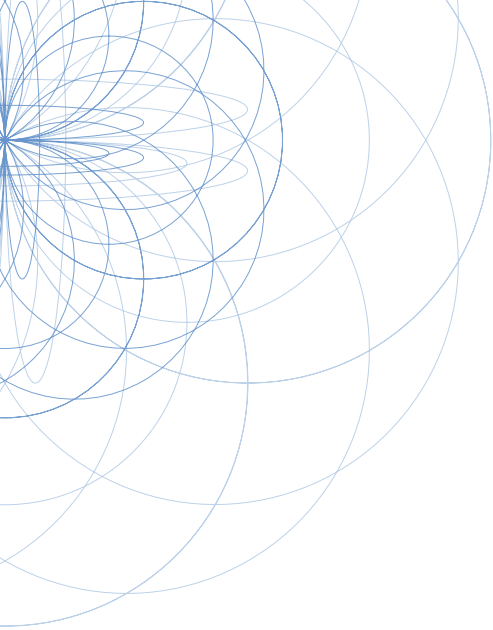
The Luxembourg Law on Securitisation Vehicles 2014



www.nautadutilh.com

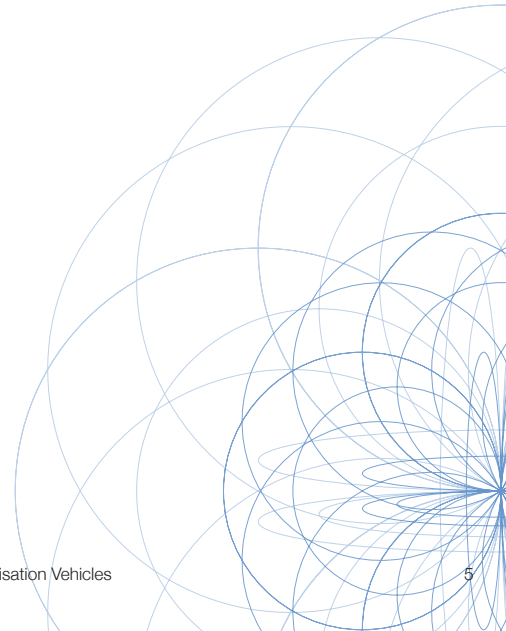
Table of contents



The Luxembourg securitisation act of 22 March 2004, as amended (the "**Securitisation Act**") provides an attractive and flexible legal, regulatory and tax framework for the establishment of securitisation vehicles.

The Securitisation Act applies to securitisation vehicles located in the Grand Duchy of Luxembourg (Luxembourg) and which elect to be governed by the Securitisation Act. It provides a complete legal framework covering all aspects of a securitisation transaction, providing to the originators, the investors, and the creditors of a securitisation vehicle the highest level of legal certainty.

The Securitisation Act defines securitisation as a transaction by which a securitisation 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.



1. Setting up of a securitisation vehicle

The legal form of a securitisation vehicle

A securitisation vehicle may either take the form of (i) a commercial company, or (ii) a fund managed by a management company based on management rules:

Securitisation company

Securitisation vehicles that take the form of a commercial company (a "securitisation company") are expressly governed by the Securitisation Act and the provisions of the act of 10 August 1915 on commercial companies, as amended (the "Companies Act").

A securitisation company may take the form of:

- a public limited liability company (*société anonyme* or "SA");
- a partnership limited by shares (*société en commandite par actions* or "SCA");
- a private limited liability company (*société à responsabilité limitée* or "S.à r.l."); or
- a cooperative organised as a public limited company (*société cooperative organisée sous forme de société anonyme* "SCSA").

A securitisation company needs only to meet the minimum capital requirement applicable to the chosen corporate form. This requirement must be met at the company level, not by each individual compartment.

It takes approximately six to eight business days to set up a securitisation company. In practice, a Luxembourg corporate service provider is appointed to provide the securitisation company with a registered office and, in most cases, directors as well as accounting and other administrative services. This appointment is formalised in a corporate service and domiciliation agreement with the securitisation company.

Securitisation fund

The Securitisation Act also allows a securitisation vehicle to take the form of a fund run by a management company and governed by management rules. A securitisation fund does not have legal personality.

The originator may choose to set up the securitisation fund as a co-ownership (*copropriété*), or, alternatively, on a fiduciary basis on behalf of its investors.

2. Regulatory aspects

Regulated vehicles

The Securitisation Act allows to set-up both regulated and unregulated securitisation vehicles. The latter are not required to obtain a license from the *Commission de Surveillance du Secteur Financier* (the "**CSSF**"). Such license is, however, required for regulated securitisation vehicles that issue securities to the public on a continuous basis.

Based on the CSSF's guidelines and in the absence of a definition of the term "public" in the Securitisation Act, a securitisation vehicle shall be deemed to offer securities to the public on a continuous basis if (i) it carries out, in total per annum, more than three (3) issuances of securities (at the level of the securitisation vehicle as a whole, not at the level of each individual compartment); (ii) the securities issued have a nominal value per security of less than EUR 125,000; and (iii) the securities issued are not subscribed for by professional investors within the meaning of Annex II of the Directive 2004/39/EC of the European Parliament and of the Council of 21 April 2004 on markets in financial instruments ("**MIFID**") or sold through a private placement. The listing of the securities issued on a regulated or alternative market does not constitute *ipso facto* an offer to the public.

Before granting a license, the CSSF must (i) approve the constitutional documents or the management regulations (as applicable) of the "securitisation vehicle"; (ii) verify the reputation of the members of the securitisation vehicle's administrative, management and supervisory bodies; (iii) examine the identity of direct or indirect shareholders able to exert a significant influence over the conduct of the vehicle's business; and (iv) validate the choice of Luxembourg credit institution appointed to act as the custodian of the vehicle's liquid assets and securities.

The CSSF usually agrees that the management of securitisation vehicles may be provided by legal persons, in which case the CSSF will, for the purpose of granting a license, assess the reputation of the managers of the legal person to be itself appointed as manager of the securitisation vehicle.

Once approved, the securitisation vehicle shall be included on the official list of securitisation undertakings, held and published by the CSSF and shall remain subject to the CSSF's supervision until the end of its liquidation, unless the securitisation vehicle has stopped issuing securities to the public and it has reimbursed securities issued during the period it was subject to the CSSF's supervision. The securitisation vehicle must provide periodical statements of its assets and liabilities and its operating results to the CSSF, which is entitled to request any information relating to the organisation, administration, management or operation of the vehicle.

In the context of cross-border securitisation structures, in case the securitisation vehicle is located in a jurisdiction other than Luxembourg and the acquisition vehicle is located in

Luxembourg (dual structure as detailed below), the Securitisation Act foresees that the entity located in Luxembourg will not be required to obtain a license.

Recent regulatory developments

Impact of the AIFM Act on securitisation vehicles

The Directive 2011/61/EU of the European Parliament and of the Council of 8 June 2011 (the "**AIFM Directive**") on Alternative Investment Fund Managers ("**AIFMs**") was implemented in Luxembourg law by the act of 12 July 2013 (the "**AIFM Act**"). It has a major impact on rules applying to the management of investment portfolios.

The AIFM Directive and the AIFM Act expressly excluded securitisation vehicles from their scope. Such exclusion seems to render securitisation vehicles even more attractive, both from an operational and a cost point of view.

The AIFM Directive and the AIFM Act use an autonomous definition of securitisation. Indeed, the formal exclusion foreseen under the AIFM Directive defines a securitisation vehicle as "*an entity whose sole purpose is to carry on securitisations as such term is defined at Article 1 (2) of Regulation (EC) 24/2009 of the ECB, and other activities which are appropriate to accomplish that purpose*". Alike the AIFM Directive, the AIFM Act refers to Regulation (EC) 24/2009 which itself defines the term "securitisation" as "*a transaction or scheme whereby an asset or pool of assets is transferred to an entity that is separate from the originator and is created for or serves the purpose of the securitisation and/or the credit risk of an asset or pool of assets, or part thereof, is transferred to the investors in the securities, securitisation fund units, other debt instruments and/or financial derivatives issued by an entity that is separate from the originator (i.e. transferor of assets to the securitisation structure) and is created for or serves the purpose of the securitisation, and:*

(a) in case of transfer of credit risk, the transfer is achieved by:

- *the economic transfer of assets being securitised to an entity separate from the originator created for or serving the purpose of the securitisation. This is accomplished by the transfer of ownership of the securitised assets from the originator or through sub-participation, or*

- *the use of credit derivatives, guarantees or any similar mechanism; and*

(b) where such securities, securitisation fund units, debt instruments and/or financial derivatives are issued, they do not represent the originator's payment obligations."

Therefore, each securitisation vehicle must assess its activities in light of the above definition to establish whether it falls within the scope of the AIFM Act.

For interpretation purposes, the CSSF refers to the clarifications provided by (i) the European Central Bank in its "Guidance note on the definitions of financial vehicle corporation and securitisation under regulation ECB/2008/30", (ii) the European Single Market Agency ("ESMA") Guidelines on key concepts of the AIFMD of 13 August 2013,and (iii) the FAQ of the European Commission of 25 March 2013 on the AIFM Directive.

In a nutshell, according to the CSSF (i) the securitisation vehicles originating new loans themselves as well as those issuing structured products which principal purpose is to offer synthetic exposure to non-credit related assets should be considered as alternative investment funds ("AIFs"), whereas (ii) the securitisation vehicles that issue only debt instruments or collateralised loan obligations, as well as those which are not managed in accordance with an investment policy within the meaning of the AIFM Act do not qualify as AIFs, whether or not they fall within the definition of securitisation special purpose entities pursuant to the AIFM Act.

Consequently, a majority of the Luxembourg securitisation vehicles are excluded from the scope of the AIFM Act.

Impact of EMIR on securitisation vehicles

The Regulation (EU) No 648/2012 of the European Parliament and of the Council of 4 July 2012 on over the counter derivatives, central counterparties and trade repositories, also known as the European Market Infrastructure Regulation ("**EMIR**") entered into force on 16 August 2012 and is directly applicable in Luxembourg.

EMIR applies to financial counterparties (such as banks, investment firms, collective investment undertakings with their management companies, pension funds and insurance undertakings) but also to non-financial counterparties. The latter are very broadly defined and, considering this definition, the CSSF has confirmed in its press release No. 13/26 dated 24 June 2013 that securitisation vehicles are also covered and may thus be subject to EMIR obligations.

As non-financial counterparties under EMIR, securitisation vehicles have reporting and risk mitigation procedures obligations to comply with irrespective of the amount of the transaction. To this end, every counterparty has to choose a licensed trade repository to start reporting (reporting obligations are applicable since 12 February 2014). By contrast, clearing obligations are only triggered if the non-financial counterparty whose positions in OTC derivatives exceed a certain threshold depending on the type of derivative involved (either EUR 1 billion or EUR 3 billion). Wider obligations of risk mitigation such as daily valuation and margining should also be met for positions exceeding the said thresholds.

3. Assets and risks

Nature of the securitised classes of risks

The risks to be assumed relate to the holding of assets, whether movable or immovable, tangible or intangible, as well as those resulting from commitments assumed by third parties or that are inherent to all or a portion of the activities of a third party, such as the risks associated with a business.

The Securitisation Act does not limit the types of assets that may be securitised. Luxembourg securitisation transactions most often cover loans, securities and financial institution receivables. Although the definition of the term "assets" contained in the Securitisation Act is very broad, the securitisation of certain types of assets (e.g. commodities and real estate assets) needs proper structuring.

The acquisition and transfer of assets and risks

A securitisation vehicle is in principle not subject to any restriction with respect to the acquisition and assumption of third-party risks. It may for instance invest in existing loans transferred to it from a primary lender or acquire a stake in a loan extended by a primary lender. Nevertheless, it may not directly structure or negotiate loans which is a regulated activity reserved for credit institutions and professional lenders.

In addition, a securitisation vehicle may not take an active management role in a business.

A securitisation vehicle may assume risks, directly or indirectly, and transfer such risks to third parties.

It is possible to structure a securitisation transaction as a simple structure or a dual structure. In a simple structure, one securitisation vehicle acquires the assets or risks and issues the securities. In a dual structure, two or more vehicles are formed. One or more acquisition vehicles purchase the assets or risks, funded by loans from another vehicle which issues the securities. The return on or value of the securities is linked to the loan extended to the acquisition vehicles.

The acquisition or transfer of the existing or future risks becomes effective and enforceable against third parties as from the date of execution of the assignment agreement, unless the parties have agreed otherwise.

An assignment or transfer of risks implies a transfer of any related guarantees and/or security interests.

Nature of operations

The acquisition of assets is usually made by using a "true sale" method, implying that the securitisation vehicle becomes legal owner of securitised assets or claims and of the benefits of the rights attached to these assets or claims.

The securitisation may also be done by way of synthetic method. However, contrary to a true sale, the synthetic securitisation method does not imply any transfer of ownership of the assets or claims and only risks are transferred.

Both methods (true sale and synthetic securitisation) allow the acquisition of the same volume of credit risks.

In specific circumstances, certain types of operations where a securitisation vehicle grants loans or offers credits instead of acquiring them on the secondary market, may also be considered as securitisation operations. Specific conditions have to be satisfied for the purpose of carrying out this type of securitisation operations. The documentation relating to the issuance shall describe in full the relevant borrowers and/or the criteria to determine which borrowers will be chosen, so that investors are in a position allowing them to assess risks attached to their respective investment. The CSSF assesses compliance with these conditions on a case-by-case basis.

Validity

Transfers from a Luxembourg originator to or by a securitisation vehicle in a securitisation transaction are enforceable against all third parties (including the debtor) with no further formalities, registrations or costs required, once the securitisation vehicle has reached an agreement with the originator.

The debtor does not need to be notified of such assignment, except in rare cases where the original contract contains an anti-assignment clause and the receivable relates to a non-monetary claim of which the assignee must have been aware (provided the debtor has not waived application of this clause).

Applicable law

The Securitisation Act clarifies that the effectiveness of an assignment against third parties (including the priority of competing creditors) is determined by the law of the originator's (assignor's) permanent residence. This rule is very modern compared to most other European countries, as it largely anticipates, the implementation of the 2001 Vienna Convention on the Assignment of Receivables in International Trade. However, this rule currently applies only in the context of securitisation transactions and does not affect the application of the law of the debtor's place of residence, which is normally applied by the Luxembourg courts outside the context of securitisations.

4. Financing of underlying assets or risks

The Securitisation Act requires that the securitisation vehicle be financed by the issuance of securities (*valeurs mobilières*). Such securities may bear the form of, *inter alia,* bonds, notes, shares, warrants, units and tracking shares.

In practice, securities which are recognised as "securities" under applicable law or which constitute securities within the meaning of MiFID are deemed securities under the Securitisation Act.

The value or yield of the securities issued by the securitisation vehicle must reflect the underlying risks assumed in the securitisation and there must be an effective link between the value or yield of the securities and the underlying risks.

Although the originator of the assets may invest in the securitisation structure, a substantial part of the securities issued by the securitisation vehicle must always be subscribed by third party investors.

The financing via borrowing is allowed on an ancillary basis only.

5. Protection of investors' and creditors' rights

The Securitisation Act allows the assets and liabilities of the securitisation vehicle to be segregated into different compartments. Each compartment constitutes a separate pool of assets and liabilities. This means that the rights of investors and creditors are restricted to the assets of a specific compartment, and that they only have recourse to the asset pool of the compartment in which they have invested.

Each compartment may be liquidated separately without any adverse effects on the securitisation vehicle's remaining compartments. The liquidation of a compartment does not trigger the liquidation of the securitisation vehicle as a whole or of its other compartments.

The Securitisation Act provides a high level of protection against bankruptcy of the parties to a securitisation transaction.

The following forms of protection are in particular relevant:

- Assets are protected from the insolvency of the securitisation vehicle, the originator and the relevant service providers. The securitisation vehicle must be bankruptcy remote in order to ensure the proper functioning of the market.

- In the event of the originator's bankruptcy, the transfer-of-title rules render it difficult for the trustees in bankruptcy to recover assets previously sold to the securitisation vehicle. Thus, any transfer of title to the securitisation vehicle remains legally valid. In the event of the servicer's bankruptcy, the securitisation vehicle has the right to receive full payment before the liquidation proceedings begin.

The Securitisation Act provides that the relevant provisions of the Companies Act relating to bondholders' representation shall also apply to the holders of securities issued in a securitisation transaction. To provide flexibility, it is however possible to set up a specific regime of representation which may differ from the legal representation mechanism laid down in the Companies Act.

For regulated securitisation vehicles, the CSSF considers however that the relevant bondholders' representation provisions contained in the Companies Act may only be excluded if another bondholder representation mechanism is established.

In both cases, the chosen bondholder representation/decision making procedure must be fully described in the issue documents.

6. Contractual provisions recognised by law

The Securitisation Act expressly states that the following contractual provisions are valid and enforceable:

Non-petition clause

Such clause protects the securitisation vehicle against insolvency actions initiated by investors. The investors contractually waive their right to bring such proceedings against the securitisation vehicle. An insolvency suit filed by such a contracting party will therefore be automatically rejected by the Luxembourg courts.

Limited-recourse clause

By using limited-recourse clauses, investors or creditors waive their right to seek enforcement against any assets other than those specified in the contract.

Subordination clause

Such clause subordinates the payment rights of investors and/or creditors to the rights of others.

7. Tax treatment of securitisation vehicles

General remarks

The effectiveness of a securitisation transaction largely depends on the tax treatment of the vehicle since all taxes due by the vehicle effectively reduce the return available for investors. Hence, the Securitisation Act seeks to maximize tax neutrality.

Corporate tax

Securitisation companies are in principle fully subject to Luxembourg corporate tax at a combined (standard) rate of 29.22%[1] (for the City of Luxembourg). All income derived from the securitised assets or risks is included in the securitisation company's tax base. However, the Securitisation Act provides that a securitisation company may deduct for tax purposes all obligations assumed vis-à-vis investors and creditors (e.g. interest, dividends, etc.). Therefore, the securitisation company's tax base may be virtually close to nil. Furthermore, due to the deductibility under the Securitisation Act of the obligations assumed vis-à-vis investors (be it under debt or equity securities), securitisation companies have more flexibility than normal companies in combining equity and debt instruments.

Securitisation funds

Securitisation funds are subject to the same tax treatment as collective investment funds (*fonds communs de placement*), with the exception of a subscription tax (*taxe d'abonnement*) which is not due.

Securitisation funds are considered transparent for Luxembourg tax purposes and, therefore, are not subject to corporate tax.

Net worth tax

Securitisation vehicles are explicitly exempt from the annual net worth tax of 0.5%.

Dividend withholding tax

Under domestic law, dividend distributions made by a company that is subject to tax in Luxembourg are subject to a 15% withholding tax. Distributions and other proceeds allocated to its investors by a securitisation vehicle governed by the Securitisation Act, however, are characterised as interest payments from a national tax point of view and therefore are not subject to withholding tax.

1 Luxembourg corporate income tax is currently levied at an effective rate of 29.22% for companies established in Luxembourg city. Corporate income tax is a combination of national corporate income tax ("Impôt sur le Revenu des Collectivités"- currently levied at a rate of 21% increased to 22.47% by a 7% surcharge in respect of the unemployment fund) and municipal business tax ("Impôt Commercial Communal " - currently 6.75% for Luxembourg city). Companies with annual profit of less than EUR 15,000 are subject to Luxembourg corporate tax at effective rate of 28.15%.

Value Added Tax (VAT)

Management services provided to securitisation vehicles governed by the Securitisation Act are exempt from VAT.

Registration taxes

A fixed registration tax of EUR 75 will be payable for the incorporation and for the subsequent modification of the articles of a securitisation company. The fixed registration tax of EUR 75 is also due for the establishment of a securitisation fund run by a management company although that tax will be levied upon incorporation or modification of the articles of incorporation of the management company. Special rules apply to the contributions of real estate assets located in Luxembourg.

Contracts concluded in connection with securitisation transactions governed by the Securitisation Act are exempt from registration duties, with the exception of certain specific instruments (related to Luxembourg real estate, aircraft or vessels). Outside these exceptions, contracts may also be registered voluntarily in which case a negligible fixed registration tax will be due.

Luxembourg does not levy a stamp duty on the issuance or transfer of securities.

Luxembourg tax at the level of investors

Capital gains realised by a Luxembourg parent company or a Luxembourg permanent establishment of a foreign company, on shares held in a securitisation vehicle governed by the Securitisation Act are excluded from the scope of the participation exemption normally available for gains realised on qualifying shareholdings.

Distributions made by a securitisation company should by extension also not be eligible for the participation exemption at the level of the recipient if the latter is a regular Luxembourg-resident company or a Luxembourg permanent establishment of a foreign company.

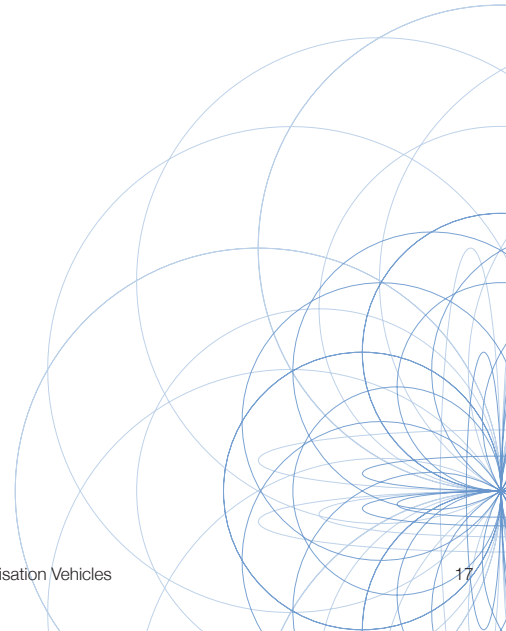
Non-resident investors in a securitisation vehicle which do not have a permanent establishment in Luxembourg to which the securities issued by the securitisation vehicle can be attributed should not be subject to Luxembourg tax on the income realised on their debt or equity securities.

International aspects

The tax efficiency of a securitisation transaction will to a large extent depend on local tax consequences, i.e. in the country where the securitisation vehicle's income is sourced.

Such tax treatment will depend on the national law of the countries concerned and their interpretation of their tax treaties with Luxembourg as well as EU law.

The Luxembourg authorities have taken the stance that a securitisation company governed by the Securitisation Act should be eligible for treaty benefits with respect to income received from treaty countries or EU member states since such a company is taxed as a regular company under Luxembourg law and is thus a Luxembourg resident for treaty purposes. This position, however, will have to be confirmed along the way, especially with regard to the anti-abuse legislation which may be applied in certain countries (where the securitisation company's income is sourced).



Contact

We hope you found this publication useful and welcome the opportunity to answer any questions you may have with respect to its contents.

For legal/regulatory matters, please contact:

Josée Weydert
Banking & Finance Partner
T. + 352 / 26 12 29 97
E. josee.weydert@nautadutilh.com

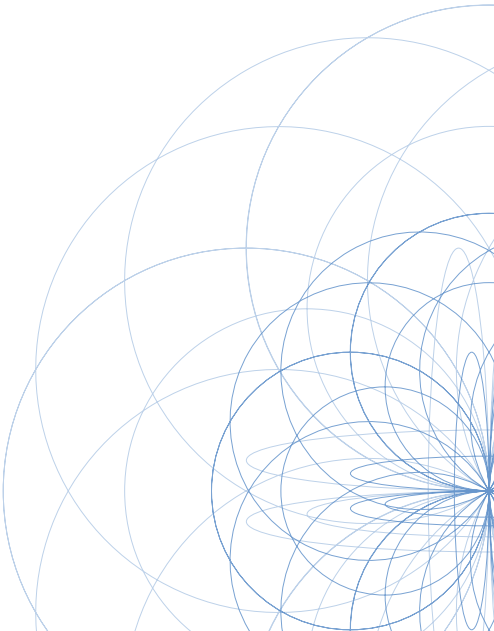
Jad Nader
Banking & Finance Counsel
T. + 352 / 26 12 29 63
E. jad.nader@nautadutilh.com

For tax matters, please contact:

Jean-Marc Groelly
Tax Partner
T. + 352 / 26 12 29 95
E. jean-marc.groelly@nautadutilh.com

Christophe Joosen
Tax Partner
T. + 352 / 26 12 29 45
E. christophe.joosen@nautadutilh.com

www.nautadutilh.com



Challenge the obvious