

Secure Securitisations in Malta

Securitisation transactions in Malta, that is the raising of capital through the transfer of assets and risk from the transferee (“Originator”) to special purpose vehicles (“SPVs”) and converting the same into financial instruments issued by the latter, are regulated by the Securitisation Act (Chapter 484 of the Laws of Malta) (“Act”).

The Act represents a truly comprehensive framework for the regulation of securitisations. The robust yet flexible legal architecture provided by the Act, together with the neutral tax treatment of these transactions, make Malta a jurisdiction of choice for the structuring of securitisations.

Types of Securitisation Transactions

Under Maltese law, a securitisation transaction may take one of three principal forms:

- (i) **Asset securitisation**, where the Originator transfers and the SPV acquires securitisation assets which may be any asset, whether existing or future, whether movable or immovable, and whether tangible or intangible. The types of assets which may be securitised are quite broad including rental income and home loans;
- (ii) **Synthetic securitisation**, which does not involve a transfer of receivables by the Originator to the SPV but the involves the assumption by the latter of the risks of the assets of the Originator through the use of credit derivatives or similar securities such as CDOs; and
- (iii) **Loan securitisation**, whereby the SPV grants a secured loan or other secured facility or facilities to the Originator.

Regulatory Treatment and Formal Requirements

Securitisation transactions are not regulated as such but are subject to certain legal requirements in order to be treated as securitisation vehicles. Essentially, the vehicle's constitutive documents must include specific provisions that the vehicle is subject to the provisions of the Securitisations Act and that proper notice is provided to the Malta Financial Services Authority (“MFSA”) on the appropriate form whenever the vehicle intends to enter into one or more securitisation transactions. It is however important to emphasise that the securitisation vehicle must still comply with the relevant legal provisions relating to offers of securities to the public, where applicable.

Legal Form of SPV

A securitisation vehicle may be established as:

- (a) a company, including an INVCO or SICAV;
- (b) a commercial partnership;
- (c) a trust created by a written instrument; or
- (d) any other legal structure approved by the MFSA for a securitisation transaction.

It is to be noted that the Civil Code also provides for the use of foundations in securitisation transactions.

The vehicle may be established under the laws of Malta or the laws of any other EU or EEA State or any other jurisdiction which is signatory to a multilateral or bilateral memorandum of understanding with the MFSA¹.

Bankruptcy Remoteness

The concept of “bankruptcy remoteness” of the SPV is fundamental to any successful securitisation structure. It essentially refers to the safeguards taken to insulate the SPV from the possibility of becoming insolvent due to the external and ancillary factors to the securitization transaction itself.

The Act itself provides for the methods in which the SPV is to achieve its bankruptcy remoteness:

1. Separation from the Originator

Although the Originator and the SPV are separate legal persons, the Act creates further safeguards to ensure that the SPV is insulated from the potential insolvency of the Originator. To this end it provides that no proceedings taken against the Originator under any law, including any dissolution and winding-up proceedings will have any effect on:

- (a) the SPV;
- (b) any securitisation assets acquired or risks assumed by the SPV, as well as any cashflow or other asset of the SPV;
- (c) any payments due by the underlying debtors in connection with the securitised assets.

2. Limited Powers

In order to prevent the SPVs from incurring liabilities which are not related to the securitisation transaction, the Act provides that SPVs may not carry out any other trade or business, unless it is ancillary to the securitisation transaction. Furthermore, SPV's objects must be specifically limited to such matters that are necessary to carry out the transactions intended or required to implement or participate in a securitisation transaction and all related and ancillary acts, including the acquisition, management and collection of credits and other receivables or other securitisation assets, the assumption of risks, the granting of secured loans, the issue of financial instruments or the borrowing of funds to finance the acquisition of assets or the assumption of risks, the engagement of service providers to administer or support its activities and the entering into derivative instruments.

¹ For a full list of Memoranda of Understanding (MOU) signed by the MFSA please refer to the following link:
<http://www.mfsa.com.mt/pages/viewcontent.aspx?id=22>

True Sale

A successful Securitisation Transaction would require the complete and final transfer of ownership of the securitisation assets from the Originator to the SPV. It is only in this way that assets are insulated from the potential insolvency of the Originator and thus the uninterrupted flow of cash to the SPV generated by the assets so transferred. Furthermore this has the additional benefit to the Originator who removes the assets transferred from its balance sheet and thus, if subject to capital adequacy rules, will free up capital.

In terms of Maltese law, the Originator and the SPV are at liberty to select any method of transferring the securitisation assets, including, without limitation, by novation, sale, assignment and declaration of trust.

The Act provides that, notwithstanding any underlying contractual or statutory prohibition or restriction on the Originator to assign in whole or in part the securitisation asset to any third party, when a securitisation asset is assigned to an SPV, such assignment will be treated as final, absolute and binding on the Originator, the SPV and on all third parties, and such assignment will not be:

- (a) subject to annulment, rescission, revocation or termination, variation or abatement by any person and for any reason whatsoever;
- (b) subject to any rights of the creditors of the Originator for any reason whatsoever;
- (c) subject to any rights of a liquidator, provisional administrator, receiver, curator, controller, special controller of the Originator or other similar officer of the Originator for any reason whatsoever.

Furthermore, the Act also makes further provision to relax the requirements on assignment under the Civil Code. For example the underlying debtor of an asset transferred by the Originator to the SPV will not have a claim against the SPV in connection with any obligation relating to the securitisation asset so transferred. Thus, in the event of the transfer of a loan to the SPV, the underlying debtor (borrower) of the said loan continues to enjoy all rights against the Originator who will remain solely responsible for the performance of all obligations under the loan agreement. Furthermore, contrary to the situation under the Civil Code, the transfer of the loan would not require the notification which to be provided to the borrower to be by judicial act but could be by any means in writing.

Recharacterisation Risk

Intrinsically connected to the concept of 'true sale' is that of 'recharacterisation risk'. This refers to the risk that the transfer of the assets by the Originator to the SPV is recharacterised as a secured loan. Thus the ownership and risks thereto would not be deemed to have transferred from the Originator to the SPV and therefore would still be treated as still belonging to the Originator. As we have seen above, in order for a securitization transaction to be successful, it is cardinal that the securitization assets and their risk are separated from the Originator and transferred to the SPV. With this in mind the Act provides that the transfer of securitisation assets from an Originator to an SPV will be valid and enforceable in accordance with its terms and will not be subject to re-characterisation for any reason whatsoever.

Tax Treatment

Securitisation includes any transaction or arrangement whereby a securitisation vehicle (i) acquires securitisation assets from an Originator, (ii) assumes any risks from an Originator; or, (iii) grants secured loans or other secured facilities to an Originator, through the issuance of financial instruments.

Under current Maltese law tax rules, a securitisation vehicle may claim deductions in respect of the following:

- **Relevant Expenditure** in accordance with Maltese tax rules;
- **Acquisition price** – Amounts payable to the Originator for the acquisition of securitisation assets, or the assumption of risks;
- **Finance costs** – Premiums, interest or discounts relating to financial instruments issued, or funds borrowed, to finance the acquisition of securitisation assets or the assumption of risks;
- **Operating costs** – Expenditure incurred in respect of the day-to-day administration of the securitisation vehicle including legal and audit costs; and
- **Residual deduction** – Where, after taking into account the above deductions, the securitisation vehicle has remaining taxable income, it may **opt** to claim a further deduction of an amount equal to the remaining taxable income effectively reducing the taxable income to 0.

On the basis of these deductions, a securitisation vehicle, has no taxable income in Malta. Furthermore, it is relevant to point out that, whilst an amount equal to the deductions under the acquisition price and residual deduction categories would constitute deemed income for the Originator, no Malta tax is payable on such deemed income if the Originator or assignor is not tax resident in Malta.

Further Developments

Further to a Consultation Document on 'Proposals for Securitisation Cell Companies Regulations 2014 issued on the 4th of September 2014, the Malta Financial Services Authority ('MFSA') has recently published the final draft of the Securitisation Cell Companies Regulations, 2014 ('the SCC Regulations') which are set to become law before the end of the year. This new body of law is to be issued under the Companies Act (Chapter 386 of the Laws of Malta). The new regulations, continue to enhance Malta's offering as a jurisdiction of choice for the structuring of securitisations by adapting and extending the protected cell company structure to cater for securitisation activity.

The Regulations have been drawn up with the aim of setting out a framework for a new type of Cell Company acting as a special purpose vehicle in Malta - the Securitisation Cell Company (the 'SCC'). By uniting the highly sophisticated frameworks provided in the Securitisation Act with the protected cell company concept, the proposed Regulations will provide a legally entrenched framework for the segregation of different sets of assets and risk instruments within a single special purpose vehicle, the SCC, thus allowing for the launch of multiple asset-backed or insurance-linked securities without incurring any risk of cross-contamination between the different sets of creditors and investors.

Hence, the proposed framework for securitisation cell companies retains all the benefits introduced by the Securitisation Act while providing increased flexibility, enhanced investor protection and economies of scale.