

Application of ATAD rules to securitization vehicles

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The Luxembourg law implementing the European Union (EU) Anti-Tax Avoidance Directive (ATAD) introduced certain tax provisions, among which a limitation to interest deductibility and rules countering hybrid mismatches within the EU, that apply for the first time with respect to financial years starting on or after 1 January 2019. These rules have been completed by a further law transposing ATAD 2, with effect from financial years starting on or after 1 January 2020, which extends the territorial scope of the anti-hybrid mismatch provision to third countries.

These new rules raise numerous questions in relation to the deductibility of payments that are typically due by debt-financed securitization companies. The ATAD and Securitization working group of the Luxembourg Capital Markets Association (LuxCMA)¹ has therefore reflected on the various issues that such securitization companies may be confronted with and has summarized its technical analysis in the LuxCMA "Technical Position Paper on Deductibility of Payments by Securitization Companies Financed by Debt" that was released on 26 October 2020. The paper is available for members only through the LuxCMA website.

What does it mean for you?

The paper focuses specifically on the treatment of payments under the interest limitation rule and the anti-hybrid mismatch rules. More specifically, next to commentaries on the general definition of the concept of interest and the principle of symmetry, the paper analyzes in more detail how income realized from specific investments, such as distressed/non-performing debt, payments in the context of most commonly used types of swaps and payments under specific types of bonds issued by securitization companies, are to be treated for the purposes of the interest limitation rules.

Especially for debt acquired by securitization companies at a significant discount reflecting the fact that the debtor is in financial distress, particular attention must be paid, at inception, to build a strong economic valuation model, as such model will constitute the basis for assessing revenue recognition and thus application of the interest limitation rules.

In addition, the paper explains the concept of structured arrangements, which is relevant for the purposes of applying the anti-hybrid rules and examines its application to payments made by securitization companies under notes they have issued.

Outlook

Lacking detailed guidance issued so far by the Luxembourg tax authorities on the application of the various provisions, the aim of the LuxCMA paper is to offer positions that are considered by the working group as reasonable and defensible, based on the law as in effect on the date of this paper.

How EY can help?

EY has actively participated in the ATAD and Securitization working group of the LuxCMA. Please do not hesitate to contact our EY professionals who can help you to further understand and assist you in assessing the impact of the aforementioned rules on your securitization vehicles or trades involving securitization vehicles and to provide advice on how to best adapt to the new rules.

¹The ATAD and securitization working group is composed of Luxembourg tax law professionals and experts in securitization transactions, including representatives from EY, and represents a large number of relevant advisers in the Luxembourg securitization sector.

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EY Contacts

TAX ADVISORY SERVICES



Bart Van Droogenbroek
Partner, Tax Leader, EY Luxembourg
Tel: +352 42 124 7456
Bart.Van.Droogenbroek@lu.ey.com



Dietmar Klos
Partner, Real Estate Leader, EY Luxembourg
Tel: +352 42 124 7282
Dietmar.Klos@lu.ey.com



Vincent Rémy
Partner, Tax, EY Luxembourg
Tel: +352 42 124 7611
Vincent.Remy@lu.ey.com



Christophe Joosen
Partner, Tax, EY Luxembourg
Tel: +352 42 124 7222
Christophe.Joosen@lu.ey.com

SECURITIZATION ASSURANCE TEAM



Papa Saliou Diop
Associate Partner, Assurance, EY Luxembourg
Tel: +352 42 124 8539
PapaSaliou.Diop@lu.ey.com



Oliver Cloess
Associate Partner, Assurance, EY Luxembourg
Tel: +352 42 124 8696
Oliver.Cloess@lu.ey.com