

Securitisation, tax issues and anti-avoidance

February 2008

Tax Issues In Securitisation

Agenda

- What is Securitisation?
- Why do companies securitise?
- Overview of the main types of securitisation.
- Overview of key tax considerations.
- Impact of IFRS
- Managing the tax aspects of a securitisation transaction.

What is Securitisation?

- “Securitisation is the pooling of homogeneous, financial, cashflow producing, illiquid, unrated assets in a special purpose vehicle (“SPV”) and financing that pool of assets through the issue of marketable securities”

Why do companies securitise?

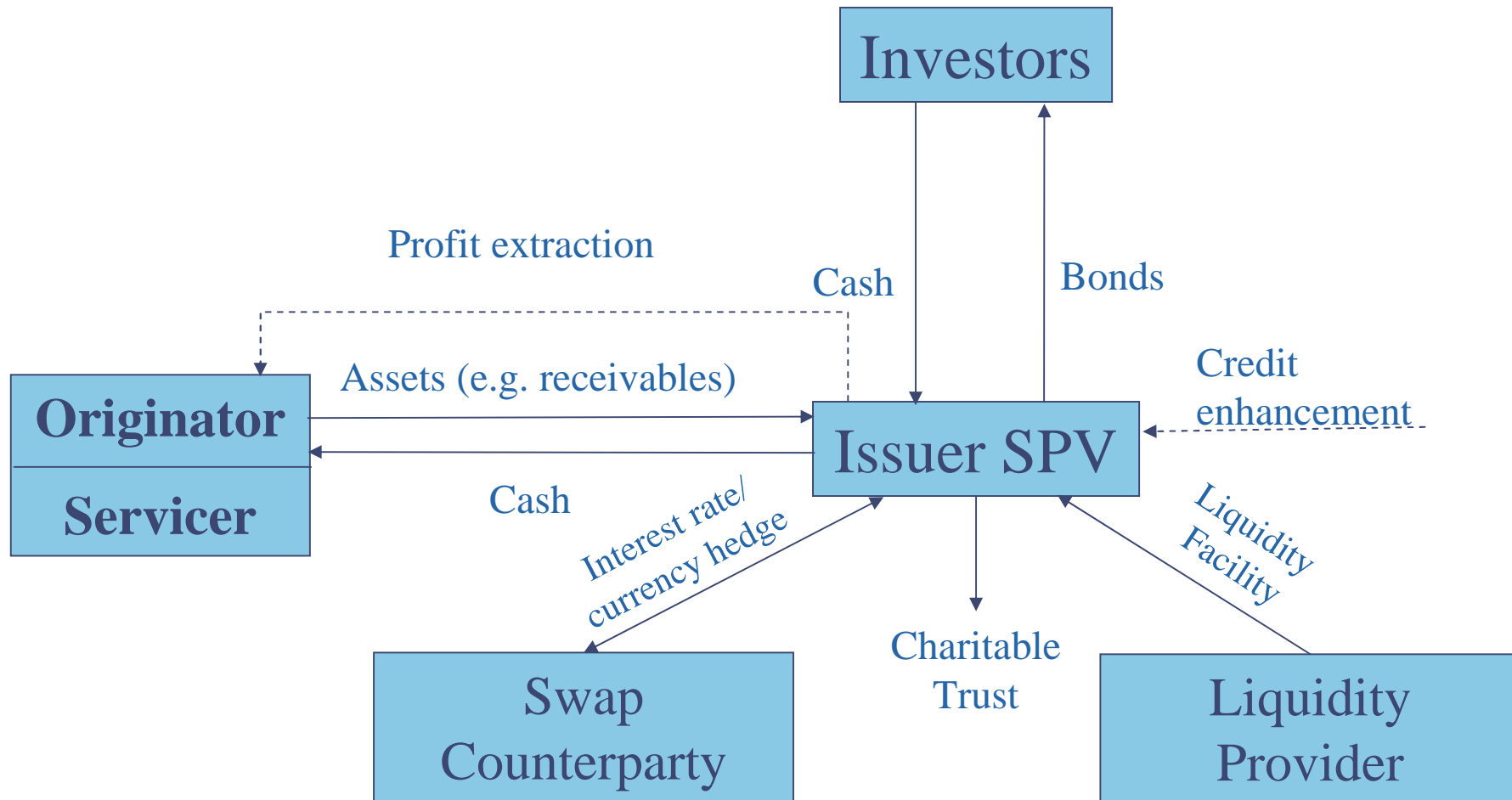
- Reduce funding costs.
- Diversify funding sources.
- Reduce regulatory capital requirements.
- Re-deployment of capital
- Portfolio and Risk management.

Basic Types of Securitisation

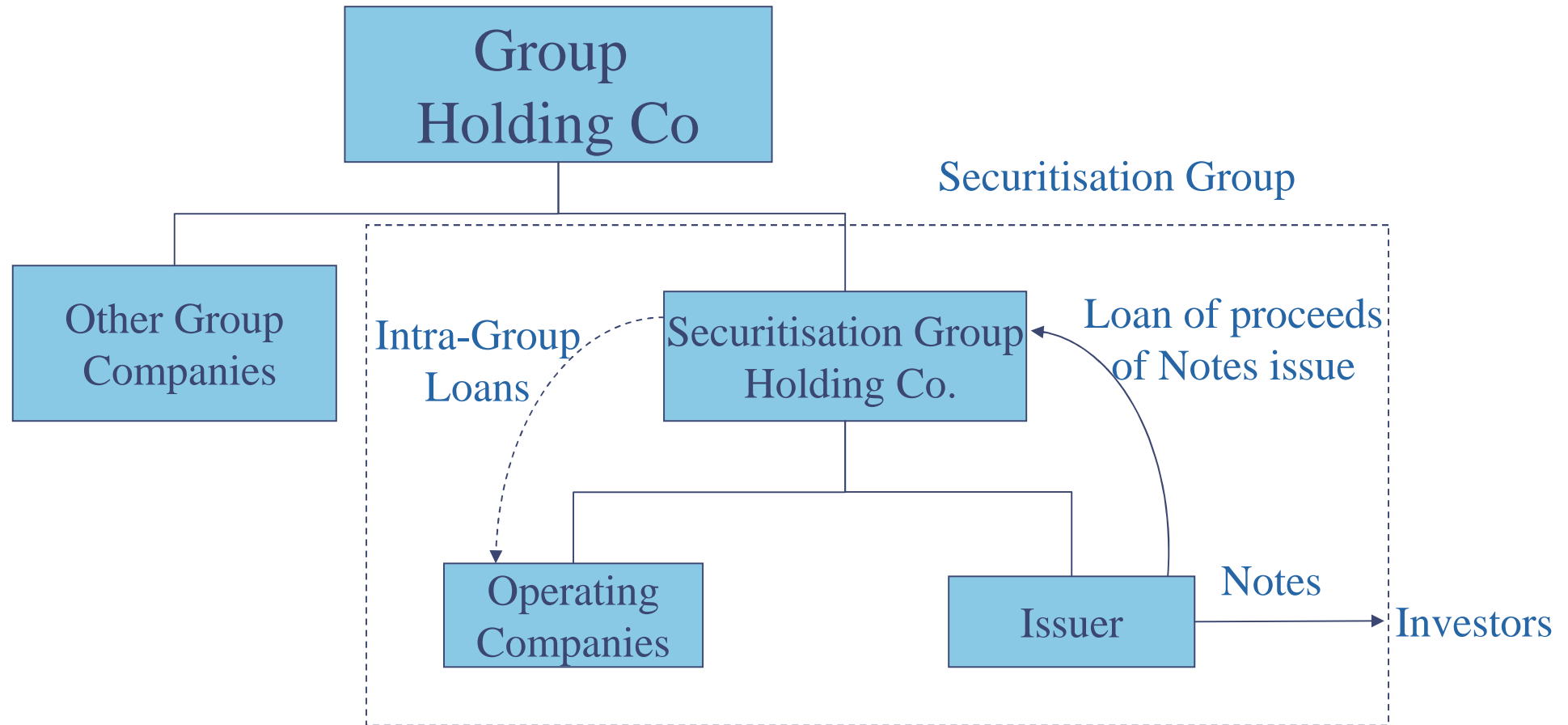
3 Basic Types:

- Asset sale securitisation.
- Whole business securitisation.
- Synthetic securitisation

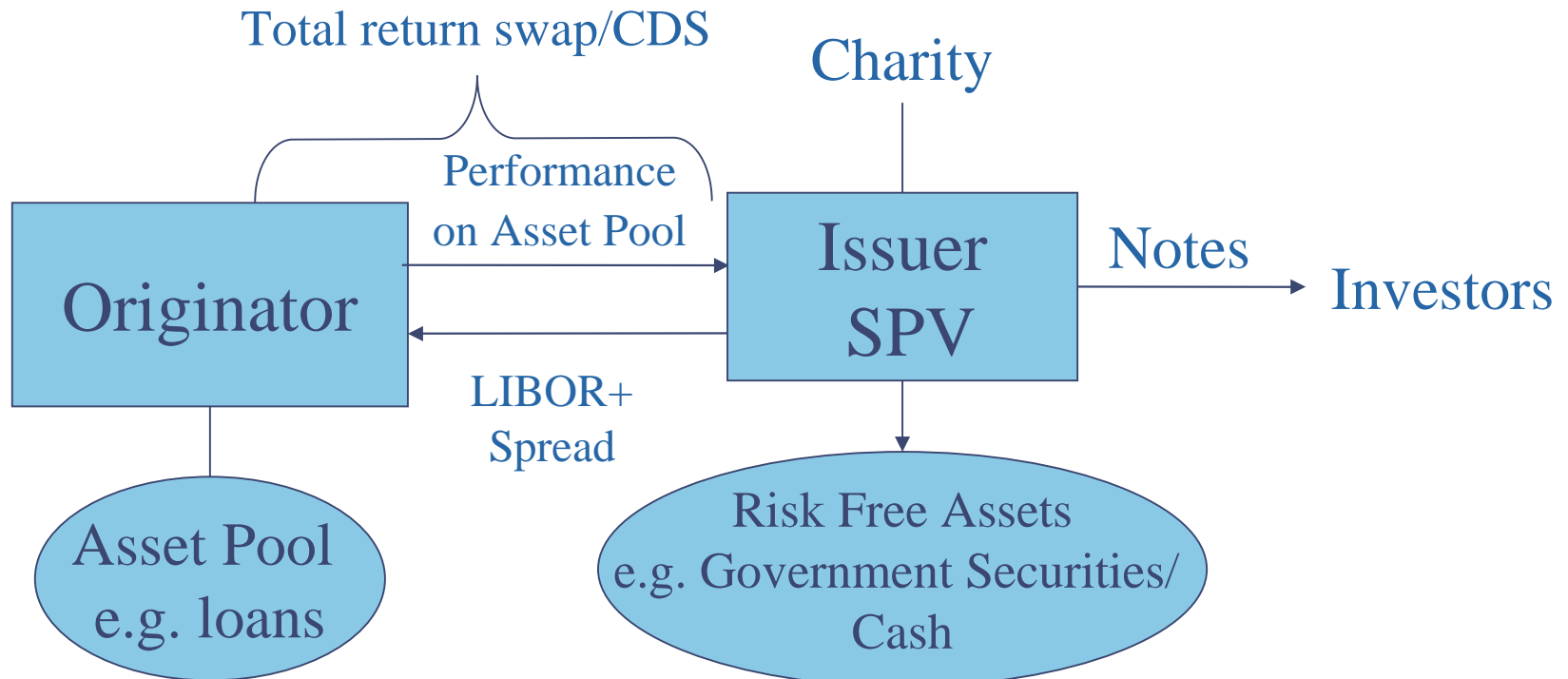
'Asset Sale' Securitisation – Basic Structure



'Whole Business' Securitisation – Basic Structure



'Synthetic' Securitisation – Basic Structure



- Originator hedged against changes in value and return from Asset Pool
- Originator obtains no funding from the transaction

Securitisation – Key Tax Objectives

- Tax neutrality: Securitisation transaction should not create any new tax liabilities.
- Timing of taxation: Securitisation transaction should not accelerate any tax liabilities.
- Certainty of tax treatment - No unexpected/unfunded tax liabilities.

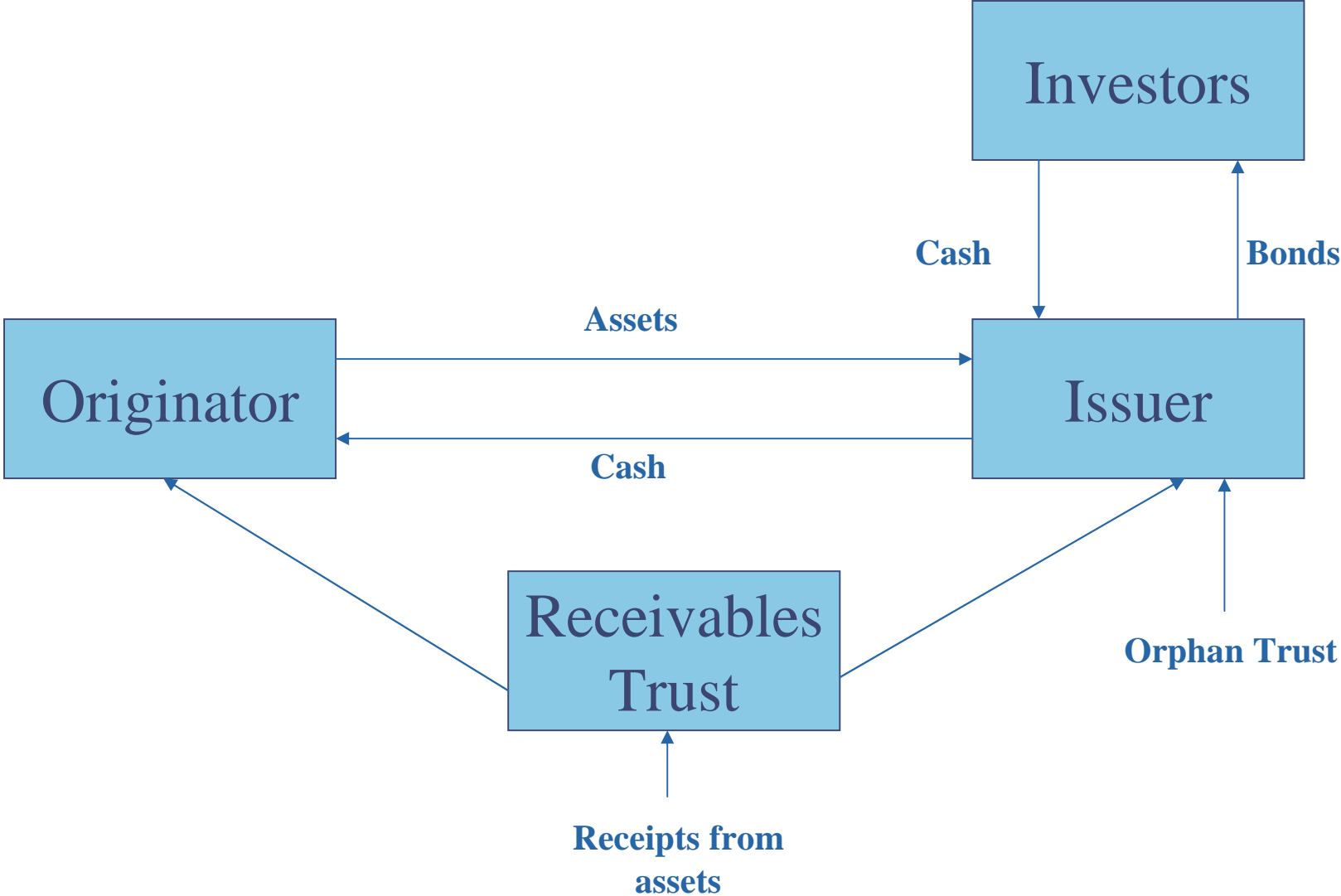
'Asset Sale' Securitisation – Taxation of originator

- Taxation of sale of receivables to SPV:
 - Consideration brought into account on sale (i.e. book value v market value)
 - Timing of recognition of profit arising on sale for tax purposes
 - Impact of other taxes (e.g. stamp duty, VAT).
- Taxation of credit enhancement mechanism (e.g. subordinated loans).
- Relief for bad debts
- Deductibility of transaction expenses.
- VAT implications of servicing arrangements.

‘Asset Sale’ Securitisation – Taxation of Issuer

- Objective: Tax symmetry
- Tax residence - onshore v offshore
- Taxation of income from underlying assets.
- Deductibility of interest payable on Notes and liquidity facility.
- Taxation of interest rate and currency hedges
- Impact of withholding taxes:
 - Income on underlying assets
 - Interest on notes issued.
- Deductibility of profit extraction mechanism
- Impact of anti-avoidance rules (e.g. distribution rules)
- Taxable presence / “PE” issues if non-resident Issuer

Receivables Trust



'Whole Business' Securitisation – Key Tax Considerations

- Deductibility of financing costs (i.e. on Notes and all intra-group loans)
- Impact of withholding taxes on all financing cash flows
- Level of tax 'shelter' within the Securitisation Group over term of securitisation (to be modelled based on expected profitability, etc.)
- Availability and mechanics for group loss relief between Securitisation Group companies and other group companies
- Impact of security arrangements (e.g. is the Securitisation Group 'de-grouped' from the main group as a result of the security charges?)
- Impact of 'latent' and/or 'secondary' tax liabilities

'Synthetic' Securitisation – Tax Considerations

- No disposal of underlying assets by originator.
 - No transfer duties
 - No potential direct tax timing difference
 - Withholding tax position on underlying assets preserved
- Need to ensure originator will obtain deductions for payments under total return swap/CDS
- No issues concerning profit extraction from SPV.
- No issues concerning servicing of Asset Pool.
- Similar Issuer taxation considerations although may be easier to locate Issuer offshore.

Impact of IFRS

- Will IFRS apply to securitisation SPVs?
 - Not mandatory for solus A/Cs although UK GAAP (FRED 30) likely to introduce similar concepts.
- Applies with effect from 1 January 2005.
- Impact of IAS 39:
 - Move away from conventional accruals concept to ‘fair value’ concept
 - Potential fair value treatment of derivative hedges could lead to unfunded tax liabilities.
 - Impact of move from accruals to “amortised cost” treatment of debt assets and liabilities
 - De-recognition treatment in originator and Issuer

Managing tax in a securitisation transaction

- Tax is a fundamental aspect of the transaction since it has a direct impact on cashflows and will drive the structuring.
- Rating agency requirements will mean a high level of tax certainty is required - Impact on tax opinions.
- WBS transactions require extensive tax work (i.e. tax due diligence, tax deed of covenant negotiation, tax shelter modelling, etc.).
- Tax needs to be considered early.
- Opportunities for tax planning?

Ownership of income for tax purposes

- Why is the issue so acute in the banking/financial sector?
 - Multiplicity/volume of cross-border cash flows
 - Value of cross-border cash flows
 - Prevalence of synthetic cash flows and industry-standard transactions giving rise to synthetic cash flows – stock loan; repo; swap; other hedging transactions
- Status of the issue for us

UK – Italy treaty

Article 10

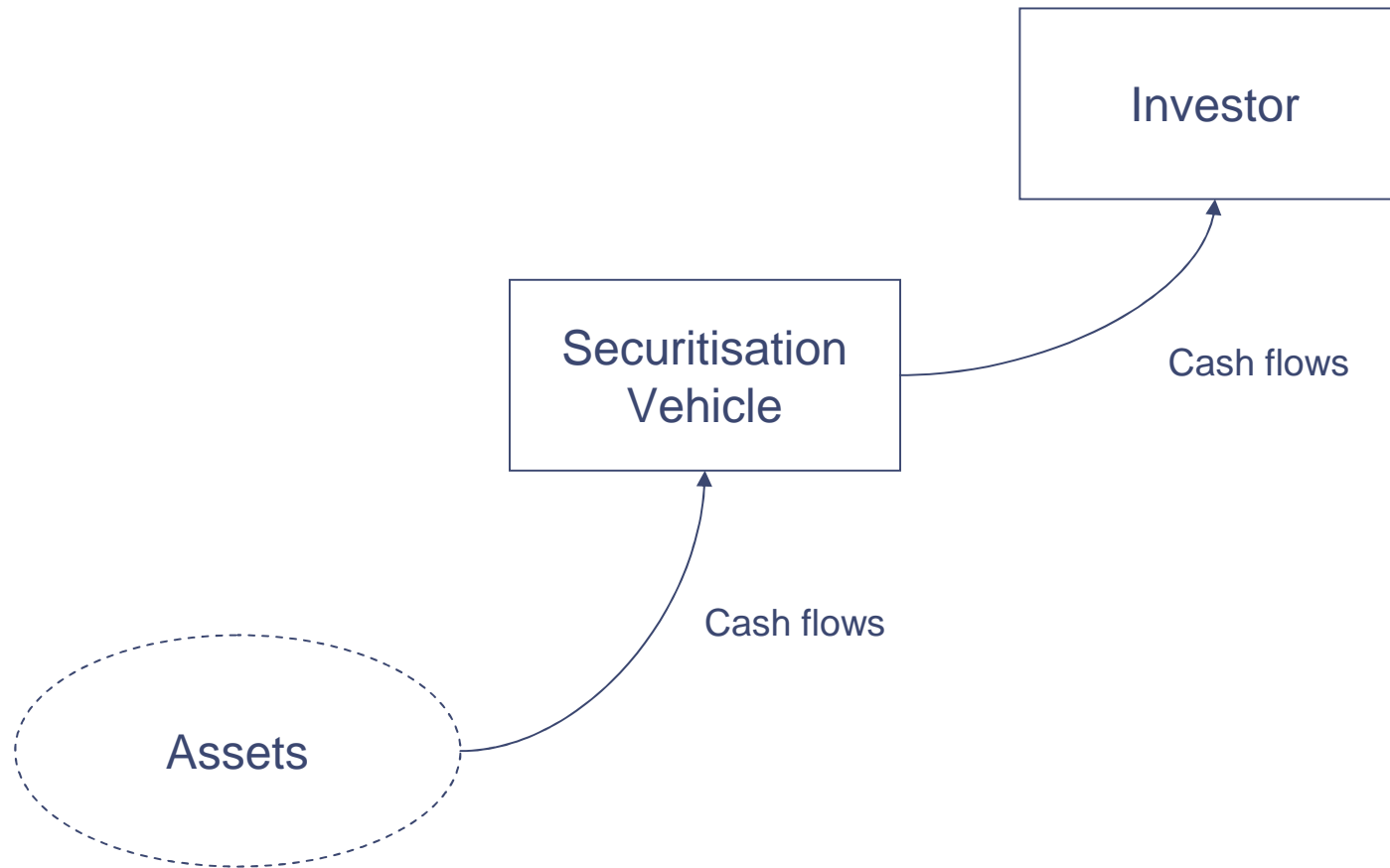
Dividends

(4)(a) A resident of the United Kingdom who receives dividends from a company which is a resident of Italy shall – subject to the provisions of subparagraph (b) of this paragraph – be entitled, if he is the beneficial owner of the dividends, to

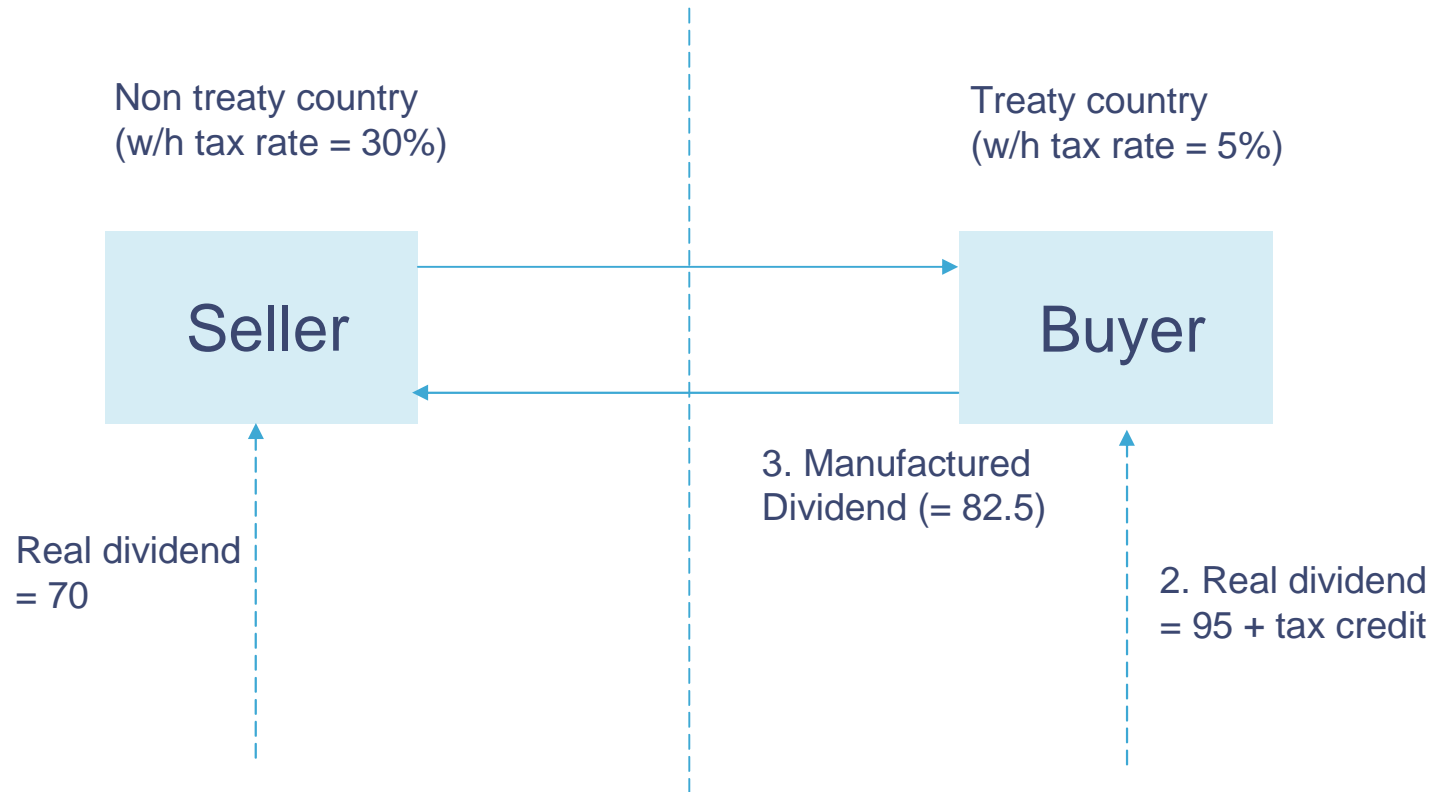
Access to Double Tax Treaties – Relevance of Beneficial Ownership

- Treaty Position
- Question: Who is the “beneficial owner” of a dividend/coupon paid in connection with repo’d/borrowed securities?
- UK law definition:
 - Highly developed concept
 - Beneficial ownership may be divorced from legal ownership
 - Classic example is trust where trustee has legal ownership and beneficiaries have beneficial ownership

Access to Double Tax Treaties – Relevance of Beneficial Ownership



Cross Border Issues – Access to Double Tax Treaties

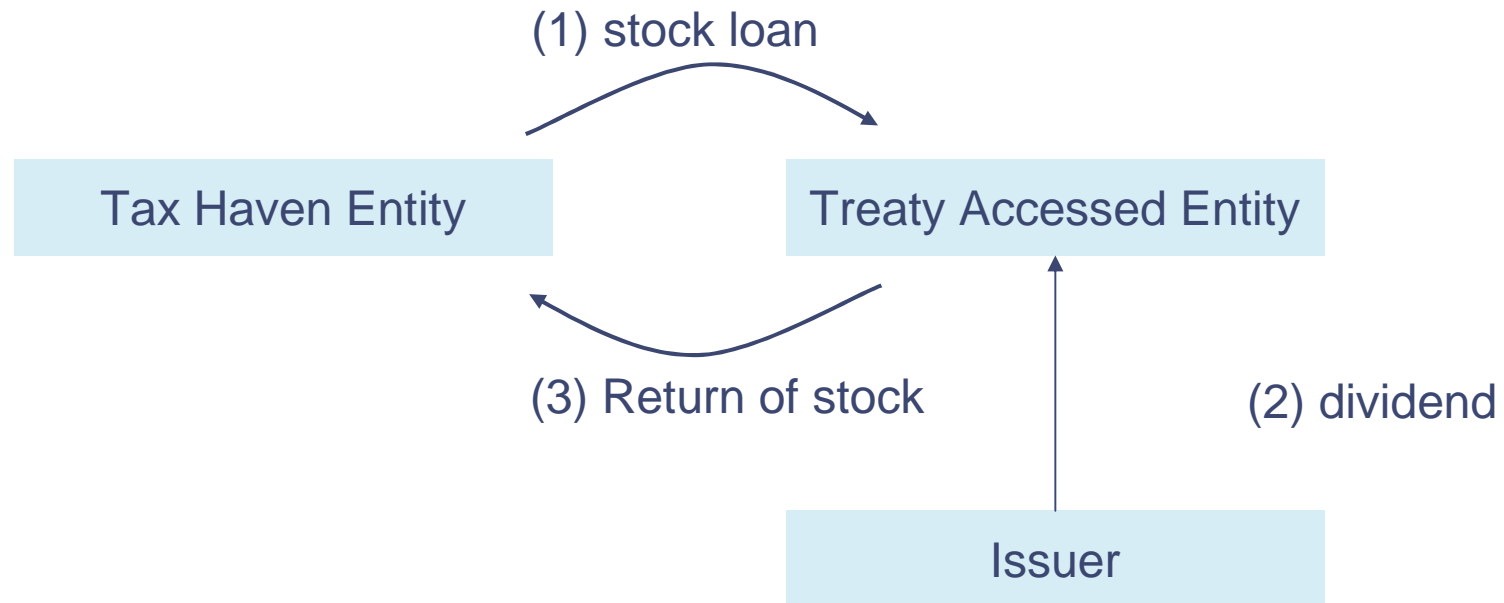


Beneficial Ownership – Key Concepts

- Overseas territories
 - Often no local law concept of beneficial ownership
 - May refer to formal (i.e. legal) position, e.g. repo treated as outright sale
 - May “look through” to seller if repo treated in substance terms (e.g. as a collateralised loan)
 - Difficulties with tax “transparent” entities (e.g. US LLCs)
 - Position varies from country to country

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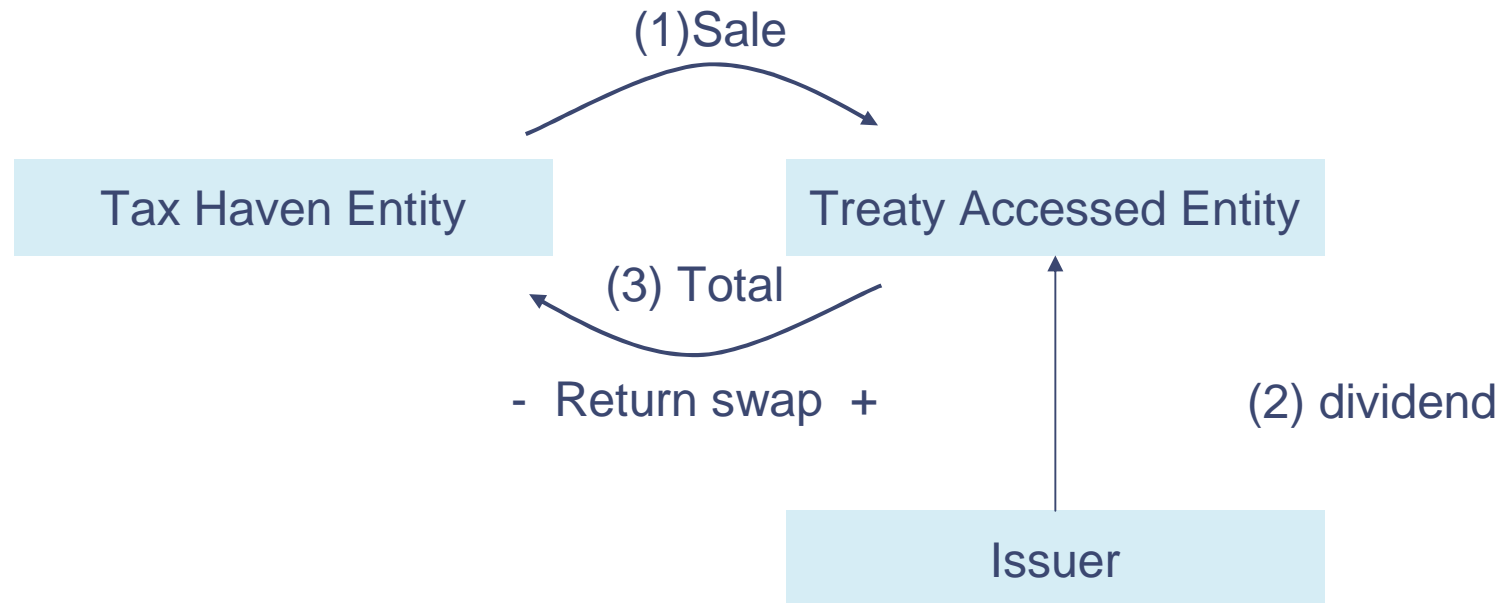
Example 1



- is there any difference to the analysis if there is a repo transaction not a stock loan?
- what if the equities transaction is collateral to a different transaction?

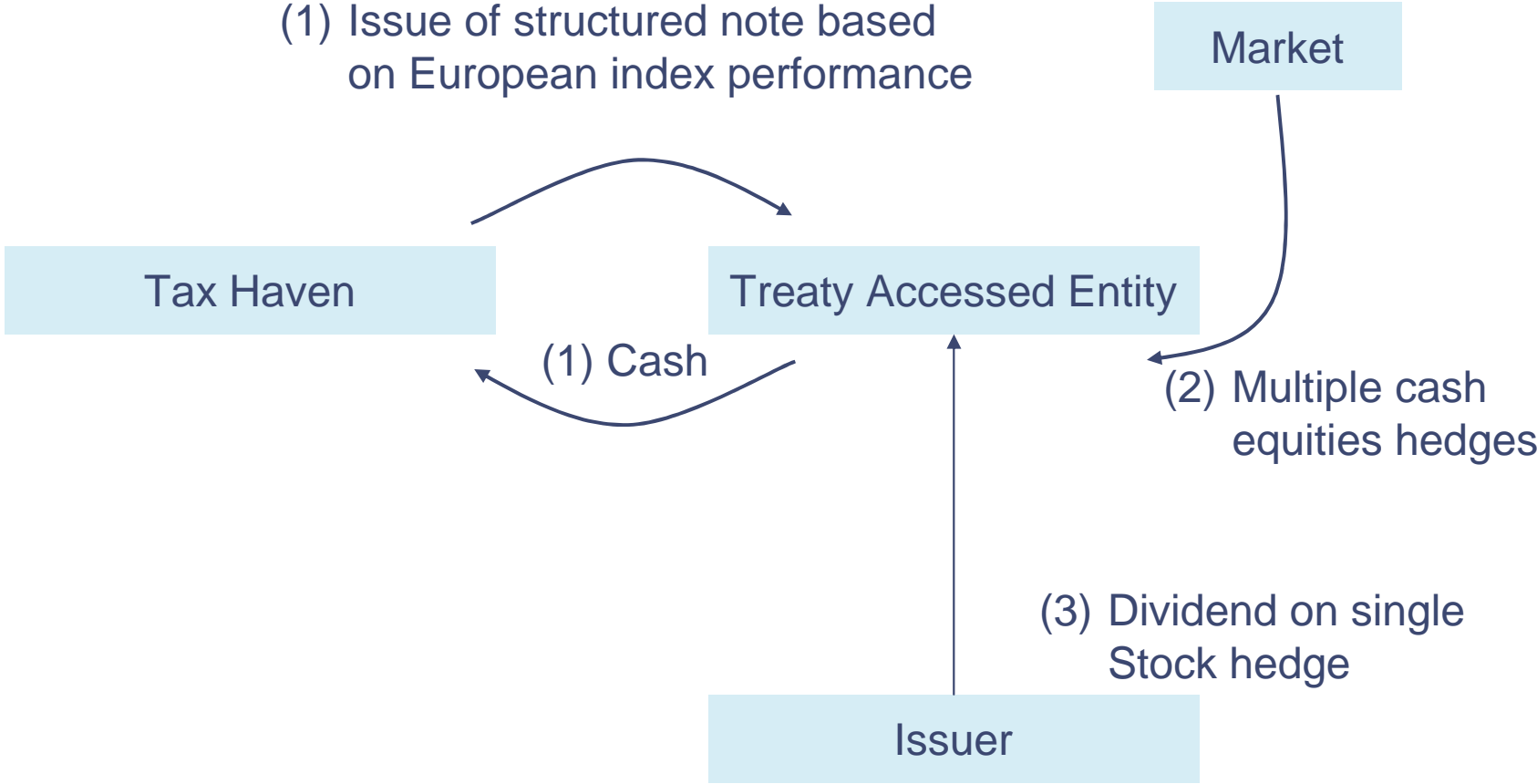
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Example 2



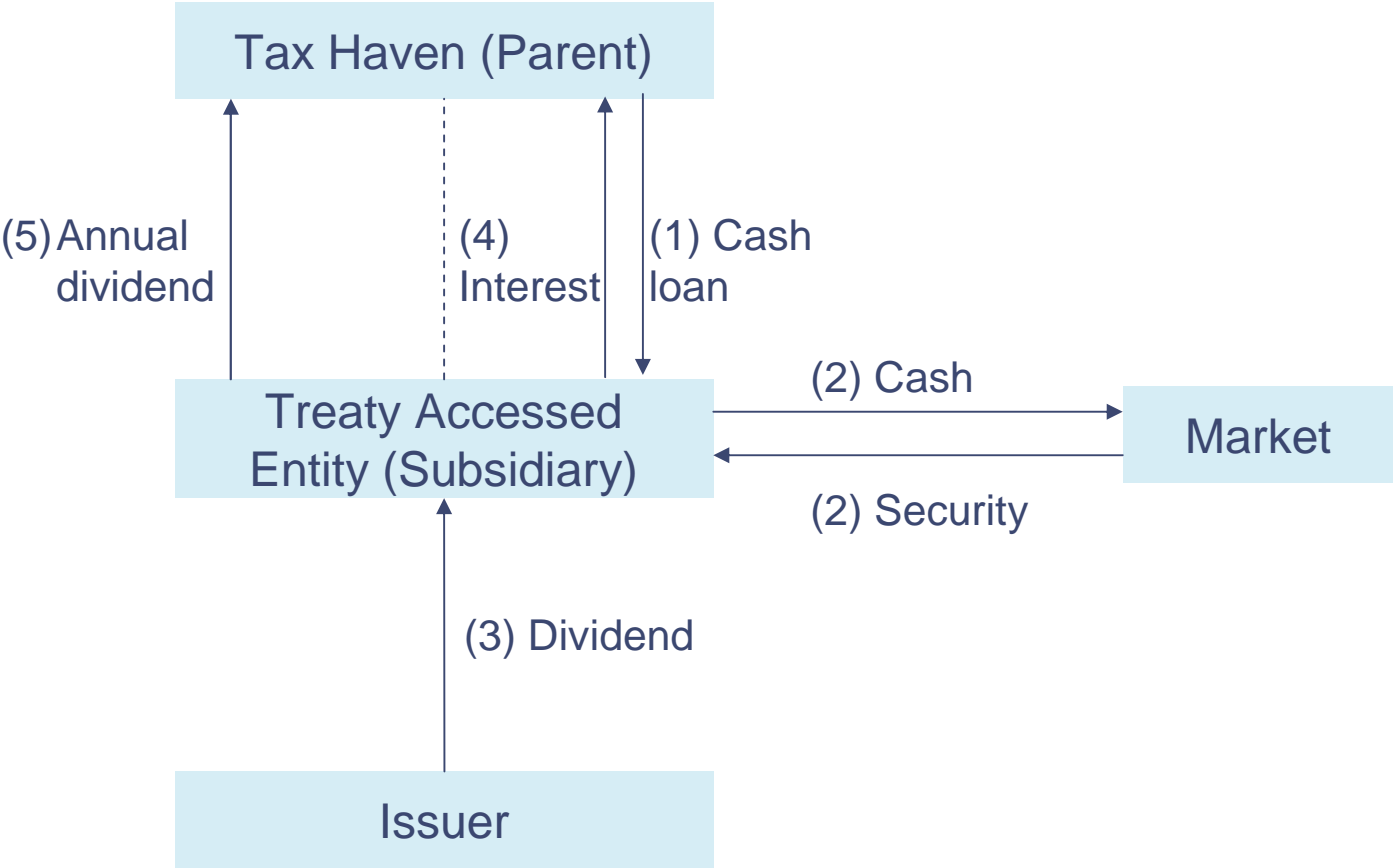
- Would it make any difference if the tax haven entity and the treaty accessed entity were related parties?
- Would it make any difference if the total return swap were simply a price swap without dividend performance?

Example 3



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Example 4



Thank you!

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