AMENDMENTS TO THE LUXEMBOURG SECURITISATION LAW

Over the past years, the Luxembourg law dated 22 March 2004 on securitisation (the "**Securitisation Law**") has proven a successful framework for a wide variety of securitisation, repackaging and financing transactions.

On 9 February 2022, Luxembourg adopted a long-awaited law updating the Securitisation Law and clarifying certain questions in the interest of legal certainty. The changes will enter into force in the coming weeks. In this briefing, we set out an overview of the changes and their market impact.

As a preliminary note, it is worth remembering that the Securitisation Law and the EU Securitisation Regulation constitute two completely distinct legal regimes and it is perfectly possible for a transaction to come within the ambit of one, the other, neither or both. The Securitisation Law is an "opt-in" regime whereas the EU Securitisation Regulation applies mandatorily where the transaction meets the definition of a "securitisation", meaning that a vehicle which elects to be subject to the Securitisation Law may or may not be a securitisation special purpose entity for EU Securitisation Regulation purposes.

Key aspects

- Key aspects of the Securitisation Law will be modernised and **legal certainty** increased.
- The **available means of funding** will be broadened beyond the current requirement to raise financing via the issuance of securities.
- The **active management of debt portfolios** is now permitted, which will enhance the attractivity of the Securitisation Law for CLO-type structures.
- **Partnerships** can be used as securitisation vehicles.

The innovations that will be introduced can be grouped into 3 categories:

- Increased flexibility on the financing side
- Rules regulating the assets held by a securitisation vehicle
- Corporate governance rules

We examine each in turn below.

1. INCREASED FLEXIBILITY ON THE FINANCING SIDE

a. Types of funding

The Securitisation Law currently requires a securitisation vehicle to issue securities, the value or return of which depends on the securitised assets. This requirement has led to lengthy discussions as to what constitutes a "security" for these purposes, particularly in situations where the financing instruments issued were governed by foreign laws and it failed to include more complex or novel forms of financial instruments. It also led to significant complexity and

uncertainty around the use of loan funding for leverage or liquidity management purposes or during any warehousing phase.

Going forward, a securitisation vehicle may not only fund itself via any form of financial instruments (as opposed to the narrower concept of securities), but also via loans. In each case the value of or return on the relevant financial instruments or loans must depend on the underlying assets. This can easily be achieved by, e.g., making the loan limited recourse to the securitised assets or ensuring that its value or return otherwise tracks that of the underlying assets. This change is welcome as it simplifies the discussion around the characterisation of the funding instruments which can be used and allows securitisation vehicles to be funded via loans such as asset-backed or profit participating loans.

b. Issuance to the public

Any securitisation vehicle issuing securities on a continuous basis to the public needs to be licensed by the CSSF. The Securitisation Law does not define the concept of "on a continuous basis to the public", although the concept has been clarified by the CSSF in its *Frequently Asked Questions*.

The Securitisation Law will now include a statutory definition of this concept, thus increasing the legal certainty in this important area. The main rule will remain unchanged and any vehicle that issues financial instruments to the public more than 3 times per financial year will need to be regulated. The law will however now clarify that an issuance will not be seen as being made to the public if it falls within any of the following categories:

i. The issuance is solely made to professional clients as defined in MiFID II, as implemented in the financial sector law.

ii. The denomination of the financial instruments offered is equal to or exceeds EUR 100,000.

iii. The financial instruments are distributed by way of a private placement.

These conditions are broadly based on the guidance provided by the CSSF except that the minimum wholesale denomination is lowered from EUR 125,000 to EUR 100,000. This is a welcome alignment between the Securitisation Law and the EU Prospectus Regulation (though there is a slight difference in approach, as in EU Prospectus Regulation terms the equivalent concept would be an exempt offer to the public rather than the issuance not being considered an offer to the public). As is currently the case, the assessment of the number of issuances is made across the vehicle as a whole (and not on a compartment-by-compartment basis).

2. RULES IMPACTING THE SECURITISED ASSETS

a. Active management

The Securitisation Law is currently silent on the question of whether a securitisation vehicle can actively manage its assets (or appoint a third party to do so on its behalf).

One of the major innovations is a provision according to which a securitisation vehicle may solely securitise a debt portfolio that is actively managed if the

financial instruments issued for the purposes of such securitisation are not offered to the public.

This provision removes any doubt that the active management of a debt portfolio is possible unless the relevant securitisation is offered to the public. With this clarification, Luxembourg looks set to offer an efficient legal framework for actively managed collateralised loan obligations (CLOs), putting Luxembourg on the map of managers of CLOs.

b. Acquisition of real assets

The law will now also provide that a securitisation vehicle may acquire directly or indirectly the assets which it securitises. Besides allowing the securitisation vehicle to directly own the assets generating the cash flows that are securitised (such as the assets subject to a lease if the lease receivables are securitised), this provision also confirms that a securitisation vehicle can acquire the assets or risks to be securitised indirectly, either through a fully owned subsidiary or via the acquisition of an entity holding these assets or risks. It will need to be seen how far this change will impact the current position taken by the regulator that securitisation vehicles should, in principle, not own non-financial assets.

c. Granting of security

The Securitisation Law currently provides that a securitisation vehicle may only grant security over its assets (i) for the purpose of securing its own obligations in connection with the securitisation of those assets, or (ii) in favour of its investors. Any security for the obligations of a third party may be null and void. This very prescriptive and unduly restrictive rule will now be changed, and securitisation vehicles will be allowed to give security for obligations relating to the securitisation transaction. Thus it will no longer be excluded that a securitisation vehicle could give security for the obligations of third parties. This will, for example, allow a securitisation vehicle that acquires a junior loan to provide security over that loan in favour of the senior lenders, as is occasionally required. Until now, this has been a barrier to securitisation vehicles acquiring such loans. Similarly, where the securitisation vehicle holds assets via one or more wholly owned subsidiaries, it will now be possible to have the securitisation vehicle grant security, or give guarantees, for the indebtedness of its subsidiaries. Furthermore, the previous sanction that any security granted in violation of this rule is null and void will now be removed.

3. CORPORATE GOVERNANCE RULES

a. New corporate forms available

Under the Securitisation Law, securitisation vehicles are either established as a securitisation fund or as a company. In the latter case, only *société anonyme*, *société en commandite par action* or *société à responsabilité limitée* are currently permitted.

It will now also be allowed to use tax transparent partnerships such as a *société en commandite simple* or a *société en commandite spéciale*.

Partnerships subject to the Securitisation Law will need to prepare and publish annual accounts on the basis of the provisions of the law of 2002 on the register of commerce and on financial statements and will not benefit from exemptions in that respect.

b. RCS registration of securitisation funds

Closing an important gap, the Securitisation Law now caters for the registration of securitisation funds with the Luxembourg register of commerce and companies.

c. Annual accounts and distributions

Where a compartment is financed by way of equity, the financial accounts relating to such compartment will be approved by the shareholders of the relevant compartment only. Similarly, in such case the determination of the distributable assets and reserves, as well as of the legal reserve, will be made on a compartment-by-compartment basis.

d. Ranking of securities

The Securitisation Law will also provide for a framework governing the ranking of different classes of funding and in particular confirm that, unless otherwise agreed, any form of debt ranks senior to shares, units and beneficiary units and fixed income debt ranks senior to profit participating debt.

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