IFC
International
Finance
Corporation
World Bank Group

Investor risk Disclosure Practice and Regulation

US, EU and Russia 2007

M_STRIDE
Standard Risk
Disclosure Environment

M_STRIDE Report

Standard Risk Disclosure Environment

International Finance Corporation

АЛЬПИНА БИЗНЕС БУКС

2007

Table of Contents

International Finance Corporation (IFC)

IFC, a member of the World Bank Group, fosters sustainable economic growth in developing countries by financing private sector investment, mobilizing private capital in local and international financial markets, and providing advisory and risk mitigation services to businesses and governments. IFC's vision is that poor people have the opportunity to escape poverty and improve their lives. In FY07, IFC committed $8.2 billion and mobilized an additional $3.9 billion through syndications and structured finance for 299 investments in 69 developing countries. IFC also provided advisory services in 97 countries. For more information, visit www.ifc.org.

IFC in Russia

Russia became a shareholder and a member of IFC in 1993. As of June 30, 2007, IFC has invested around $3.2 billion of its own funds in 150 projects in the country across a variety of sectors. At present, Russia is the largest country exposure in IFC's global portfolio, with a total committed portfolio of $2.2 billion.

Russia became a member and shareholder of IFC in 1993. IFC's investment portfolio in the country stands at $2 billion, making it the largest country exposure for IFC globally. IFC has invested in key sectors including agribusiness, banking, construction materials, health care, housing finance, information technologies, infrastructure, leasing, mining, oil and gas, pulp and paper, retail, and telecommunications. For more information, please visit www.ifc.org/europe.

In fiscal year 2007, IFC invested over $495 million in financial sector, general manufacturing, agribusiness, oil and gas, and telecom projects, including our first partial credit guarantee and interest liquidity facility to enhance a mortgage-backed securitization. For more information, please visit www.ifc.org/europe.

IFC Advisory Services
Russia Primary Mortgage Market Development Project

Mission

Assist in the development of the Russian residential mortgage lending market, raise its efficiency, investment attractiveness and increase mortgage affordability to borrowers.

Goals

- improve legal and regulatory residential mortgage lending framework;
- establish and promote standards of terminology, operations, procedures and credit products;
- promote mortgage lending awareness and best practices via seminars, consultations and training for creditors and borrowers.

Scope

- assist adoption of amendments to the laws and regulations in such areas as:
  - housing construction financing;
  - registration of rights to and transactions with real estate;
  - advanced mortgage products and derivative securities.
- develop and implement standards in residential mortgage lending, including such areas as origination, underwriting and closing, servicing, information exchange and disclosure, portfolio analysis and risk management;
- conduct seminars, workshops and other educational and awareness raising events for the mortgage market lenders and borrowers.

Partners

The Project actively cooperates with:

- the principal representatives of the Russian mortgage industry in the framework of the Working Group SUPER in the areas of development, implementation and promotion of the market standards and legislative initiatives;
- partner mortgage lenders, including regional banks which will receive consultations on organization of efficient process of mortgage lending and implementation of the world-class standards;
- specialized professional market participants in the form of conferences, trainings and consultations;
- relevant legislative and regulatory bodies.

M_Family Products

The Project has developed a suite of residential mortgage lending tools and services for the Russian market participants. The tools are is such areas as borrower protection policies, information disclosure and exchange, legal documentation standards, terminology, overall mortgage lending guidelines.

IFC Russia Primary Mortgage Market Development Project is financed, among others, by the Governments of Switzerland and the Netherlands.

About SECO

The State Secretariat for Economic Affairs is the Swiss Confederation's competence center for all the core issues related to economic policy. Its aim is to create basic regulatory and economic policy conditions to enable business to flourish and benefit all. SECO also represents Switzerland in the large multilateral trade organizations and international negotiations, and is involved in efforts to reduce poverty and help developing countries with transition economies build sustainable democratic societies and viable market economies. Each year, Switzerland spends about 1.9 billion Swiss francs on development cooperation and transition assistance to countries.

About EVD

The Agency for International Business and Cooperation (EVD) is part of the Dutch Ministry of Economic Affairs. Its mission is to promote and encourage international business and international cooperation. As a State agency and a partner to both private-sector and public-sector organizations, the EVD aims to help them achieve success in their international operations.

M_STRIDE
Standard Risk Disclosure Environment Report

Note to the Reader

In 2007 IFC Advisory Services undertook an initiative to review and analyze the legislative and regulatory environment of mortgage backed securities investor disclosure regimes. This effort was specifically focused on relevant practices and regulation in US, EU and Russia in the context of the Russian residential mortgage market.

The aim of this initiative is to provide a set of practice guidelines and recommendations that will be useful to lawyers, financial institutions and investors looking for international best practice in the area of information disclosure relating to Mortgage-backed Securities in Russia, not only for initial public offerings in the international markets, but also, for on-going compliance to local regulatory requirements.

Keeping with the tradition of the IFC Advisory Services Russia Primary Mortgage Market Development Project to uniformly name our products and services, the activities within this initiative were aptly dubbed M_STRIDE, which is an acronym for Mortgage Standard Risk Disclosure Environment.

This Report constitutes an initial M_STRIDE framework document, a discourse on the underlying ideology of the initiative and an invitation to the international legal and finance community to participate in the initiative by providing insight and review.

The *mission* of M_STRIDE is to contribute to the process of international standardization of securitization by setting guidelines and making recommendations on best practices in information disclosure relating to asset-backed securities and in particular mortgage-backed securities.

M_STRIDE *promotes standardization* by capturing best practices based on a comparative analysis of the laws and regulations concerning disclosures. The scope of the analysis focuses on recent regulations concerning disclosures of asset-backed securities in the US, UK and Europe and point to overlaps as well as gaps in the regulatory architecture in Russia.

The *goal* of M_STRIDE is to devise a standard approach to risk disclosure and facilitate promulgation of relevant best practices via a set of market practitioner-oriented guidelines as well as regulator and other market stakeholders bound suggestions on appropriate amendments to the statute and custom.

Key *beneficiaries* and target audience for the M_STRIDE include Russian residential mortgage lenders, both seeking external funding and portfolio-holding oriented ones, as the risks associated with the asset need to be understood by and disclosed to both types currently present on the market.

Auxiliary beneficiaries are the regulator, including banking and financial market authorities, legal counsel to the lenders, mortgage lending analytics community.

As a consequence to improved standardization regime in the area of risk disclosure, which the authors shall shamelessly attempt to assign in part to M_STRIDE activities, the ultimate beneficiary shall be the investor and the lender alike, profiting from better pricing and cost of capital, respectively.

The *questions* we undertook to investigate and are posing to the readers revolves around the relation of financial risks and legal issues, particularly such of residential mortgage loans extended to private individuals in Russia. Such narrow bounds of the discussion are intentional so that degree of concreteness can be achieved in addition to enabling inference to a more common observation.

We are of the opinion that such relation exists; moreover, it is the duty, whether codified or implied, of the legal counsel and other relevant advisors to the parties to transactions, particularly to investors in the instruments produced by such transactions, to appropriately disclose the very existence of certain risks and to extend the opinion on their materiality or severity. Such disclosure needs to be public, complete, timely and relevant in order to serve as a basis of action by a prudent investor or another qualified party.

It must be also keep in mind the complexity of such financial instrument as securitization. Whilst the avowed purpose of disclosure in securities is an investor's protection,[1] securitization transactions are becoming so densely complex that no single human being can possibly (or credibly) be said to understand them.[2]

If prospectus disclosures, for example, are of transactions that are so horribly complex that no one human being can understand them then what is the point of disclosures in the first place? Hence we expect that the developed standards of disclosure should balance the thoroughness and conciseness

We frequently use the words 'convergence' and 'common or customary usage for all'. These terms capture an essential theme of M_STRIDE – whilst the financial instruments produced by securitization are within the reach of global investors, the most substantial legal risks of these instruments are manifestly local. Customary codes of conduct and procedures are important for the standardization of market practice.

One particular area of focus is disclosures both in securitization prospectuses and in relation to on-going reporting requirements, since disclosures are meant first to protect the investor but must be sensitively balanced against the potential costs to growing and dynamic markets. In today's global markets, it is important

[1] See, Hazlem citation.

[2] Schwarcz, op. cit., Note 32, referring to the scholarly literature hailing the complexity of structured finance transactions in the aftermath of the Enron collapse, states: "…complexity goes far beyond Enron, that relatively few people can understand structured transactions, and that some transactions may not even be understandable by any single person." In Note 61, Schwarcz cites: Liesman, S. (Jan 23, 2003) "deciphering the Black Box: Many Accounting Practices, Not Just Enron's, Are Hard to Penetrate," Wall St. J., at C1 "(quoting Philip Livingston, President of Financial Executives International, as calling the new rules for derivatives "a monstrosity of accounting standards that nobody understands," including accountants and chief financial officers)." In Note 79, Schwarcz also cites: Oster, C. and Brown, K. AIG (Jan 13, 2002) "A complex Industry, A Very Complex Company," Wall St. J., at C1 "(observing, in the context of American International Group, that the problem is "not obfuscation, it's sheer complexity").

to develop disclosure standards based on efficiency since investors will have to quickly and ultimately decide the fate of jurisdictions that have too cumbersome and therefore, anti-competitive regulatory regimes.

The evolution of international standards in the area of private international law comes from the day to day practice of lawyers. International standards, whether informal or formal, are the result of the accretion of practices created by lawyers concerned with the legal risks of international transactions.

Through these transactions, a type of international *Lex Juris* authored by lawyers and market practitioners, much like the *Lex Mercantoria*, is currently being developed for securitization transactions.[3] These implicit standards are near-enough universal, and therefore, applicable and comparable across jurisdictions.

In closing, while the recent US residential mortgage lending and securities issuance troubles provide ample evidence to the importance of appropriate disclosure practices and statute, M_STRIDE is envisioned to be more universal and not opportunistic of such crisis.

Joseph Tanega, Andrey Milyutin,
Rustam Turkmenov,
and Tatyana Koroleva

Moscow, London 2006, 2007, 2008

[3] See, Frankel, T. (Jan 2003) "The Law of Cross-Border Securitization: Lex Juris" 12 *Duke J. of Compa. & Int'l L.* 475. "Does the system that is evolving today as *lex Juris* for cross-border securitization provide a useful model for other laws in a global context? This part anticipates the future of *lex Juris*. In a fast-moving and changeable environment, a system of grounded in private lawmaking can be more flexible and very useful when conflicts ultimately arise. It can be copied by other actors and adjusted to their needs, natures, and cultures, to become a truly cosmopolitan private lawmaking process. This private lawmaking, however, requires a relatively small group of interacting private law-makers, and a peaceful coexistence with applicable domestic laws." "I conclude that *lex Juris* belongs to a growing number of cross-border contract-based legal systems, for example, laws concerning the Internet. *Lex Juris* may be the forerunner of a new type of lawmaking regulating global activities: law-like rules that escape tight control of domestic laws, but take them into account; rules that are highly flexible for a fast-changing environment, but quickly unified into standards and guidelines of sufficient predictability." *Id*., at 476-477.

1 INTRODUCTION

1.1 Purpose of report

The purpose of this report is to provide a comparative analysis of the disclosure requirements for asset-backed securities in the US, EU and Russia in order to support the development of the Russian mortgage-backed securities market. The report will not only compare the regulatory requirements of the different regimes, but also identify and develop a set of high level principles and detailed elements for disclosures concerning asset-backed securities which may be used by legal practitioners and bankers for the production of prospectuses and on-going reporting to investors.

1.2 Complexity and Disclosure in the Financial Markets

Securities regulations throughout the world are being led by a set of prudential techniques aimed at reducing risk. These include risk analysis, real time reporting and capital adequacy rules.[4] Indeed, arguably the leading principles-based, risk-focused approach[5] to regulating and calculating the capital adequacy of internationally active banks, Basel II,[6] sets out as a fundamental principle, that above all else, securitization should be almost scientifically judged, controlled and measured in terms of its economic substance and not merely on its legal form. This fundamental principle of substance over legal form is well known in common law jurisdictions,[7] and used to pierce the veil of corporate fraud schemes, turning the convoluted ("many transactions") of a corporate group into one transaction, and thereby reducing the legal complexity into a simple, understandable, traceable and usually, taxable determination of economic value.[8] The economic agents in these complex transactions

---

[4] Jopson, B. (26 Feb 2007) "Dominance of the Big Four Under Attack," *Financial Times Special Report, FT International Accountancy, Financial Times*, at 1.

[5] The current Federal Reserve Chairman, Ben Bernanke, has urged US regulators to support "principle-based, risk-focused" oversight. See, Grant, J. (May 15, 2007) "Bernanke Calls for UK-Stye Regulation," 19:11.

[6] Basel Committee on Banking Supervision (June 2007) *International Convergence of Capital Measurement and Capital Standards, A Revised Framework Comprehensive Version*, available at: http://www.bis.org/publ/bcbs107.pdf.

[7] It also poses a bit of a conundrum as to how lawyers are to provide legal opinions on securitization transactions if their legal opinion needs to take a view on the economic substance of a transaction, when their expertise is limited only to the legal issues.

[8] The Courts applying the substance over form doctrine interpret the purported set of independent and separable transactions as a single transaction. If the independent and separable transactions were to remain so, then the parties engaged in the transaction would likely be benefiting in terms of tax efficiency, say. However, if the set of transactions are deemed to be one transaction, then the scheme would fail and the parties would be held liable for whatever governmentally imposed penalty is due. For a discussion of US tax law doctrines of substance over form, see *Long Term Capital Holdings, et. al. v. United States of America*, 330 F. Supp. 2d 122, decided August 27, 2004. In *Long Term Capital Holdings*, the "steps-transaction doctrine" is defined as "the steps in a series of formally separate but related transactions involving the transfer of property as a single transaction, if all the steps are substantially linked. Rather than viewing each step as an isolated incident, the steps are viewed together as components of an overall plan." *Greene v. U.S.*, 13 F.3d 577, 583 (2d Cir 1994). Courts have identified three tests for determining

might be lauded for their cleverness in being able to steer clients' money through a maze of regulatory and legal risks, taking advantage of loopholes in cross-border taxation, ensuring that enforcement procedures will take place in the most advantageous jurisdictions, and selecting the most favourable accountancy treatment.[9] However, the problem of complexity remains. Whilst the avowed purpose of securities regulations is disclosure for investor protection,[10] securitization transactions are becoming so densely complex that no single human being can possibly (or credibly) be said to understand them.[11] If prospectus disclosures, for example, are of transactions that are so horribly complex that no one human being can understand them then what is the point of disclosures in the first place?

The US Securities Commission cognizant of this ever growing complexity in disclosures believes that well-structured regulations that are principled-based may actually reduce the information overload experienced by practitioners, and contribute towards a normative objective of understanding complex transactions without resort to overly legalistic presentations.[12]

whether to apply the steps transaction doctrine, the "end result," the "interdependence," and the "binding commitment" tests. See *Associated*, 927 F.2d at 1522. In general, "the doctrine will operate where the circumstances satisfy only one of the tests." See *True v. U.S.*, 190 F.3d 1165, 1175 (10th Cir. 1999); see also Greene, 13 F.3d at 583-85; Associated, 927 F.2d at 1527-28.

9 See, Schwarcz, S.L. (2004) "Rethinking The Disclosure paradigm in a World of Complexity," 2004 U. Ill. L. Rev. 1. Schwarcz states: "Notwithstanding that desirability [i.e. lower-cost-financing through disintermediation which is socially desirable], these transactions [i.e. structured transactions] are always extremely complex and, in the case of securitizations, often rely on multiple SPEs. Furthermore, in order to integrate disparate disciplines such as bankruptcy, tax, securities law, commercial law, accounting, and finance, structured transactions often appear to be highly convoluted. Disclosure of a complex and convoluted structure to investors of the originator—the audience on which this article primarily focuses—may well be either too detailed for many of those investors, even institutional investors, to understand assimilate, or too superficial to allow investors to fully assess the transaction and its ramifications. The problem is compounded where, as is common, an originator engages in numerous such transactions." *Id* at 4-5.

10 See, Hazen, T.L. (4th 3d. 2002) where he states that "federal securities law's exclusive focus is on full disclosure". *Id* at 740.

11 Schwarcz, op. cit., Note 32, referring to the scholarly literature hailing the complexity of structured finance transactions in the aftermath of the Enron collapse, states: "…complexity goes far beyond Enron, that relatively few people can understand structured transactions, and that some transactions may not even be understandable by any single person." In Note 61, Schwarcz cites: Liesman, S. (Jan 23, 2003) "deciphering the Black Box: Many Accounting Practices, Not Just Enron's, Are Hard to Penetrate," Wall St. J., at C1 "(quoting Philip Livingston, President of Financial Executives International, as calling the new rules for derivatives "a monstrosity of accounting standards that nobody understands," including accountants and chief financial officers)." In Note 79, Schwarcz also cites: Oster, C. and Brown, K. AIG (Jan 13, 2002) "A complex Industry, A Very Complex Company," Wall St. J., at C1 "(observing, in the context of American International Group, that the problem is "not obfuscation, it's sheer complexity").

12 See, US Federal Register, Part II Securities and Exchange Commission, 17 CFR Parts 210, 228, et al. "Asset-Backed Securities; Final Rule, January 7, 2005, (herein referred to as "US Final Rule of Asset-Backed Securities (2005)" or "Final Rule ABS (2005)", available at: http://www.sec.gov/rules/final/33-8518fr.pdf, §III.B.1, at 1531. "As we stated in the Proposing Release, however, we remain concerned that current disclosure practice has resulted in the inclusion of undue boilerplate language in ABS filings, particularly prospectuses and registration statements, and a disproportionate emphasis on legal recitations of transaction terms. Further, as disclosure practice may have been driven primarily by the staff review process and by observing and conforming to filings for other transactions, disclosures may have been included form other filings or retained from prior filings without necessarily considering their applicability or continued applicability with respect to

In this report, we will examine the disclosure requirements under US, EU and Russian laws for asset backed securities, constantly referring to the substance over legal form theme. In brief, our thesis is that in a world of utter complexity, the purpose of disclosure requirements for asset backed securities is to lower the threshold of perceived risk for potentially transacting parties, and thus, enable and stimulate a market which would otherwise be perceived too dangerous to transact. Although there are various types of disclosure requirements, from mandatory disclosures incurring strict liability to permissive disclosures which may be omitted so long as their omission is explained, the overall purpose of disclosures for complex transactions is to overcome the initial hurdle of information asymmetry between the potentially transacting parties. However, as the events in the sub prime markets of the spring and summer of 2007 indicate, the success of a regulation in overcoming the initial information asymmetry between seller and buyer of particular asset-backed securities does not necessarily mean that the general market understands how the critical disclosures relating to the valuation of the underlying assets, such as delinquencies and loss information, may be accessed.[13]

Indeed, the liquidity crunch allegedly "caused" by the failures of sub prime market of mortgage-backed securities is very much symptomatic of the information asymmetry occurring at another level, that is, where the regulators have failed to explain the workings of complex asset-backed regulations to the general public.[14] This risk of unexplained complexity of regulation is an issue which we hope this Report will provide a platform for further and intense discussion. Although most securities, especially asset-backed securities regulations are likely to be subsumed under

the transaction in question. The cumulative effect of these practices is to diminish in some cases the usefulness of the disclosure documents through the accumulation of unnecessary detail, duplicative or uninformative disclosure and legalistic recitations of transaction terms that obscures material information. *Efforts to revise disclosure documents in response to our "plain English" initiative have certainly helped by demonstrating that even the most complex structures can be described clearly and accurately without resorting to overly legalistic presentations*. [Emphasis added and footnotes omitted.] The SEC appears to dichotomize "uninformative" legalistic disclosures and "material information" which again implies an economic substance versus mere legal form type of argument. Without its admission, the subtext of their comment is that the SEC's own previous "rule-based approach" had probably led to much of the difficulty in understanding the complexity of disclosures. The SEC's go-forward strategy regarding asset-backed securities is to mandate only those disclosures which are material. Whilst materiality appears to be based on a reasonable person standard, we would claim that materiality depends on whether the particular identified factor would impact negatively or positively on the net present value of the investment. Although there are plethora of sophisticated alternative models for determining the value of an investment, we assume for our purposes that in determining the economic value of an investment, the great majority of investment professionals would not deny the usefulness of a net present value model for their calculations.

[13] See, Tanega, J. (24 August 2007) Letter to the Editor, *Financial Times*, at 10, available at: http://www.ft.com/cms/s/0/68a04296-51da-11dc-8779-0000779fd2ac.html.

[14] In a strong sense, the message raised in Note 9 should be applied self-reflectively to the regulator who chides the legal practice for failing to use plain English, but in effect, does not help market participants, which includes opinion formers such as financial journalists, pundits, and other media-genic personalities to understand the basic framework or operations of complex asset-backed securities regulations. Although greater transparency through standard reporting is one of the aims and obvious beneficial effects of asset-backed securities regulations, we find nothing in the news media by government officials or regulators who have said that factual disclosures of asset-backed securities are available for public scrutiny and are already mandated by the law. One announcement, even as a point of education, about the stability of financial disclosures and their public availability during the market spasms of the spring and summer of 2007 would have been welcomed to quell the ever rising tide of ignorance amongst the rumour mongers.

a consultation process which involves very limited public participation, and almost little or no education of the potential benefits and threats of regulation. Our view is that at least in a normative sense, a well-formed regulatory regime of disclosures acts as a subsidized risk management advisory service to both the issuer and the investors.[15]

As we plough through the detailed rules of disclosure for asset backed securities in the US and EU and compare these to those found (and not found) in Russia, there are bound to be regulatory gaps. We are seeking in this report to define the high-level benchmark of disclosures required for a nascent market, that is, specifically the mortgage-backed securities market of Russia.

Another complexity which cannot be ignored about securitization is that it is a new type of private international financial law being created by its legal practitioners—a type of *lex Juris* which needs to be flexible rather than doctrinaire in order to keep up with dynamic financial market innovations. The development of the international *lex Juris* is part of a wider trend towards what scholars and regulators have called the movement towards convergence in corporate reporting under the securities laws.[16] The argument is that efficiencies can be gained by having a pan-European-US securities regulations, which allows issues to be sold to investors in a much enlarged market.[17] Through contractual precedents created and replicated by international practitioners we have a profound basis which informs the development of international convergence, and in turn, sets the foundation for the development of international standards of disclosures for particular market instruments.

Since securitization is primarily focused on bringing (1) the lowest risk form of liquidity to otherwise illiquid assets and (2) transforming the value of long-term cash flows into an immediate market price, securitization practitioners are naturally seeking markets which offer a safe haven in terms of legal enforceable stability and transparency, and deep liquidity. Securitization is a set of legal and financial techniques which allow the value of underlying illiquid assets to become dematerialized into fungible financial instruments. However, an important limit to these techniques as demonstrated by the subprime crash of 2007 is that the cash flows from the underlying assets which are the basis for the valuation of the securities must be providently selected under appropriate underwriting policies, otherwise the credibility of the entire issue is called into question, no matter what the credit rating. A more nuanced view of the subprime debacle of 2007 tells us that new regulatory disclosure requirements for asset-backed securities should be introduced to the markets not only for the sake of transparency, but *carefully*, with the broad participation of all the major sectors who may have an interest in the markets survival since regulatory driven disclosures may not be completely understood by the general public, and in fact, completely ignored. For example, during the February to September 2007 period, while the press and many pundits focused on the deteriorating asset quality of subprime issues, there was no press release or media coverage of the actual disclosure requirements for asset-backed securities under US Regulation

[15] It is arguable that the UK Financial Services Authority through its risk-based set of regulations provides such a risk management service to financial institutions. See, UK FSA (2006) *Financial Risk Outlook*, at v, available at: http://www.fsa.gov.uk/pubs/plan/financial_risk_outlook_2006.pdf.

[16] Alexander, K., Ferran, E., Jackson, H.E. and Moloney, N. (January 2007) "A Report on the Transatlantic Financial Services Regulatory Dialogue," at 5, Harvard John M. Olin Center for Law, Economics, and Business, The Social Science Research network Electronic Paper Collection: available at: http://papers.ssrn.com/sol3/papers.cfm?abstract_id=961269.

[17] See, European Commission (2005) "A Stronger E.U.-U.S. Partnership and More Open market for the 21st Century, at 196.

AB. Even a cursory reading of the first few paragraphs of this regulation are telling since it requires detailed presentation of "delinquency experience in 30 or 31 day increments,"[18] which, in effect, means that issuers of asset-backed securities are required to report delinquencies on a monthly basis on the new Form 10-D.

In the comments prior to the enactment of Regulation AB, many issuers objected to this new standard disclosure for delinquencies since different issuers had different methods for curing delinquencies as well as different timeframes as per the underlying agreements. Prior to the effective date of Regulation AB (1 January 2006), the practice of issuers was to report loss and delinquency data only on an annual financial statement. The markets reacted to news of assumptions about the valuation of subprime assets without checking the publicly available information about the cash flow performance of the underlying assets. Thus, the irony of the most complete security regulation on asset-backed securities in the world is that while it aimed at setting a disclosure regime on the basis of enhanced transparency, almost no one after its promulgation could point to the regulation and say that it was sufficient to overcome market asymmetric information. As we shall see, one of the fundamental points of regulations governing asset-backed securities is to overcome information asymmetry at the issuer-to-investor level.

We believe that the US Regulation on asset-backed securities does this job adequately, but at the general market level involving participants in collateral markets, understanding of the policies of asset-backed securities regulations and how they operate are sorely lacking. Given this lack of understanding and the need to correct market misconceptions about asset-backed securities, it is important to consider asset-backed securities disclosures as *risk management standards.* In this regard, for our purposes the main question is what level of disclosures is most appropriate for Russian mortgage backed securities?

1.3 Appropriate Level of Complexity of Disclosures

Securitization disclosures should help investors scrutinize the underlying pool of assets and all the major parties to the transaction that together pose essential risks and catastrophic failure to the issue over its lifetime. However, at the same time, the mandatory disclosures should not be so broad and deep so as to completely scare off potential investors with prospects of unlimited liability or continuous high-level costs of compliance. Overregulation can be detrimental to market development as can be seen in the rather lacklustre trend in US initial public offerings in the wake of the US Sarbanes-Oxley Act.[19] As Lucas Papdemos, the European Central Bank's vice-president, responsible for financial stability issues, states,

> A key question is how we can obtain sufficient data to help improve our detection and understanding of risks and vulnerability without imposing restrictions and burdens which would unnecessarily hamper innovation and efficiency in financial markets.[20]

[18] 17 CFR 229.1100(b)(2).

[19] See US Sarbane-Oxley Act, 2002, at http://www.sec.gov/spotlight/sarbanes-oxley.htm

[20] Simensen, I. and Atkins, R. (22 Aug 2007) "'Not Uncritical' Subprime Exposure Drags Down German Banks," Financial Times, at 9.

A delicate balance must be struck in the regulatory regime that allows for and positively encourages the continuous and sustainable development of the capital markets. For example, in 2001, Brazil raised the regulatory standards in the Novo Mercado, which resulted in attracting vast amounts of capital from foreign investors and driving trading and issuance volumes to record levels.[21] In China, after the introduction of reforms in the capital markets and corporate governance, similar effects were produced.[22] The general policy of enabling sufficient information to overcome the unquantified uncertainty of relatively new markets and reducing unnecessary and burdensome costs of compliance is difficult to maintain in practice. We can only hope that the principle-based and risk-focused approach advocated in this paper will help practitioners and regulators alike strike the appropriate balance that achieves a sense of risk-tolerance.[23]

1.4 Justifying Disclosures for Market Development

Disclosures are at the heart of securities regulations.[24] The purpose of disclosures in securities regulations at least at the level of the initial public offering is to mitigate the information advantage which issuer-sellers have over investor-buyers.[25] As Akerloff (1970) famously argued, markets in which the sellers have an information advantage have a temptation to sell and represent lower quality items as higher quality items to less informed buyers. Let us call this form of information asymmetry "dysfunctional asymmetry". As a consequence of this dysfunctional asymmetry, the lower quality goods will tend to drive out higher quality goods from the market, which if iterated over time, will lead to an equilibrium where there is no trading at all or market failure.[26]

Ironically, there is less chance of market collapse where the information advantage favours the buyer. Let us call this form of information asymmetry "functional asymmetry". Since the buyer will be able to more accurately assess the quality of the goods, the forces of supply and demand will prevail, and bad quality items will be seen for what they are and more accurate pricing will occur. That is, transactions will occur at prices distinguishing between lower level and higher quality goods.[27] Schwarz in summarizing the Akerlof solution to the "lemons problem" states that it is "it is up to the seller to achieve a solution to this problem of quality uncertainty" and

[21] Varvel, E. (May 30, 2007) "Plenty of listing options for every need," *Corporate Finance Financial Times Special Report, May Edition, Financial Times*, at 6.

[22] *Ibid.*

[23] See model of expected risk tolerance in Figure 8: Schematic of US ABS Regulatory Approach—Lensing of Disclosures at 83 below.

[24] See Hazen *supra.*

[25] This is the so-called information asymmetry problem. See Akerloff, G. "The Market for Lemons: Quality Uncertainty and The Market Mechanism", *Quarterly Journal of Economics*, August 1970.

[26] Market failures may occur where the uncertainty regarding the quality of the product is so great that it is impossible for the customer to calculate the product's value, e.g., used cars, health care for the elderly, the availability of credit markets in developing countries, the quality of asset-backed securities in countries which lack standards in underwriting and so on.

[27] Although scholars have called this latter situation information asymmetry in favour of the buyer, it would be more precise to say that the situation in which buyers and sellers transact is when they are in a state of risk symmetry. That is, when their subjective perception of the risk for a given level of information is equivalent. See, Tanega, J. (2005) "Securitization

"one obvious solution is guaranties, such as warranties on the sale of goods, in order to shift the risk from the buyer to the seller."[28] However, the lesson to be learned for the asset-backed securities markets is that mandatory disclosures by the seller help overcome dysfunctional asymmetry so long as such information is pertinent to the investor understanding the quality of the investment.[29] A well-structured disclosure regime that aims at functional asymmetry therefore should reduce the risk of market failure since more accurately informed investors will be able to distinguish between lower and higher quality issues, encouraging market expansion.[30]

The proper policy relating to mandatory disclosures therefore should be seen as assisting in setting a floor of the types of information which investors need in order to more accurately price what would otherwise remain qualitatively uncertain. Put positively, such disclosures should be directly or indirectly related to the quality of the underlying assets. The disclosure items should be presented in a manner which enables the investor to comprehend the risks and rewards of the transaction. We believe this is an ongoing risk management process.

1.5 Rules-based versus Principles-based, Risk-focused Approach

One of the significant, although arguably over boiled,[31] debates amongst legal scholars, supervisory regulators and international accounting bodies regarding disclosures is whether the standards setting out disclosures should require mere compliance to legal rules (i.e., "rule-based") or be based on principles which upon their implementation in practice, can be reasonably interpreted between the supervisor and the regulatee (i.e., "principles-based") and further, that such principles in implementation require a quality management system based on risk identification, assessment, monitoring and control, in short, "risk-based".[32] The literature indi-

Framework under Basel II: A Risk Based Approach to Substance over Form" *Journal of International Banking Law and Regulation*, 12:623-625.

[28] Schwarz, S.L. (2004) "Rethinking the Disclosure paradigm in a World of Complexity," *University of Illinois Law Review*, at 25.

[29] See, Cox, Hillman, and Langevoort (3rd 3d. 2001). One theory of disclosure is that it is a means of trouncing the monopoly management has over corporate information, and is necessary because as Schwarcz states, "…separation of ownership and control can cause managers to maximize their own utility at the expense of investors." Citing Cox et al, at 358.

[30] It is interesting to note that the investment banking fraternity of the United States would not believe this sort of theorizing, as Schwarz quoting Frank Partnoy, Professor of Law, University of San Diego School of Law who states that "his former colleagues at the Morgan Stanley investment banking firm 'would have balked at the idea' of permitting disclosure of the details of deals." Whilst this makes sense from an individualistic trading perspective, it makes no sense from a regulatory perspective aiming at sustainable market development. Schwarcz (2004) "Rethinking the Disclosure Paradigm in a World of Complexity," note 25 *supra*.

[31] See, Cunningham, L.A. (March 13, 2007) "A Prescription to Retire the Rhetoric of "Principles-Based Systems" in Corporate law, Securities Regulation and Accounting", Research Paper 127, Boston College Law, available at SSRN: And for a review of the theoretical literature on principles-based regulation, see Ford, C.L. (March 11, 2007) "New Governance, Compliance, and Principles-Based Securities Regulation", American Business Law Journal, Forthcoming Available at SSRN: . Bottom of Form

[32] See, for example, Bruce, R. (March 29, 2007) "As a rule, Principles Should Dominate," *FT Compliance Special Report, Financial Times*, at 1-2.

cates that there is a general consensus towards a principles-based[33] and risk-focused approach, but that this does not necessarily mean that "management and auditor behaviour will be principles-based and risk-based in practice."[34]

The principles- and risk-based approach generally favour market solutions and are more difficult for regulators to enforce.[35] For the sake of the administrative convenience of the regulator, a rule-based system is preferred since the bright lines of regulations allow for less ambiguity regarding enforcement actions. For a principles-based system, whilst the regulations may be subject to interpretation, the intention is that reasonable and rationale parties will converge towards agreeable market solutions. However, we are struck by the fact that our comparative analysis of disclosure requirements shows there is very little consistency in the use of methodological terminology in reflecting on what constitutes rule-based, principles-based or risk-based approaches. For example, so-called rules that purport to be rule-based may be couched in a principles-based approach and vice versa.[36] It is not likely, given the different legal traditions, that regulators from different jurisdictions will use legal terminology which is consistently meaningful across jurisdictions. However, for any given asset-backed securities transaction (see below) the basic constellation of transaction parties and transaction agreements, as well as the fundamental risks associated with the underlying assets, are formatively and essentially similar in different jurisdictions. And it is at this level of revealing the structure of the transaction that a comparison of the disclosure rules of different jurisdictions may be made.

1.6 Justifying Disclosures as Part of Risk Management "Culture" System

At one level, for purpose of protecting investors to the maximal extent, we would recommend the use of the US and EU standards of disclosures as the high-level benchmarks for sophisticated and complex issues. Whilst there are obvious differences between the two systems of disclosures which we will discuss below, with the US being linked to numerous regulatory legacies and the EU relegating particularities of implementation to Member States, both systems of disclosures esteem "plain language"[37] and prize "materiality".[38] Both systems in other words recognize the need to make disclosure systems work within reasonable human limitations and

[33] See, Bruce, R. (March 29, 2007) "Sarbanes-Oxley, Emphasis on Rules May Go in the Dustbin of History," *FT Compliance Special Report, Financial Times*, at 2. Quoting John Rowden, head of S404 technical advice at PwC, "The overall direction is away from a rule-based specification towards an approach which permits appropriate judgment. We are moving towards an approach where common sense defines the scope of work." Richard Bennison, head of audit at KPMG states, "The US is trying to take a high-level top-down approach which is what people advocated from the beginning. Sarbanes-Oxley would have had a lot more support if it had started that way."

[34] *Ibid* at 1; see also Note 9 *supra*.

[35] *Ibid* at 2.

[36] Bruce, R.(29 March 2007) "As a rule principles should dominate," *Financial Times, Surveys REC1*, at 5.

[37] See Note 9 above.

[38] Federal Register (7 Jan 2005) *Final Rule Asset-Backed Securities*, at 1509, available at: http://www.sec.gov/rules/final/33-8518fr.pdf, hereinafter referred to as *Final Rule Asset-Backed Securities*.

dimensions.[39] In practical terms amongst market professionals, no system of disclosure would be considered successful, if as one securitization practitioner was heard to say, "An investor in New York has to spend two hours reading a prospectus and not be able to understand it."

For purposes of market development, the US regulations concerning asset-backed securities may be seen as encapsulating the general principles and definitions of current practice of a mature market and simultaneously, the most comprehensive set of instructions and commentary as to what constitutes relevant disclosures in the asset-backed securities market.[40] However, the wholesale translation of these rules to an inchoate market is not necessarily appropriate. The disclosure rules under the level I EU Prospectus Directive[41] and level II EU Prospectus Regulation,[42] and translated into local rules by Member States,[43] though not perfectly simple, may be a more appropriate set of disclosure requirements for markets looking for a relatively less burdensome set of disclosure requirements. In principle, however, the major risk categories used in the US relating to asset-backed securities transactions are universally applicable and are aligned to the concept of functional asymmetry as we have derived from the doctrine of economic substance over legal form[44] and Akerloff's idea of information asymmetry (see above).

That is, if we examine a securitization structure from a purely formal legal perspective, a true sale or assignment of assets of cash flows from the originator to a bankruptcy-remote SPV-issuer is considered a critical aspect of the legal form of the transaction. However, from an economic substance perspective, the risks that are attendant to the failure of the SPV are negligible. Therefore, under the US rules regarding disclosures of asset-backed securities, only nominal identification disclosures are required of the SPV-issuer.[45] In contrast,

[39] There is a firm tradition in securities regulations to use an ordinary prudent person as the standard for comprehending disclosures, with special exception given to sophisticated investors. See, citations. Given the complexity of the financial markets, there is some scholarly debate of moving the traditional reasonable person standard towards an "informed investor" standard, arguing that professionals in the financial markets are essentially buyers and sellers of specialist information. This may be appropriate for some segments in the market, but for new issues, this shift in standard could have the deleterious effect of promoting dysfunctional information asymmetry in favour of the seller.

[40] See, *Final Rule Asset-Backed Securities*, *op cit.*

[41] Directive 2003/71/EC available at: at http://ec.europa.eu/internal_market/securities/prospectus/index_en.htm.

[42] Commission Regulation (EC) No. 809/2004 with specific reference to "Annex VII Minimum Disclosure Requirements for Asset Backed Securities Registration Document (Schedule)" and "Annex VIII Minimum Disclosure Requirements for the Asset Backed Securities Additional Building Block," available at: available at: http://ec.europa.eu/internal_market/securities/isd/mifid2_en.htm.

[43] For an especially good compilation of the EU's level I and level II rules relating to asset backed securities, see, Irish Stock Exchange (2005) *Listing and Admission to Trading -- Guidelines for Asset Backed Securities,* available at http://www.ise.ie/?locID=145&docID=162.

[44] See Basel II, Basel Committee on Banking Supervision (June 2007) *International Convergence of Capital Measurement and Capital Standards, A Revised Framework Comprehensive Version*, available at: http://www.bis.org/publ/bcbs128.pdf.

[45] See, *Final Rule Asset Backed Securities*. "Consistent with current practice and our proposals, we are not requiring audited financial statements regarding the issuing entity for the asset-backed securities in Securities Act or Exchange Act filings." *Id* at 15.

under the EU rules, the centrality of the issuer being the subject of disclosures remains intact.[46] However, in both disclosure systems, a major portion of the mandatory disclosures covers what is the ultimate risk to the transaction, which is the quality of the underlying assets. In relation to this point it is important to note that events in the US subprime market in early 2007 reveal a major irony and limitation of disclosure rules.

That is, whilst mandatory disclosures may be required to reveal the risks attendant to the underlying asset portfolios, purported formal compliance may not necessarily reveal failures in underwriting practices nor do such regulations address the dysfunctional asymmetry of mass media commenters on the state of actual publicly available disclosures. One wonders whether it would not be a reasonable limit of the fundamental freedom of speech to indict those who falsely scream "fire" in a tightly coupled market theatre where the market participants are driven to the exits.[47] Having the strictest disclosure regime in the world, the US rules could not prevent, even with the best intentions, market failures.

The lesson is perhaps that no matter how tightly we draw the required disclosures, the legal liability map will not, in principle, ever match the economic risk map. Thus, whilst the initial transfer of assets must be accomplished legitimately, and whilst the initial legal liability for failure of payment may fall on the SPV-issuer, no rational investor would look only to the credit risk of the SPV-issuer for satisfaction of the obligations of the securities. From a functional symmetry perspective, the investor will need information that will reduce the level of qualitative uncertainty of the transaction. In a word, the investor will seek a level of knowledge that is risk symmetric to the entities that are genuinely accountable and responsible for the payments owed under the securities.

1.7 The Need for Separate and Distinct Disclosures for Asset-backed Securities

It is obvious that the asset backed securities transactions are essentially different from normal securities transactions given that the status of the issuer is one of convenience, holding a number of contractual relationships in order to restructure cash flows and re-order priorities of payments to different classes of investors. Thus, standard disclosure items for the Issuer would be inapplicable to asset-backed securitizations. They may in fact not sufficiently capture categories of information which may be significantly relevant to investors of asset-backed securities, such as "the background, experience, performance and roles of various transaction

[46] This is much like blaming the casing of the bullet for the murder and leaving the person holding the smoking gun blameless.

[47] The allusion is to Supreme Court Justice Oliver Wendell Holmes's often misquoted statement, "The most stringent protection of free speech would not protect a man in falsely shouting fire in a theatre and causing a panic," in *Schenck v. United States* 249 U.S. 47 (1919). Under current US law, the limit against free speech is protected under the doctrine of *Brandenburg v. Ohio*, 395 U.S. 444 (1969) where inflammatory speech cannot be punished by the government unless it is directed to inciting or likely to incite imminent lawless action. Nevertheless, during the height of the 2007 subprime crisis one of the authors overheard a securitization lawyer say, "Ten lenders in jail in California for subprime malfeasance would be enough to put a stop to this rotten business at a national level."

parties, including the sponsor, the servicing entity that administers or services the financial assets and the trustee."[48]

Usually, the market literature regarding securitizations emphasizes the dramatically reduced credit risk of the SPV-issuer in comparison to the originator, which by implication should make the investment more attractive to the investor. Credit rating agencies are perhaps somewhat responsible, if not complicit, for this skewed perception. The argument that the credit risk of the SPV-issuer is much less than the originator, and therefore, the investment is much safer is somewhat of a *non-sequitur*.

The purpose of the credit rating exercise in a securitization structure is to ensure that the SPV-issuer achieves a *targeted* credit rating that would make it attractive to institutional investors. In many cases, the practice is to recommend sufficient or ample credit enhancement in favour of the SPV-issuer, which would then result in the SPV-issuer having a credit-rating higher than the originator's. This of course lends credence to the assertion that the transaction is financially well supported.

However, given the credit rating agency's power, knowledge and incentive to guide, and set benchmarks of credit risk in the transaction, the credit ratings themselves should be considered indicative of the risk of default only if they are relatively recent and read in the larger context of market disclosures. Whilst every prospectus may reveal the securities have achieved a particular credit rating, there is very little said to warn the investor that such ratings are susceptible to liquidity risk in the face of market volatility.

The goal of the regulatory disclosure regime, as we have stated above, should be to enable market participants to reduce the qualitative uncertainty of transactions. Whilst credit risk may be made transparent in the asset-backed securities transaction, liquidity risk remains persistently residual.

The disclosures which are most likely to help reduce the qualitative uncertainty of the investment to investors include information centring on two major risk areas: the transaction parties and the transaction agreements.

- Transaction parties[49]

Who are the parties responsible and liable for particular acts?

- Transaction agreements

What are the underlying rights and duties of the agreements underlying the securitization transaction?

[48] See, section on "Disclosure" at I.C., at 1509.

[49] US SEC Regulations S-K—Subpart 229.1100 Asset Backed Securities (Regulation AB) (May 2006) available at: http://www.sec.gov/about/forms/regs-k.pdf. See §229.1001(a)(3) (Item 1101) Definitions: "Identification of key parties to the transaction, such as servicers, trustees, depositors, sponsors, originators and providers of credit enhancement or other support, including a brief description of each such party's roles, responsibilities, background and experience." *Id* at 109.

At a fundamental level, the disclosures should help the investor determine who is liable in case there is transaction failure. Thus, the types of disclosures relating to transaction parties include their basic identification so that aside from judging their reputation risk, they may be contacted (served or subpoenaed) in case of litigation, and their particular relationship to the future cash flows of the transaction can be assessed so that their roles and responsibilities can be characterised from financial and legal perspectives.

The types of disclosures relating to the transaction agreements summarise the major terms of each agreement, and the potential financial and legal repercussions of a failure in the performance of the defaulting party, Under the US and EU laws, there are requirements to disclose the "material" transaction agreements[50] that are normally referred to by market participants as "support documentation,"[51] that is, supporting the validity of the prospectus by establishing the legal relationships between the various transaction parties.

These two categories can be further divided into sub-categories that identify the specific transaction parties and the specific types of transaction agreements. These can vary from transaction to transaction, but in general, the types of parties and agreements relating to an asset-backed security transaction are as follows:

- Transaction parties
  - Sponsors
  - Depositors
  - Issuers
  - Underwriters
  - Servicers
  - Trustees
  - Originators
  - Significant obligors of pooled assets
  - Government licensing authority

- Transaction agreements
  - Pooling and service agreement
  - Trustee services
  - Credit enhancement and liquidity support
  - Insurance and guaranty
  - Other agreements relating to essential risks of payment and delivery on underlying assets and asset backed securities

Regulatory definitions can be found for most of these transaction parties, and in some broad sense, their functional relationship to a typical asset-backed security transaction can be gleaned from these definitions. However, where the participants to the transaction play a material role to the transaction but are not defined

[50] See, US Final Rule Asset Backed Securities (2005), and EU Prospectus Directive 2003/71/EC and EU Prospectus Regulation (EC) No. 809/2004.

[51] Otherwise also known as the "deal bible".

explicitly by the regulations, such legal entities should be disclosed in the prospectus, otherwise the fundamental purpose of the disclosure regime would be defeated.[52]

Similarly, the same point can be made with regard to agreements which have a direct relevance to the calculation of the cash flows or the material risks of the transaction.[53] However, what constitutes "material items" is many times left to the discretion of the issuer to determine.[54] In effect, the materiality criterion is the legal term for the information required which will overcome dysfunctional asymmetry.

The problem of determining the relevant and material parties and agreements relates to the general problem of the complexity of the transaction. The trade-off between specifically defining *all material items* and what is practicable for setting humanly understandable documentation relates to finding the appropriate dividing line between standardized-mandatory and discretionary-voluntary disclosures. This problem would appear intractable if all material information should have to be disclosed under the binding of one document — a single prospectus.

The prospectus, theoretically, would have to cover not only the expected values of the transactions but also all the expected risks. We would suggest that a way out of this problem is already found in practice. That is, the disclosure process can divided into a two-step process where the standardized-mandatory disclosures help define the general characteristics of the transaction in a base prospectus or base set of filings, and that the specific risks of the transaction are defined in subsequent supplemental prospectuses and filings that are offerings of specific types of financial securities.[55] This two step process hails an important development in overcoming the dysfunctional asymmetry inherent in any market for asset-backed securities since it naturally separates the functions of the originator and the arranger. On the one hand, this two-step process enables originators or conduits of originators to source assets for portfolios which have generic cash flow character-

[52] See, 17 CFR 229.1100(d)(1) which states: "If the asset-backed securities transaction involves additional or intermediate parties not specifically identified in this Regulation AB, the disclosure required by this Regulation AB includes information to the extent material regarding any such party and its role, function and experience in relation to the asset-backed securities and the asset pool. Describe the material terms of any agreement with such party regarding the transaction, and file such agreement as an exhibit."

[53] *Ibid*.

[54] Amongst the many examples of disclosures where the materiality criterion is applied, see, under US laws relating to asset-backed securities: 17 CFR 229.1100(b)(6) on material information relating to delinquencies and loss; 1100(d)(1) disclosures to the extent material concerning additional or intermediate parties; 1100(e) relating to "any pertinent governmental, legal or regulatory or administrative matters and any pertinent tax matters, exchange controls, currency restrictions or other economic, fiscal, monetary or potential factors in the applicable home jurisdiction that could materially affect payments on, the performance of, or other matters relating to, the assets contained in the pool or the asset-backed securities." Under EU law, see the EU Prospectus Directive 2003/71/EC Art. 5.1: "the prospectus shall contain all information which, according to the particular nature of the issuer and of the securities admitted to trading on a regulated market, is necessary to enable investors to make an informed assessment of the assets and liabilities, financial position, profit and losses, and prospects of the issuer and of any guarantor; and of the rights attaching to such securities. This information shall be presented in an easily analysable and comprehensible form."

[55] See section below on "Shelf Registration".

istics, and on the other hand, enables specialist arrangers to structure securities which meet the specific risk appetites of investors with specific risk characteristics and priorities of payments.

In mature markets, the structuring process is based on laws which allow for the legal segregation of the underlying assets into a bankruptcy-remote vehicle (usually a trust) so that such assets cannot be made part of or consolidated with the insolvent company. The development of asset-backed markets is mirrored and many times driven by the types of issuing vehicles available in a particular jurisdiction. For example, in the U.S., the grantor trust is the basis for simple pass-through vehicles, where the certificate holders are deemed owners of the underlying collateral and entitled to a pro-rata share of the cash flow of the pool assets. The major restriction with grantor trusts is that principal payments cannot be accelerated in favour of any particular class of security holders. This relatively simple structure may be most useful to asset-classes which are relatively robust against prepayment risk in times of interest rate fluctuation, and thus, have been used mainly for automobile loans.[56]

However, in the development of the residential real estate mortgage markets, the most important issuing vehicle is the real estate mortgage investment conduit (REMIC) which enables the issuance of multiple-class securities backed by mortgages or real property not subject to tax at the trust or entity level so long as they are in compliance with the REMIC requirements as provided in the U.S. Tax Reform Act of 1986.[57] For countries looking to broaden and deepen their real estate mortgage markets, legislation does not need to necessarily mimic the structural features of REMIC, but the preferred trajectory of asset-backed securities related regulation should be towards a framework that allows for multiple-class, sequential-pay mortgage-backed securities, of which the two-step prospectus process is a built-in feature.

1.8 Goal of Asset-backed Securities Regulatory Architecture

Although the avowed purpose of asset-backed securities regulation is to protect the investor, we would suggest that the actual goal of asset-backed securities regulation should be to enable relatively illiquid assets found in one jurisdiction to become relatively liquid by legal transformation to the *largest investors* in other jurisdictions. The key here is that whilst investors exist in any jurisdiction, being able to access the pool of funds of the largest investors ensures that the cost of the transaction will be reduced and that the sellers of the asset-backed securities will receive the "best execution" price in the world. This will require disclosure rules and practices that meet the most rigorous requirements of jurisdictions where such investors reside. At the moment, considering the current state of the regulations of the Russian mortgage-backed securities, this goal may appear to be distant. However, it is important to distinguish what needs to be done as part of accomplishing a strategic goal that furthers the rapid development of the asset-backed securities markets and what is likely to be done if only the vested interests of banking intermediaries are protected.

[56] See, Davidson, A. Sanders, A., Wolff, L., and Ching, A. (2003) *Securitization, Structuring and Investment Analysis*, at 20.

[57] *Ibid* at 21.

As we shall see in the history of the asset-backed securities market below, disintermediation has been a crucial aspect in the development of the asset-backed markets. Ironically, it is the discipline of disintermediation that should reduce investment banking fees for costly non-transparent credit support and liquidity support agreements, and enable future Russian mortgage-backed securities to be treated by sophisticated institutional investors as "commoditized financial products". So long as this goal of developing a superhighway of commoditized issues to the largest institutional investors is kept in mind, we can begin to see what types of disclosures should become standardized.

1.9 From Standardization of Disclosures to Standard Documentation

The point of standardization is twofold: (1) achieving efficiency per transaction by reducing transaction costs and (2) achieving certainty in meaning relating to those elements and components of transactions which are in effect "boiler plate", that is, repeatable elements and components to all securitization transactions. Asset-backed securities disclosures should contribute to standardization in the second sense. However, the US in its description of its Final Rule on Asset-backed Securities (2005) criticizes the mindless repetition of boiler plate clauses that come from transaction agreements and states that this practice should be reduced.[58] The main reason for this criticism is that such repetition adds nothing to the meaning of long prospectus documentation. The question of what constitutes the absolutely necessary minimum disclosures to an asset-backed securities transaction is still open, although we are of the opinion that they will be items that define the legal relationships of the parties since these will in turn define the legal substance of the overall transaction.

In sum, the goal of the regulatory regime is to help overcome dysfunctional asymmetry, and achieve risk symmetry between the largest institutional investors and asset-backed securities sellers. The practical significance of standardization in the securitization markets, however, is to build bridges to the world's largest pools of liquidity.

[58] See, US Final Rule Asset-backed Securities (2005) at 1509.

2 SECURITIZATION

2.1 Brief history of securitization markets

USA

It is generally agreed that securitization, like other financial innovations, was invented in response to problems with traditional financial instruments. In the 1970s, U.S. banks and savings and loan associations were heavily dependent on balance sheet management and were neither considered to operate very efficiently, nor perform the functions of intermediation effectively in the US.[59]

The U.S. Department of Housing and Urban Development created one of the first transactions using a mortgage-backed security. In brief, the Government National Mortgage Association (GNMA—"Ginnie Mae"), guaranteed the first mortgage pass-through securities. These were relatively simple certificates that allowed the principal and interest payments on mortgages to "pass through" to investors.

Ginnie Mae was soon followed by Fannie Mae, a private corporation chartered by the federal government, along with Freddie Mac to promote homeownership by fostering a secondary market in home mortgages. After these initial transactions, US investment banks set up their own mortgage trading departments to deal in notes and securities issued by state agencies.

Growth in the pass-through market led to innovations especially as originators sought a broader MBS investor base. In response, Fannie Mae issued the first collateralized mortgage obligations (CMO) in 1983. More complicated than pass-throughs, CMOs redirect the cash flows of the issuing trust to create securities with different payment features.

The goal of CMOs was to overcome prepayment risk which was seen as the main obstacle to expanding demand for pass-throughs. Prepayment risk for MBS investors is the unexpected return of principal stemming from consumers who refinance the mortgages that back the securities. Homeowners are more likely to refinance mortgages when interest rates are falling. As this translates into prepayment of MBS principal, investors are often forced to reinvest the returned principal at a lower return. CMOs accommodate the preference of investors to lower prepayment risk with classes of securities that offer principal repayment at varying speeds. The various bond classes with various payment conditions are called tranches.[60]. Some tranches can be subordinate to other tranches and some CMOs may include 50 or more tranches. In the event of a default of the loans in the underlying securitization pool, investors in the subordinated ("junior") tranche would suffer loss before the unsubordinated ("senior") tranche.

[59] Frankel, T. (Spring 1998) "Cross-Border Securitization: Without Law, But Not Lawless." *8 Duke J. Comp. & Int'l L. 255.*

[60] Tranche comes from the French for "slice".

As part of the Tax Reform Act of 1986, Congress created the Real Estate Mortgage Investment Conduit (REMIC) to facilitate the issuance of CMOs. Today almost all U.S. CMOs are issued in the form of REMICs. In addition to varying maturities, REMICs can be issued with different risk characteristics. REMIC investors—in exchange for a higher coupon payment—can choose to take on greater credit risk. Along with a simplified tax treatment, these changes made the REMIC structure an indispensable feature of the MBS market. Fannie Mae and Freddie Mac are the largest issuers of this security.

The first asset-backed securities (ABS) date to 1985 when the Sperry Lease Finance Corporation created securities backed by its computer equipment leases.[61] Leases are similar to loans in that they involve predictable cash flows from lease payments made by the lessee. Sperry sold its rights to the lease payments to an SPV and interests in the SPV, in turn, were sold to investors through an underwriter.

Since then, the market has grown and evolved to include the securitization of a wide variety of asset classes, including auto loans, credit card receivables, home equity loans, manufactured housing loans, student loans and even future entertainment royalties.[62] Credit card receivables, auto and home-equity loans make up about 60 percent of all ABS[63] while manufactured housing loans, student loans and equipment leases comprise most of the rest. Meanwhile the industry continues to innovate, looking for new assets to securitize such as auto leases, small-business loans and "stranded cost recovery" ABS. The latter refers to bonds backed by fees which newly deregulated utilities have won authority to include in future billings as an offset of previous investment.[64]

Today, the US securitization market retains a global number one position in terms of depth of liquidity and market share.

European Union

While a specific form of securitization has been in existence in Danish and German mortgage markets[65] for more than 100 years, securitization in its modern sense emerged in Europe in the 1980s with the issuance of the first UK MBS. Since then the volume of ABS issuance has seen almost uninterrupted growth.[66] The introduction of EURO in January 1998 spurred the development of securitization markets. Starting from a

[61] Cameron L. Cowan Partner, Orrick, Herrington, and Sutcliffe, LLP (November 5, 2003) Notes from speech before the Subcommittee on Housing and Community Opportunity Subcommittee on Financial Institutions and Consumer Credit United States House of Representatives Hearing on Protecting Homeowners: Preventing Abusive Lending While Preserving Access to Credit, available at http://financialservices.house.gov/media/pdf/110503cc.pdf

[62] *Ibid*.

[63] *Ibid*.

[64] *Ibid*.

[65] Rouwenhorst, K. G. (Dec 12, 2004) "The Origins of Mutual Funds" (December 12, 2004) Yale ICF Working Paper No. 04-48, available at: SSRN http://ssrn.com/abstract=636146.

[66] First half of 2003.

relatively flat base in 1998, the market grew by 55% in 1999, 36% in 2000 and 55% in 2001. By 2007, the volume of securitization issuance hit a new record with EURO 458.9 billion issued.[67]

Europe has become the second largest securitization market in the world, with significant developments in a number of innovative asset-classes. One of the main features distinguishing the EU from US markets is that in the EU, originators and issuers face a host of regulatory impediments due to the fragmentation of the legal regimes on the EU countries.

In response to the desire to realize the economic benefits of securitization, the EU has undertaken significant regulatory reform, with the majority of European member states adopting specific laws enabling the securitization of receivables.

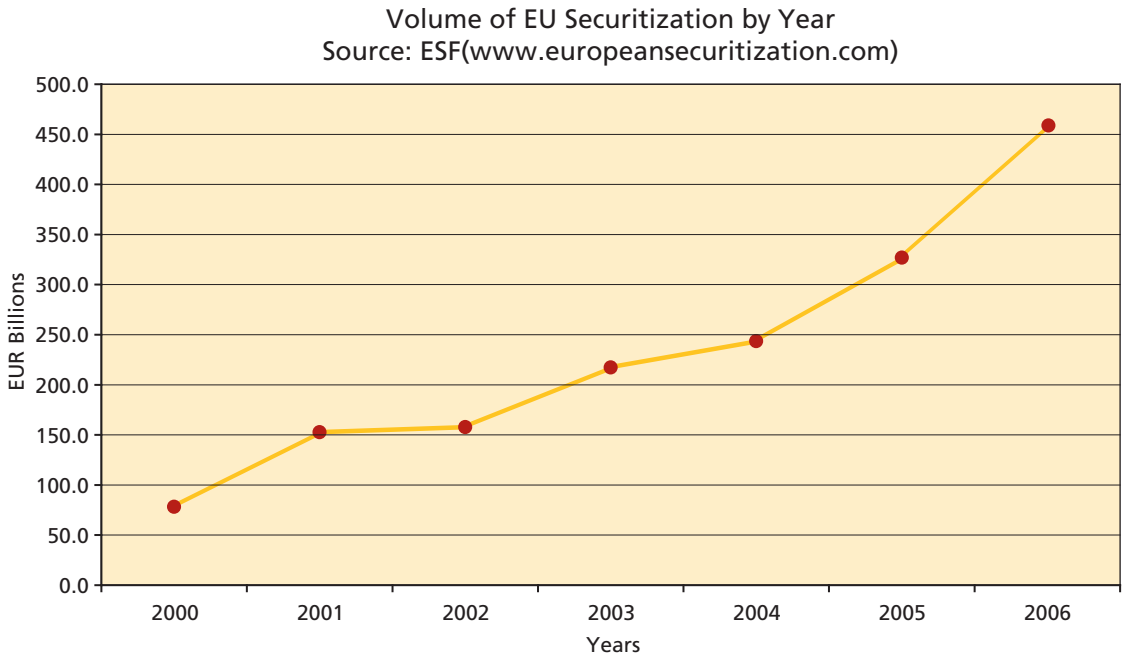
Table 1: Enactment of European Securitization Laws by Member States

1988:	France First European Securitization Law
1990:	Belgian Securitization Law
1992:	Spanish Securitization Law
1999:	Italian and Portuguese Securitization Law
2003:	Greek Securitization Law
2004:	Luxembourg Securitization Law

Table 2: Firsts in European Securitization Transactions

1985:	UK transaction
1995:	Irish transaction
1996:	UK non-conforming transaction
1996:	Dutch fixed rate pass-through
1999:	UK multi-currency transaction
2000:	Italian transaction
2000:	UK buy-to-let transaction and UK Master Trust Structure
2004:	Irish non-conforming transaction
2006:	Dutch master trust structure

[67] ESF (Winter 2007) Securitization Data Report , available at: http://europeansecuritization.com/ESFDataTEMPLATEv-2FINAL.pdf.



Russia

The first securitization transaction in Russia occurred in 2004 and was backed by Diversified Payments Rights (DPR). The DPR structure was used because it was considered the most effective solution to the extenuating legal uncertainties and regulatory environment. Despite the promulgation of the mortgage backed securities law in November 2003 which was aimed primarily at establishing the enabling environment for domestic transactions, there were no market issues until 2006. In that year, VTB, a state-owned bank, issued the first Russian MBS for a total amount of 88.0 mln USD divided into 3 tranches.[68] 2006 proved to be a breakthrough year for Russian securitization market, showing a 17-fold growth in value with 12 transactions across a number of different asset classes.[69] According to Moody's, the Russian market plays a leading role in setting the direction and trends in the securitization markets of the emerging markets.

However, as of mid-2007, the Russian market for asset-backed securities is in an early and difficult stage of transition. The Russian legal environment is fraught with many implicit impediments to the rapid development of wholly domestic securitization transactions. Most of the transactions are undertaken through cross-border SPV's which normally requires enlarged volumes of assets being securitized. Most transactions so far have benefited very large commercial entities. Therefore, one of the important economic benefits of

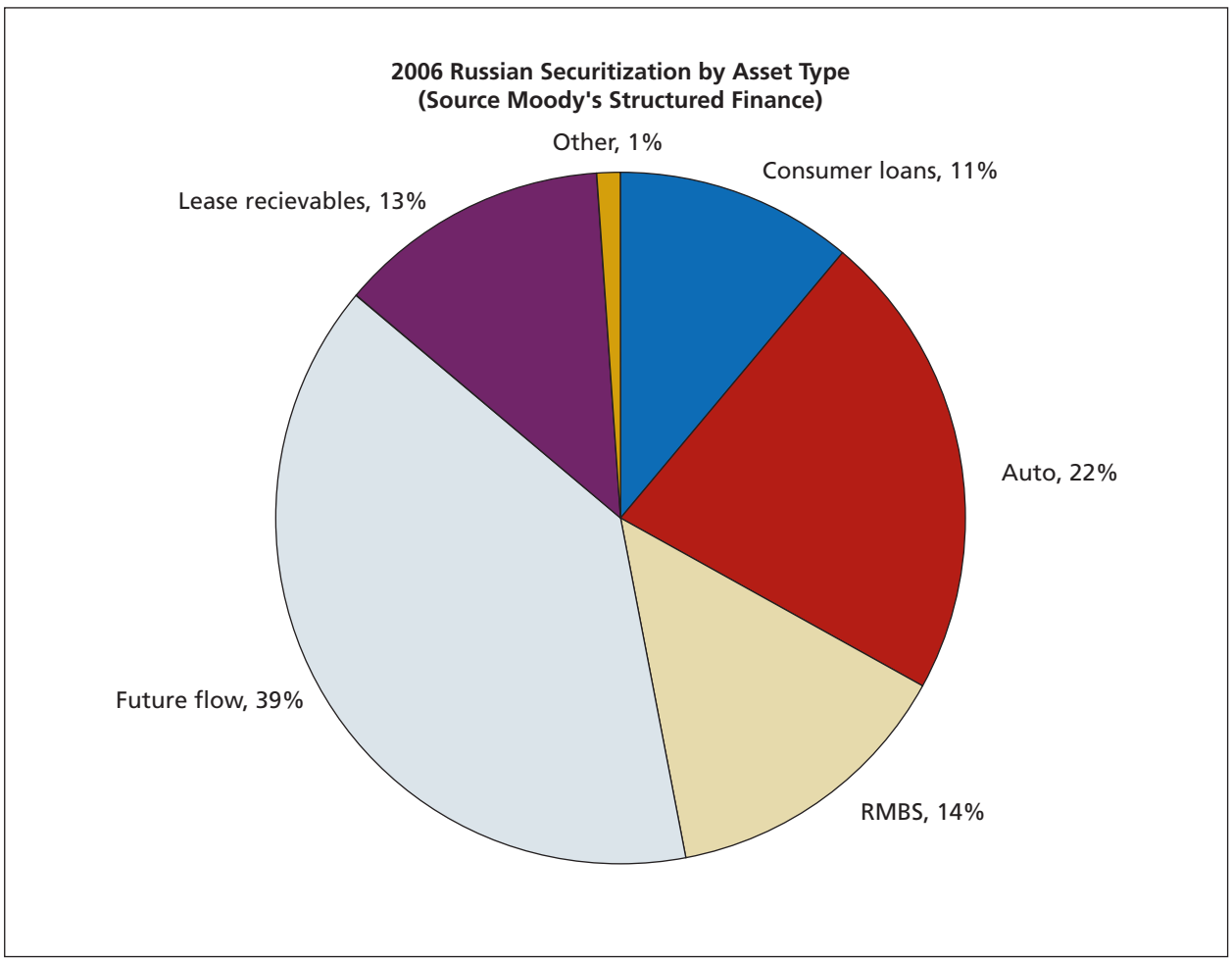
[68] MOODY'S Investor Service (8 June 2006) Pre-sale Report: Russian Mortgage Backed Securities 2006-1 S.A.

[69] MOODY'S Investor Service (22 January 2007) "EMEA New Markets Structured Finance: Record Issuance in 2006 While Further Growth and Asset Class Diversification Expected for 2007," Structured Finance Research.

securitization, namely, providing businesses that normally could not easily raise capital through traditional bank facilities access to the capital markets, has yet to be achieved.[70]

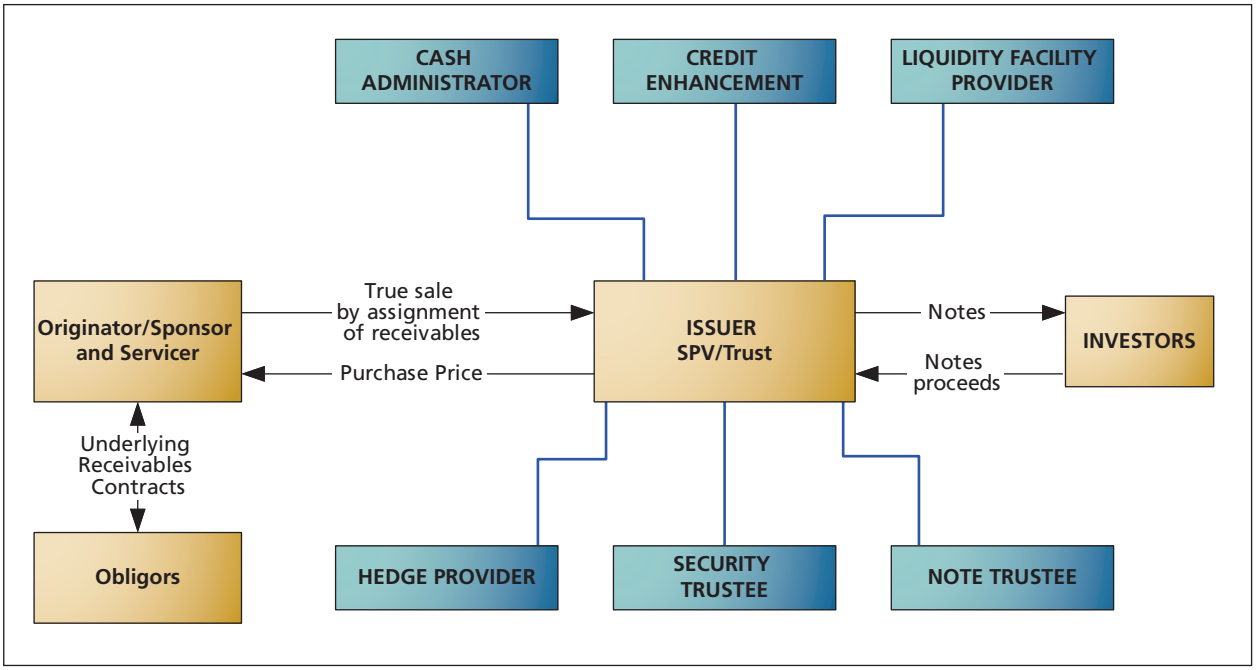
By the end of 2006, the Government prepared a set of amendments to the existing legislation with the aim of removing obstacles to securitization. It is expected that these amendments will promote the development of ABS markets in Russia. One of the fundamental aspects of any legal regime concerning ABS is that functional roles and responsibilities of the transaction parties are defined.

EMEA New Markets Structured Finance:
Record Issuance in 2006 While Further Growth and Asset Class Diversification Expected for 2007



[70] See, Schwarcz, S.L. (1993) "The Parts are Greater Than the Whole: How Securitization of Divisible Interests Can Revolutionize Structured Finance and Open the Capital Markets to Middle-Market Companies," *Columbia Business Law Review*, Vol. 1993, at 139, available at SSRN: http://ssrn.com/abstract=868532

Figure 1: Traditional Asset-backed Financing Structures
Classic Securitization Via True Sale



2.2 Definition of major parties

In this section, we set out definitions of the major parties to typical asset-backed securitization transactions. From a legal perspective, the definition of the functional roles and responsibilities of each of these parties are important for the investor to understand, not least because the performance of these parties affect the value of the transaction and are therefore considered major risk items. The reputation and competence of the parties form part of the risk assessment in determining whether the parties have the capability of fulfilling their duties as per the transaction agreements.

One of the initial difficulties with securitization structures is understanding the meaning of the various labels given to specific parties, the specific functions required of each party, and the somewhat overlapping nature of some of the labels. There is no international standard regarding the meaning of the various labels given to parties, although the International Accounting Standards have published distinctions regarding consolidation and the treatment of special purpose entities and variable interest entities.[71] Thus, it is impor-

[71] See, Gololobov, D. and Tanega, J. "Sham SPEs, Part I: The Legal Issues of International Accounting Standards on the Consolidation of Special Purpose Entities," **International Company and Commercial Law Review,** Vol. 17, Issue 11, at 304-317, Nov. 2006; and Gololobov, D. and Tanega, J. on "Sham SPEs, Part II: The Regulatory Gaps of International Accounting Standards Concerning the Consolidation of Special Purpose Entities," **International Company and Commercial Law Review,** accepted for publication in Vol. 17, Issue 12, at 369-380, Dec. 2006.

tant in the first instance to determine what a particular party's role and duties are in the overall transaction despite whatever label is given. The roles and responsibilities of each party define the legal relationships amongst the parties and therefore, together with the transaction agreements, define the legal substance of the entire transaction.

Our position is that the legal substance of the agreement circumscribes the ultimate economic value of the transaction. We briefly review the roles of each major transaction party in turn.

Issuer

The issuing entity, the *Issuer*, is a legal entity that has the reporting obligation to a relevant regulatory authority and has the legal duty to disclose all material facts and risks to investors.[72] The issuer is usually set up in the form of a *Special Purpose Vehicle* (*SPV*) in a jurisdiction which allows for the implementation of the bankruptcy remote principle (where the title, interests and rights to the assets' cash flows are transferred to a bankruptcy remote vehicle), the security arrangements are provided for the benefit of investors, and the favourable tax treatment to investors.

Two types of SPVs are many times used. One SPV is used to effect the bankruptcy remote principle and ensure that the title and rights to the cash flows of the assets are transferred to a "Purchasing SPV".

Another SPV which receives the title and rights of the assets from the Purchasing SPV is used to effect the issuance of the notes to investors and is designated as the "Issuing SPV" or "Issuer". The legal definition of an issuing *SPV* is specified in the jurisdiction where it is established and will need to be recognized as a legal entity in the jurisdiction in which it issues securities. Special types of corporate form have been established in various jurisdictions to accommodate asset-backed securitization structures—see Luxembourg[73] and Jersey[74] laws relating to "Cell Companies".

Another vehicle of convenience is the trust, which allows for the separation of legal title and beneficial interests. The legal title of the assets is held by the Trustee, and the beneficial interests to the trust's estate are sold in the form of asset-backed securities to investors. The major objectives of the *Issuer* are usually limited to passively owning or holding the pool of assets (e.g. the "Purchasing SPV") and issuing the asset-backed securities (e.g. "Issuing SPV") supported or serviced by those assets, and other activities of the Issuer are those reasonably related to accomplishing these objectives.[75]

---

[72] See, US 17 CFR §17 CFR 1101(b); Regulation AB, Item 1101(b).

[73] For Luxembourg laws relating to protected cell companies, see Rutsaert, Q. (2007) "Protected Cell Companies – A New Trend in the Securitisation Industry Analysed From a Luxembourg and International Perspective," Journal of International Banking Law and Regulation, at 1 – 8.

[74] For Jersey laws on "The jersey Protected Cell Company" and the "Incorporated Cell Company (ICC)", see The Companies (Jersey) Law 2005 (Amendment No. 8), which came into effect on February 1, 2006.

[75] See, US SEC Regulation AB , Item 1101(c)(2)(ii).

Originator, Sponsor, Seller or Transferor

These names refer equally to the party who intends to sell and securitize a portfolio of assets. In cash flow based transactions, the *Originator* removes assets from its balance sheet through a "true sale" operation. The Sponsor[76] is the legal entity[77] that organizes[78] and initiates[79] an asset-backed securities transaction by selling and transferring assets,[80] either directly or indirectly including through an affiliate, to the Issuer.[81] In some instances, the transfer of assets occurs in two steps: first, the financial assets are transferred by the sponsor to an intermediate entity, often a special purpose entity created by the sponsor for a securitization program and commonly called a *Depositor*, and second, the *Depositor* will transfer the assets to the Issuer for the particular asset-backed transaction.[82] If there is not a two-step transfer, the terms "sponsor" and "depositor" are used interchangeably in the markets.[83]

Investors

Typically, the large institutional investors are the targeted investor base for placement of commercial paper (CP) or asset-backed commercial paper (ABCP) and for the distribution of asset backed securities (ABS). It is often considered that the size and complexity of these issues and the nominal value of the notes make these securities unsuitable for retail investors in many transactions. For public issues, the prospectus and information memorandum are meant to disclose all material risks to the investors.

---

76 "While "sponsor" is a commonly used term for the entity that initiates the asset-backed securities transaction, the terms "seller" or "originator" also are often used in the market. However …in some instances the sponsor is not the originator of the financial assets but has purchased them in the secondary market." US SEC (Jan 2005) Final Rule Asset-backed Securities, note 46, at 21.

77 "Sponsors of asset-backed securities often include banks, mortgage companies, finance companies, investment banks and other entities that originate or acquire and package financial assets for resale as asset-backed securities." US SEC (Jan 2005) Final Rule Asset-backed Securities, II., at 21.

78 "The structure of asset-backed securities is intended, among other things, to insulate asset-backed securities investors from the corporate credit risk of the sponsor that originated or acquired the financial assets." US SEC (Jan 2005) Final Rule Asset-backed Securities, I.A., at 8.

79 "A sponsor typically initiates a securitization transaction by selling or pledging to a specifically created issuing entity a group of financial assets that the sponsor either has originated itself or has purchased in the secondary market." US SEC (Jan 2005) Final Rule Asset-backed Securities, II., at 22.

80 "In a basic securitization structure, an entity, often a financial institution and commonly known as a "sponsor," originates or otherwise acquires a pool of financial assets, such as mortgage loans, either directly or though an affiliate. It then sells the financial assets, again either directly or through an affiliate, to a specially created investment vehicle that issues securities "backed" or supported by those financial assets, which securities are "asset-backed securities."" US SEC (Jan 2005) Final Rule Asset-backed Securities, I.A., at 10.

81 See, US SEC (Jan 2005) Final Rule Asset-backed Securities, III.B.3.a., at 110.

82 See, US SEC (Jan 2005) Final Rule Asset-backed Securities, II., at 22.

83 *Id*, note 47, at 23.

The prospectus, information memorandum and supporting transaction documentation are poured over by the law firm representing the lead manager to determine and ensure conformity of the documents to listing and disclosure requirements. Credit rating agencies also analyse these documents, and in many instances, provide advice on what would constitute the appropriate legal structures to meet targeted credit ratings for particular issues and tranches.[84]

Servicer

The term Servicer refers to any legal entity responsible for the management or collection of the pool assets or making allocations or distributions to holders of the asset-backed securities.[85] Prior to the transfer of title (true sale) of the assets, normally the originator plays a servicing function. However, when the true sale takes effect, the Issuer normally engages the originator in a service agreement whereby the originator is contracted to perform the servicing function. Parts of this servicing function might be outsourced to other servicers, such as a super-servicer which having economies of scale can provide an efficient service at a reduced cost.

Thus, under the US Regulation AB, the disclosure item relating to the Servicer requires information regarding the *entire* servicing function, including a clear introductory description of the roles, responsibilities and oversight requirements of the entire servicing process and the parties involved.[86] The term Servicer does not include a Trustee for the Issuer or the asset-backed securities that makes allocations or distributions to holders of the asset-backed securities if the Trustee receives such allocations or distributions from a Servicer and the Trustee does not otherwise perform the functions of a Servicer.[87]

---

[84] See BIS, "Credit ratings and complementary sources of credit quality information" Publication No.3 (August, 2000), available at http://www.bis.org/publ/bcbs_wp3.htm.

[85] See, 17 CFR §229.1101(j), Regulation AB Item 1101(j). The US SEC's takes a broad definition of servicer. It states that its "…definition of "servicer" is designed to capture the entire spectrum of activity to include both collection and asset maintenance activities as well as cash flow allocation and distribution functions for the ABS. This includes parties often referred to as "administrators." SEC (Jan 2005) Final Rule Asset-backed Securities, III.B.3.d., at 1601. "The role of the servicer is often not limited to administration and collection of the pool assets. The servicer often also is the primary party responsible for calculating the flow of funds for the transaction, preparing distribution reports and disbursing funds to the trustee who in turn uses the allocations provided by the servicer to distribute funds to security holders. We also recognize that in many transactions, multiple entities are used to perform different serving functions. For example, while the particular division of responsibilities may vary by transaction or asset class, an ABS transaction may involved one or more entities, sometimes called "master servicers," that oversee the actions of other servicers and may perform the allocation and distribution function. Different servicers, sometimes called "primary servicers," may be responsible for primary contact with obligors and collection efforts. In addition, one or more other servicers, sometimes called "special servicers," may exist for specific servicing functions, such as borrower work-out or foreclosure functions. The allocation and distribution functions may be with a separate entity, sometimes called an "administrator." While some servicers may be affiliated with the sponsor, other non-affiliated sub-servicers may be employed." (SEC (Jan 2005) Final Rule Asset-backed Securities, III.B.3.d.)

[86] "In addition to an appropriate narrative discussion of the allocation of servicing responsibilities, registrants also should consider presenting the information graphically if doing so will aid understanding." *Id* at Note 223 at 1536.

[87] *Id* at 1535

Obligors

Obligors cover the parties ranging from individual consumers to highly rated corporates making payments on the underlying assets being securitised. These expected payments streams are the future cash flows which are meant to service the securitization transaction and from which investors are repaid. Obligors in some jurisdictions where no securitization laws have been enacted may have certain personal rights of notification and rights to approval which are condition precedent to a transfer of obligors' payment stream to third parties. Changes in law allowing for simple notification to the obligors without the obligors' approval of the securitization transaction are important first steps in the development of an efficient securitization legal regime.

Lead manager

The lead manager is usually an investment bank that advises the seller on the structuring of a transaction and liaises with other parties involved in the transaction such as rating agencies, lawyers and credit enhancers. Where the transaction involves a public issuance of ABS or MBS, that role will also include the lead managing of the issue of securities. The lead manager is responsible for advising on the pricing, the underwriting and the allocation of the securities issued to a group of selling banks and accepts securities law responsibilities as to the compliance of the issuance with relevant securities law and regulation.

Liquidity Facility Provider

A liquidity provider typically provides a liquidity facility[88] which will provide a funding source to a securitization transaction to meet timely payments of interest and principal under the securities to the extent that there is a temporary shortfall in revenue available from the assets. Unlike credit enhancement, any drawings under the facility will become a senior obligation of the issuer ranking at least *pari passu* with the relevant securities. The types of liquidity facilities will vary according to the type of liquidity risk implied by the security. For example, in the ABCP market, they will cover disruption in the ABCP market, or where the structure requires a currency swap then they may cover currency mismatches between the assets and the ABCP itself.

Trustee

The trustee is appointed to act on behalf of the investors in a securitization transaction and is, therefore, entrusted with reaching certain key decisions which may arise during the life of the transaction. The trustee is usually established in the form of a specialist trust corporation or part of a bank which specialises in providing this service. The role of the trustee may also include holding security over the securitised assets and control over cash flows. It is often a requirement of listing asset-backed securities that an independent trustee is appointed. Trustees receive regular reports on the performance of the transaction in order to check whether, for instance, cash flow collection and distribution procedures are being complied with during the life of the deal. Typically, these reports are also distributed to the rating agencies.

Subject to appropriate indemnity and other protections, trustees are normally legally responsible for finding a replacement servicer when necessary, taking up legal proceedings on behalf of the investors and, as the case

[88] See, US SEC Regulation AB, §229.1114(a)(2).

may be, for selling the assets in order to repay investors. To enable the trustee to perform its duties and to provide adequate remuneration, the trustee receives fee payments that are senior to all other expenses and holds a senior ranking cost indemnity to cover all unexpected costs and expenses.

Paying agent

The paying agent is a bank of international standing and reputation, and is responsible for making payments on the securities to the investors. Payment is usually made *via* a clearing system with the main clearing systems in Europe being Clearstream and Euroclear). In Europe this role is often assumed by an entity affiliated to the trustee or the administrator but, unlike the practice in the United States, is not considered to be a role of the trustee itself.

Swap provider

Swaps are often used in securitizations to hedge mismatches between the assets and the relevant security. Such mismatches may relate to interest type, currency or tenor or a combination thereof. Since the swap counterparty is entering into a transaction with an SPV, it has no recourse of any value in the event of default or under certain events relating to non-commercial risks in the transaction (*e.g.* imposition of withholding tax) beyond the assets securing the securities. Losses which are not made good ahead of the investors may result in lower credit rating. Complex rules are required to be observed to produce rating compliant swaps both as to documentation issues and also swap counterparty rating.

Administrator

In commercial paper (CP) or asset-backed commercial paper (ABCP) conduit based transactions, or where a special purpose vehicle (SPV) is used in a securitization structure, an administrator will be responsible for managing the conduit or the SPV. This may include maintaining the conduit's or the SPV's bank accounts in which payments are made from the underlying assets and to the investors. The administrator will also have the duty of monitoring the performance of the assets as well as providing other corporate services, including corporate governance.

Rating agencies

There are three main rating agencies operating in Europe: Fitch Ratings Ltd (Fitch), Moody's Investors Service Limited (Moody's) and Standard & Poor's Ratings Group (Standard and Poor's). The role of the rating agencies is to provide investors with an independent opinion on the creditworthiness of a debt instrument, such opinion expressed through a standard matrix of rating levels identified by way of symbols. By providing a credit rating, the credit rating agency arguably helps overcome the dysfunctional information asymmetry and credentializes the transparency of the transaction. Essentially their role benefits the investor, and should, at least theoretically, reduce regulatory cost. It is usually made clear in any offering document that the rating is not intended to be a recommendation to buy or sell. The rating will address the likelihood that a debt instrument will pay timely interest and repay principal in full according to its terms and conditions. Although the structuring bank will have performed its own due diligence, rating agencies will conduct their own independent review of the entire transaction covering asset, legal and credit risks related issues. On a periodic basis,

the rating agencies will undertake surveillance of closed transactions during the lifetime of the transactions. During market downturns, credit rating agencies are publicly criticized and blamed for encouraging market bubbles by having conflict of interests. The U.S. regulation of credit rating agencies as of June 2007[89] is too recent to see how it may affect their behaviour in the ABS markets.

Regulators

Regulators (*i.e.* the bank and finance commission or any similar regulatory body) are concerned mainly with four aspects of securitization:

- *Allocation of capital*
  Where the availability of the liquidity facility protects the conduit against a deterioration of the quality of the securitised assets, particularly in ABCP conduits sponsored by banks which provide liquidity facilities to cover all or part of the risks, and where regulators determine the required weighting of these facilities on the books of the financial institution. These facilities usually have a maturity of up to 364 days and only cover market risk, and therefore no capital is charged against the risk taken;

- *Transfer of credit risk*
  This concerns the legal transfer of part of the credit risk of a portfolio of bank loans, bonds or other debt obligations through the use of synthetic securitization (*i.e.* CDO's) involving derivative products (*i.e.* credit default swaps). Here regulators are particularly interested in the actual transfer of credit risk to third parties and the release of regulatory capital, as well as in the creation of economic capital;

- *Approval of offering circular*
  This is the approval of the offering circular sent to investors in the case of public transactions; and

- *Capital requirement for ABS*
  This is the determination of the capital requirement for ABS bought by investors.

From an international banking perspective, the measures which have become standard through regulatory implementation throughout the world are based on the "securitization framework" found in Basel II.[90]

Structuring Bank or Arranger

The structuring bank, often referred to as the arranger, is responsible for co-ordinating the whole transaction with respect to the originator-client, the law firms, the rating agencies and other third parties. Generally, the

[89] See SEC, 17 CFR, parts 240 and 249b "Oversight of Credit Rating Agencies Registered as Nationally Recognized Statistical Rating Organizations" at http://www.sec.gov/divisions/marketreg/ratingagency.htm.

[90] Basel Committee on Banking Supervision (June 2006) *International Convergence of Capital Measurement and Capital Standards, A Revised Comprehensive Framework*, "IV. Credit Risk – Securitization Framework," available at: http://www.bis.org/publ/bcbs128.pdf

structuring bank will perform a due diligence exercise in respect of the envisaged structure including the legal aspects of the documentation, which also must take into account all accounting and tax issues.

The structuring bank is responsible for performing a due diligence exercise in respect of the assets to be securitised and on the capacity of the servicer. This function includes the identification of historical information as well as an asset audit. In case of a public issue, the structuring bank is also responsible for an information memorandum or prospectus for investors and for the accuracy of details provided to the rating agencies in support of their work.

The structuring bank is responsible for ensuring that each transaction complies with local regulatory requirements and obtaining approvals required by any relevant bank commission or listing authority.

Auditors

For securitization transactions aiming at off-balance sheet treatment under relevant Generally Accepted Accounting Principles (GAAP), the auditors of the originator will be requested to issue a de-consolidation opinion under relevant GAAP. Relevant GAAP for securitization transactions in Europe will typically include one or more of local GAAP reporting vehicles of the originator as well as some comparative adjustments relating the differences to International Accounting Standards (IAS) and US GAAP.

Auditors are often also required to undertake levels of asset due diligence, especially in relation to public transactions. Audit opinions may also be required by regulators in respect of transactions seeking regulatory off-balance sheet treatment.

Law firms

Market practice in Europe generally requires two sets of law firms to work on a transaction: the lawyers for the issuing entity such as the structuring bank, lead manager or trustee and the lawyers for the originator or seller of the assets. Law firms are invited to bid on drafting and reviewing the transaction documentation covering all structuring and funding aspects of a transaction. For public issues, the law firms will also draft the offering circular to the investors.

Law firms are also asked to provide legal opinions on various topics such as: "true sale" issues, perfection of security or ownership interest (in future receivables), and enforceability, as well as regulatory issues, if any. Whilst these opinions will almost never be couched in terms of legal certainty, they will typically need to provide levels of comfort sufficient to support the rating agency analysis of the transaction.

Traders and Sales Team

A trader or dealer buys and sells the securities generated by an offering. In securitization transactions, the securities are mainly in the form of notes secured by the underlying assets. The trader/dealer quotes both a bid and offer price for securities to clients and other counterparties on request. Institutional salespeople are responsible for building profitable relationships with large investing clients. They must have a clear understanding of

their client's investment parameters, risk appetite and, if possible, portfolio holdings. Salespeople maintain an ongoing dialogue with their trading colleagues. They also help colleagues in the primary markets - origination and syndication - assess investor appetite for specific issues.

Underwriter

The underwriter, usually a bank or a pool of banks, commits to purchase the whole issue amount of an ABS/MBS at a specified price. This gives the issuer certainty over the placement and proceeds of the securitization by transferring market risk to the underwriter for which it charges an underwriting fee.

2.3 Economic benefits of securitization for originator and investor

Originators

Securitization is increasingly becoming a popular funding instrument for commercial entities. The benefits gained through securitization to both the seller of the receivables (originator or sponsor) and the investors in the securities are making this instrument increasingly attractive. Moreover, one distinctive feature of cross-border securitizations is that a company may establish an SPV in a foreign jurisdiction and float securities in that country's capital markets enabling the company to generate funds at a cost lower than if it had tried to raise capital directly from this same foreign country.[91] This is a key benefit for originators (companies) from emerging economies. Securitization offers companies opportunities to develop expertise in parts of the process, or draw on expertise available in the global markets.

Similarly, the process offers interested parties opportunities to structure transactions in locations around the world that provide a receptive legal environment, and avoid those with restrictive and costly regulatory regimes. Further, cross-border securitization allows for credit enhancement mechanisms that effectively lower the cost of capital and thus, lower the barrier to entry for potential market participants.[92] As arrangers of cross-border securitization transactions search globally for countries where the originator can raise securitized funds in a cost-effective manner with some sense of legal certainty, numerous factors influence their decision of whether a particular jurisdiction is suitable for securitization, such as whether regulations for investor protection are overly lax or restrictive, the tax burden versus benefits, the amenities available, political stability, the breadth and depth of the local institutional investors and the market history relating to the underlying pool asset quality.

One of the lessons of the sub prime crisis of 2007 is that it is actually a repeat of history since the first crash of the sub prime market occurred in 1998 when a wave of forced write downs began with Aames Financial Corporation in 1998 and the bankruptcy of Southern Pacific Financial Corporation in October 1998. The deteriorating quality of the underlying collateral in mortgage-backed securities forced the top ten sub prime

[91] Dasgupta, P. (Summer, 2004). "Securitization: Crossing Borders and Heading Towards Globalization." *27 Suffolk Transnat'l L. Rev. 243.*

[92] *Ibid.*

lenders of 1997 to either go into bankruptcy or become acquired by other lenders.[93] For cross-border securitizations, it is hypothesized that the highest quality ("prime") assets are likely to be securitized ahead of lesser quality collateral. If these factors together form a favourable environment to the originator, then local securitization markets are likely to prosper.

Whilst the local environment may be conducive to securitization, there are various factors influencing a particular originator's decision to undertake a securitization transaction.

- Reducing financiers information costs
  Due to the specifics of its transactions structure, securitization helps firms overcome the dysfunctional asymmetry or "lemons" problem.94 Numerous types of third party consultants engaged in the preparation of the transaction appraise the state of assets and the company itself, providing pertinent information with enhanced efficiency and effectiveness to investors. The techniques for such appraisals have been developed over the course of years and provide a level of comfort and credibility to investors.

- Strategic profile and leveraging effect
  Unknown and new companies can use securitization transactions also as an effective tool to enter the capital markets, which are often restrictive and difficult to prise for new participants. Securitizations provide an alternative to bank financing and are one of the continuing factors in the dis-intermediation of the banking sector, causing more and more commoditization of financial products and resulting in more leverage for participating companies. Of course, if the underlying assets are forced to be re-valued at lower levels, then the effect of de-leveraging will have a negative impact on the value of the asset-backed securities in the secondary market.

- Efficient financing though subject to market volatility
  The fact that securitization allows certain assets to be legally detached from other originator or sponsor assets entails a symmetric detachment of the risk of the securitized assets from the other risks of the originator. Thus, the companies with a poor credit history or lower rating grade can generate and sell assets at a higher investment rating, i.e. higher price. Of course, these means there is a corresponding higher risk of market volatility for such instruments.[95]

---

[93] Davidson *et al* (2003) at 328.

[94] See, Claire A. Hill (Winter, 1996). "Securitization: a low-cost sweetener for lemons", *74 Wash. U. L. Q. 1061* Firms engaging in financing transactions, like firms engaging in most any transaction, suffer from the well-known "lemons" problem.116 The borrower (in this case, the seller of the receivables) knows more about the firm than the lender (in this case, the buyer of pool securities) does, and has an incentive to exaggerate the firm's quality. The lender knows this, and offers the borrower only a "lemons" price based on her worst-case estimate. The borrower can get the lender to offer more only if the borrower can convince the lender that the borrower is not a "lemon." Some firms have more severe lemons problems than others: The financial community - that is, the community of prospective financiers - has insufficient information to appraise such firms' prospects or their potential liabilities, and cannot learn more without incurring considerable expense.

[95] See, comments above on sub prime markets 1998 and 2007.

- Return on capital (balance sheet structure)
  Securitization can enhance managerial control over the size and structure of a firm's balance sheet. For example, from an accounting perspective, de-recognition of assets (i.e., removal from the balance sheet) can improve gearing ratios as well as other measures of economic performance (e.g., return on equity). Financial institutions also use securitization to achieve capital adequacy targets.[96] In cases where the originator is a regulated entity for capital adequacy purposes, securitization allows finance to be raised which is off the regulatory balance sheet. Since the essence of the transaction is to replace receivables with cash, the result is a zero risk weighting for capital adequacy purposes.

  Consequently, the originator can release capital that would otherwise have to be held against the risk of default on the assets. Securitization also releases capital for other investment opportunities. This may generate economic gains if external borrowing sources are constrained, or if there are differences between internal and external financing costs.

- Better risk management
  Securitization often reduces funding risk by diversifying funding sources. Financial institutions also use securitization to eliminate interest rate mismatches. For example, banks can offer long-term fixed rate financing without significant risk, by passing the interest rate and other market risk to investors seeking long-term fixed rate assets. Securitization has also enabled some organizations, particularly banks, to remove impaired assets from their balance sheets. Again, this is often done in the case of insolvency or to meet capital adequacy requirements.

  Securitization is fundamentally a risk management tool that links illiquid assets to volatile markets. It enables corporations to separate commercial and business risks from the risks associated with financing their operations. In terms of financing risks, securitization enables private sector companies to shed funding risk, by making new sources of funding available, as well as reducing interest rate and foreign exchange risk.

- Flexibility
  Securitization also benefits the financial institution or corporation that originates the securitized asset. Without securitization, a bank making a home loan usually would hold that loan on its books, recognizing revenue as payments made over time. To realize the value of the loan immediately, the bank can sell the whole loan to another institution, though this is generally not economical unless the loan is very large. The more efficient option is to pool similar loans together, as discussed above, and enter into a securitization transaction.

  The process makes even more sense for originators with assets considered illiquid, such as equipment leases or the balance due on a credit card. The latter comprises an asset class called credit card receiv-

[96] See, Basel II, *supra*.

ables that account for approximately 20 percent of outstanding ABS.[97] Similar to banks securitizing home loans, credit card companies are able to use the securitization process to provide more credit and manage their balance sheets.

- Fine-tuning administrative systems
  For new companies, the analysis and discipline of testing the administrative systems from a securitisation perspective, including day to day procedures, means that the company would be better prepared for the securitization transaction. This may also mean that the company would have an enhanced understanding of what types of actions would be necessary in order to achieve enhanced efficiencies and understand how to better achieve targeted credit ratings.

Economic Benefits to Investor

Although the major beneficiary in sale-purchase transactions in most cases is the seller, ABS are attractive and beneficial to investors for the following reasons:

- Portfolio Optimization
  Through ABS, investors can invest in the asset classes and risk tranches of their choice targeting specific associated returns. This offers investors the opportunity to optimize the structure of their portfolios and access markets which they could not otherwise invest.

- Stability
  With the exception to the sub prime, ABS have historically often been less volatile as compared to corporate bonds; and

- Higher Yield
  ABS have been known to offer a yield premium over comparably rated government, bank and corporate bonds.

- Less risky
  Due to the homogeneity of the asset portfolio, where single assets are relatively replaceable with comparable assets, ABS are usually not susceptible to event risk or the risk of a rating downgrade of a single borrower.

Given the general characterization of asset backed securities as major financial instruments that support the capital efficiency of corporations and financial institutions offering a more complete set of financial instruments to the capital markets, we turn now to a discussion of securitization laws. Although this is a complex

[97] Cameron L. Cowan Partner, Orrick, Herrington, and Sutcliffe, LLP (November 5, 2003) Notes from speech before the Subcommittee on Housing and Community Opportunity Subcommittee on Financial Institutions and Consumer Credit United States House of Representatives Hearing on Protecting Homeowners: Preventing Abusive Lending While Preserving Access to Credit., available at http://financialservices.house.gov/media/pdf/110503cc.pdf.

topic, the legal framework is fundamental to the construction of securitization transactions that are credible to institutional investors.

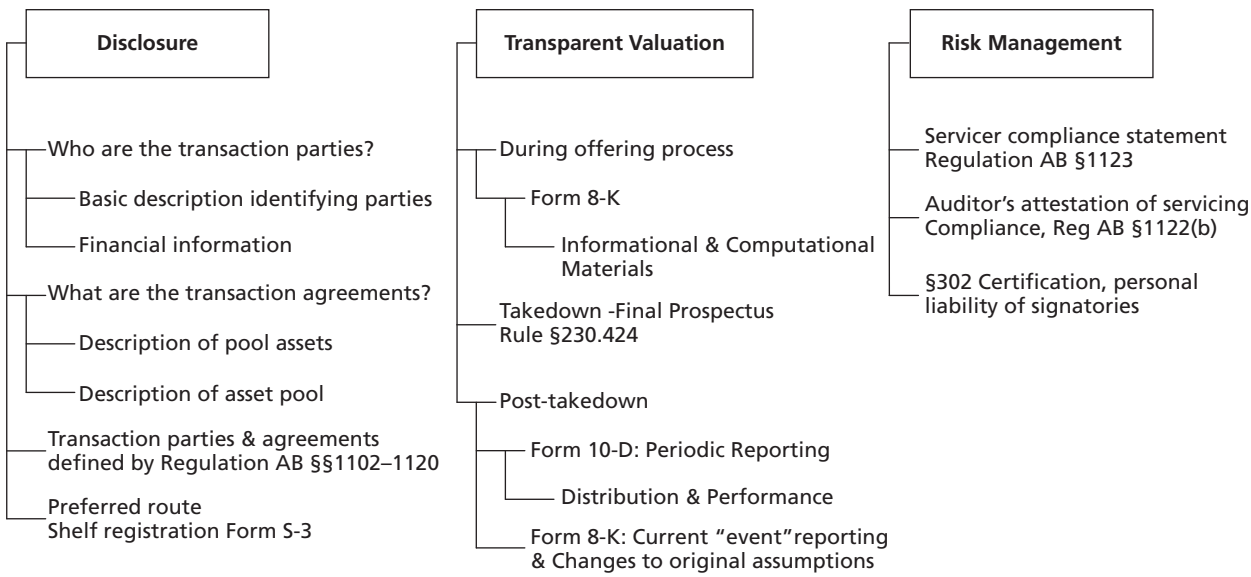
We believe that an informed asset backed securities legal framework that is principles-based and risk aware offers jurisdictions a significant opportunity for capital formation.

3 RELEVANT SECURITIZATION LAWS

In general, securities laws are driven by disclosure, transparency, and risk management. For asset-backed securities, these concerns are also paramount but are interpreted differently from normal securities since the transaction structure of asset-backed securities is radically different from normal securities transactions.

For ABS, due to the passive nature of the issuing SPV and the self-liquidating nature of the pool assets, different types of disclosures are required as well as a deeper level of transparency so that the investor may make an appropriate assessment of the value of the pool assets and the securities offered. To ensure the integrity of the disclosures the form of risk management must also be different, requiring the servicer or servicers to take front line responsibility to inform the investor that servicing criteria have been complied with and verification thereof has been conducted by an independent auditor. We illustrate how the concepts of disclosure, transparent valuation and risk management can be found in the US approach in the figure below.

Figure 2: US ABS Regulation — Disclosure, Transparent Valuation and Risk Management



Disclosures in general focus on the transaction parties and the transaction agreements, and their relevant terms and conditions, including descriptions of the pool assets and the asset pool, with specific items of disclosure under a new rule for asset-backed securities. See below under "U.S. Approach" for a more detailed discussion.

The concept of transparency simply means to provide information to investors which is sufficient for them to make their own assessments of the value of the pool assets and whatever security is being offered. The potential investor needs sufficient information to make an informed investment decision before accepting a takedown (supplemental or final prospectus) and throughout the life of the asset-backed security. It makes good sense

both theoretically and practically to expect a large amount of disclosures at the beginning of the transaction process to surmount the sheer face of dysfunctional asymmetry, and that after the asset-backed securities have survived a season of reporting for investor expectations relating to relevant and material information to taper downwards and to be substantially reduced after a few years.

Whilst the risk characteristics of asset pools may fluctuate, the majority of their valuation assumptions will be tested in the first year of reporting. The issue of how much disclosure and the penalties for individuals and institutions for non-disclosure or false disclosures are at the heart of the calculating the cost burden of the regulated market place. Regulatory authorities tend to pay lip-service to the cost-benefit of new regulations in relation to international competition for capital formation.

Higher quality disclosure, transparent valuation and risk management equates to higher barriers to entry. If regulators are looking to embrace more ABS issuance especially from foreign issuers, they may need to recognize and tolerate the risks of home jurisdictional rules of disclosure and be willing to allow investors to make their own grown-up decisions on economic and political risks.

Nevertheless at the transactional level, one of the distinguishing features of ABS is that it relies on large amounts of statistical data and investors are usually wholly reliant on the servicer to provide the appropriate information. Thus, for risk management purposes, the servicer rather than the special purpose vehicle is likely to have the awareness and responsibility over the information which the investor needs in order to make continual informed investment decisions relating to the ABS.

Risk management also dictates making individuals responsible for their actions, and in the US approach, as we shall see below, the servicer is treated as the ultimate responsible party, who must sign a servicing compliance statement[98] and is the focus of an attestation statement made by an independent public accountant.[99]

The US goes even further in terms of ensuring that the risk management responsibility may not be relegated to a corporate entity by making the relevant officer with appropriate authority sign in his or her personal capacity relating to the truth of the financial statements.[100] These three areas involving disclosure, transparency of data to aid investors make informed valuation, and ensuring that some form of personal liability is retained at the heart of the risk management process are likely to be found in most ABS regulations.

Given the globalization of financial products, at the transactional level, international practice in the securitization industry appears to converge and to replicate appropriate documentation supporting the securities transactions, At the same time, the need to deliver transparency to investors is expressed at the regulatory

[98] See, US Regulation AB, Item 1123.

[99] See, US Regulation AB, Item 1122(b).

[100] See, Final Rule Asset-Backed Securities (2005) at 1509 and §302 of the Sarbanes Oxley Act. Most commentators outside of the US would agree that submitting to an ABS regulatory regime may be appropriate to overcome information asymmetry, but requiring personal liability of officers who sign registration statements or reporting in the form of fines of up to $5 million and 20 years imprisonment per violation represents a dis-incentive to most sane market participants.

level through a dense canopy of rules and regulations that appear to require a deep expertise in the local legal eco-system where general principles are connected to myriad exceptions. Through this jungle of complexity, however, as we shall see, the general pattern for asset-backed securities regulations follows risk symmetric principles and any particular regulatory framework for asset-backed securities if it is to have a chance at competing successfully at an international level must be aimed at decreasing dysfunctional information asymmetries. We shall expand on these fundamental concepts in order build a theoretical benchmark for the comparison of ABS regulatory regimes after we have discussed the elements of the US approach to asset-backed securities.

Market participants if they are to succeed in the long run, seek risk symmetric patterns of information flow. This means that at the regulatory level, rules requiring disclosure should ideally allow for mutual reciprocal information flow between issuer and investor. At the transactional level, this is largely contract driven with practitioners from the United States exporting their knowledge and experience to Europe and further abroad.

Practice has dictated legal structures which allocate risks according to the legal relations between transaction parties and the transaction agreements which support the public issue of asset-backed securities. The securitization laws of the US and EU, whilst set in their own particular regulatory regimes, are nevertheless both concerned with providing protection to investors against false and misleading information as well as negligent omission.

From a theoretic perspective, both regimes are essentially concerned with overcoming dysfunctional asymmetry and thereby, establishing and maintaining what might be termed a risk symmetric framework for asset-backed securities. This means that investor protection is paramount and may be used as the criterion in the determination of whether any particular information should be disclosed at a particular point in time.

The risk symmetric framework means that any given point of time meaningful disclosure of material risks allows investors to make appropriate investment decisions relying on assertions of material facts made by the issuer.

On the one hand, a principles-based approach allows for the consolidation of best market practice by defining the general principles of what constitutes the essential structure of the asset-backed transaction. The foundational definition of the asset-backed security under US law acts a criterion for determining the regulatory envelop—of what should be specifically defined and what should be left to market practice uncontaminated by governmental interference. The principles-based approach also allows for further specification and flexibility in response to future developments of financial innovations.

On the other hand, a rules-based approach compels the issuer or more broadly, the signatories to the disclosure documents including the initial registration statement and ongoing reports, to report on specific items in a specified way.

These two approaches, the principles-based and the rules-based, are not necessarily antagonistic, especially at the level of reporting specific items that are relevant and material to the investor's decision making. In the rules-based approach, a regulation requiring specific items of disclosure has simply taken away any discretion on the part of the issuer or signatories, and has decided on behalf of the investor, what types of information are necessarily relevant and material to the investor's decision-making.

Against this idealized aim of asset-backed securities regulations, where one would expect substantial similarities between jurisdictions relating to disclosure items in order to achieve a risk symmetric framework, we would also expect important differences relating to the historical legacy pertaining to each jurisdiction's laws. Each jurisdiction in a word has its own complex system of laws that are path dependent. For example, the US securities has historically required three different levels of financial disclosure of a transaction party depending on the proportional level of involvement in a transaction, so called "breakpoints".[101] There is no rational or statistical basis for carrying over these breakpoints into asset-backed securities except that they are consistent with non-asset-backed securities disclosure requirements.

However, given that the US and the EU have only recently promulgated asset-backed disclosure requirements (for the US from 2006 with Regulation AB and the EU with the member states implementation of the EU Prospective Directive of 2004 and Prospective Regulation 2005), i.e., their recent history, i.e., path distance, and given that both attempt to pay deference to current market practice, i.e. path direction, there may be more a preponderance of substantive similarities between the two jurisdictions than there are substantive differences especially at the transactional level of ABS. The vectors of US and EU asset-backed securities regulations may very well overlap, especially if both regulatory communities were to agree on mutual recognition of their administrative process for foreign asset-backed securities.[102]

For purposes of this discussion, the various types of disclosure will be defined in terms of being either "principles-based", or "rule-based". A principles-based approach "leaves both the format and data items disclosed at the discretion of the organization doing the disclosing."[103] A crucial characteristic in the US's version of the principles-based regime is the determination of "materiality". If information is deemed material by the issuer, then it must be disclosed. Under the EU Prospectus Directive the near equivalent concept to materiality is "informed assessment."[104] In both the US and EU, it is the issuer who determines whether any particular information is relevant to the investor's decision-making.

In this narrow sense of principles-based versus rule-based, the SEC has indicated a preference for a principles-based approach to rule-based disclosure for both ABS registration statements and Exchange Act reports. In the Federal Rule on the Final Rule of Asset Backed Securities, the lawmakers state that they do "…not believe it would be practical or effective to draft detailed disclosure guides for each asset type that may be securitized."[105]

A narrow interpretation of the "rules-based" approach is the exact opposite of the principles-based approach. In the rules-based approach, the regulatory authority sets out the specific variables and format that must be

[101] See, the disclosure items of US Regulation AB relating to "significant obligor" §1112(b)(1)-(2), "internal and external credit enhancement" §1114(b)(2) and "certain other derivatives" §1115(b).

[102] See, US Regulation AB §1100(e) and discussion below.

[103] Stachel, D.W. (2004) "SEC Regulation AB, What an ABS Investor Wants for Christmas," available at: http://www.ssga.com/library/povw/danstachelsecregulationab20041101/page.html

[104] See, EU Prospectus Directive, Article 5(1), 2003/71/EC.

[105] US SEC (2005) Final Rule Asset Backed Securities, I.C. at 1509

adopted by all issuers.[106] The question of materiality or informed assessment is determined by the regulatory authority, and thus, completely eradicating the issuer's discretion.

Purpose of Comparison

The main purpose of the following section is to draw comparisons between the two regimes in order to find a broad common ground which we hope can be used for further comparison and gap analysis of Russian regulations.

We realize, however, that practitioners of the local jurisdictions might not find this commentary entirely satisfying since the very detailed issues of regulatory compliance are naturally analysed at the local level rather than at any abstract comparative level. We will provide some degree of analysis and critique of legal details, but not a point-for-point critical assessment.

For our purposes, if we can discern how certain disclosure categories are similar in both jurisdictions, this may lay the common ground for developing standards of asset-backed securities disclosures which would be mutually compatible to various regulatory authorities. Our bias is to point out areas of common overlap, not just in terms of legal labels, but in terms of substantive disclosure items defining legal relationships between transaction parties that may affect the value of the transaction.

We begin our comparative analysis with an analytical summary of the US Regulation AB and then move on to the EU Prospectus Directive and EU Prospectus Regulation, with specific reference to Annex VII and VIII of the latter. The reason we rely primarily on the EU Prospectus Regulation Annex VII and VIII is not only because these statutory instruments have been very successful in incorporating the fundamental principles and requirements of the EU directive and because the Annex occur at above the same level of regulatory authority as the Federal Rules of Regulation AB, that is, they must be consistently applied throughout the European Member States.

The US regulatory approach is self-declared to be principles-based with very explicit disclosure instructions. The advantage of the US approach is its explicitness but its disadvantage is that it requires a great deal of learning before becoming regarded as anything beyond convoluted.

We will endeavour to simplify and summarize the myriad of regulatory details and where possible use figures and tables to aid the understanding of the large body of regulations. The US Regulation AB (asset-backed) is nevertheless the world's first regulation devoted to asset-backed securities disclosures and despite its "stylistic shortcomings" governs the largest asset-backed securities markets in the world. We pay deference to the US approach for these reasons and because if Russian asset-backed issuers are to be made saleable to the deepest liquidity pools in the world, then they would most likely need to comply with the most rigorous standards set by the US. It may be assumed that if an asset-backed security passes muster with the US rules that it would be more than adequately pass the scrutiny required under the EU rules.

[106] Stachel (2004) *op. cit.*

We shall show that this assumption is positively affirmed in practically every instance of comparison of asset-backed securities regulations between the US and the EU.

3.1 US Approach

3.1.1 Legal Authority and Motivation

The legal authority for the regulation of asset-backed securities is based on the Securities Act 1933 ("Securities Act") and the Securities & Exchange Act 1934 ("Exchange Act"). The former is about the initial registration of securities, and the latter about on-going reporting. The US approach to the regulation of asset-backed securities is formally encoded under Federal law in Regulation AB[107] ("asset-backed") promulgated in Jan 2005 with effect from January 1st 2006. Previous to Regulation AB, there were no disclosure items tailored specifically to asset-backed securities[108] and only a few of the disclosure items in Regulation S-K were relevant to asset-backed securities, such as the description of the security.

Regulation AB was established for the purpose of informing the investor of matters critical to investment decision making. For ABS, since there is generally no management or business to describe, matters of concern to the investor include, information relating to the pool assets, servicing, transaction structure, flow of funds, enhancements, the timing and amount of expected payments on the assets and thus, expected payments on the ABS, and the impact of any credit enhancement or other support.[109]

Through the years, through the SEC's staff comment process and industry practice, informal disclosure practices developed but these were not fully transparent to issuers and investors.[110] To remedy this situation, the Final Rule on Asset-Backed Securities was promulgated on January 10, 2005 with effect on all ABS issues as of the 1st of January 2006 to formalize and improve the disclosure practices that include "…many of the items investors have previously recommended as critical to investors."[111]

In essence, Regulation AB is based on a principles-based definition of asset-backed securities, which is simply "securities that are backed by a discrete pool of self-liquidating financial assets."[112] The principles-based definition is then used to define the scope and application of the new rules, and forms a type of fundamental

[107] US Regulation AB, 17 CFR §229.1100 *et seq,* available at http://www.sec.gov/divisions/corpfin/ecfrlinks.shtml

[108] Federal Register (January 7, 2005) Part II Securities and Exchange Commission, 17 CFR Parts 210, 228 et al. *Asset-Backed Securities; Final Rule* at 1531.

[109] *Ibid*.

[110] *Ibid*.

[111] *Ibid*.

[112] *Id* at 1508. Under Regulation AB §1101(c)(1) defines "Asset-backed security" as "…a security that is primarily serviced by the cash flows of a discrete pool of receivables or other financial assets, either fixed or revolving, that by their terms convert into cash within a finite time period, plus any rights or other assets designed to assure the servicing or timely distributions

justificatory guidance for the determination of whether any particular proposed disclosure requirement should be considered within the basic definition of ABS, or whether it should be considered an exception, or in effect, whether it should be excluded because the proposal defeats the purpose of the original definition.[113] Therefore, under the US principles-based approach to ABS regulation, any and all disclosures for ABS must have a reasonable nexus to the original definition of ABS in order for it to be justified within the ABS disclosure regime.

Regulation AB addresses "four primary regulatory areas" affecting asset-backed securities: Securities Act registration; disclosure; communications during offering process; and ongoing reporting under the Exchange Act.[114] In this summary, we focus on disclosures and specifically, on the major disclosure requirements for asset-backed securities by foreign issuers or backed by foreign financial assets.[115] However, before delving into the requirements for foreign ABS, let us briefly summarize the structure of Regulation AB.

Summary of Regulation AB Structure

Regulation AB is a sub-part of Regulation S-K[116] relating to disclosures and consists of twenty-three sections, §1100 to §1123, also known as "Items". The following are some of the major features of Regulation AB:

Item 1100

identifies features that are generally applicable to the entirety of the sub-part, including guidance on the presentation of delinquency and loss information, when they must be reported, alternative methods for presenting third party financial information and guidance on foreign ABS.

Item 1101

sets out a principles-based definition of asset-backed securities and specific terms of art that are related to this principles-based definition.

Item 1102–1122

comprise the "basic disclosure package for Securities Act registration statements for ABS offerings" and for Exchange Act reports, such as "updated financial information regarding certain third parties and disclosure regarding legal proceedings,"[117] tax matters, and any material changes to information covering the report period.

---

of proceeds to the security holders; provided that in the case of financial assets that are leases, those assets may convert to cash partially by the cash proceeds form the disposition of the physical property underlying such leases." *Id* at 1600.

113 The definition of ABS is used "…to demarcate the securities and offerings to which the new rules apply." *Ibid.*

114 *Ibid*.

115 17 CFR 229.1100(e).

116 US SEC Regulation S-K, 17 CFR 229 *et seq.*

117 *Ibid*.

Item 1121
sets forth the requirements for disclosure reports on Form 10-D relating to cash flows and performance of the asset pool and the allocation of cash flows and distribution of payments on the ABS.[118]

Item 1122
specifies the requirements for the assessments of compliance with servicing criteria and the filing of attestation reports by registered public accounting firms on such assessments.[119]

Item 1123
identifies the form of the separate servicer compliance statement as per the particular servicing agreement of the transaction.[120]

Table 3: Regulation AB Disclosure Items

Item	Title
1100	General
1101	Definitions
1102	Forepart of registration statement and outside cover page of the prospectus
1103	Transaction summary and risk factors
1104	Sponsors
1105	Static pool information
1106	Depositors
1107	Issuing entities
1108	Servicers
1109	Trustees
1110	Originators
1111	Pool assets
1112	Significant obligors of pool assets
1113	Structure of the transaction
1114	Credit enhancement and other support, except for certain derivatives instruments
1115	Certain derivatives instruments
1116	Tax matters
1117	Legal proceedings
1118	Reports and additional information
1119	Affiliations and certain relationships and related transactions
1120	Ratings
1121	Distribution and pool performance information
1122	Compliance with applicable servicing criteria
1123	Servicer compliance statement

[118] *Ibid.*

[119] *Ibid.*

[120] *Ibid.*

3.1.2 Transaction Parties and Transaction Agreements

Out of the three-three sections of Regulation AB (see Table above), seven define major transaction parties and six sections deal with transaction agreements and the quality of the assets, i.e. "static pool information," "pool assets," "structure of the transaction," "credit enhancement and other support, except for certain derivatives instruments," "certain other derivatives instruments," and "distribution and pool performance information". The two sections on servicing (§1122 and §1123) form a an extensive definition of the role and responsibilities of the servicer. Similarly, §1119 "Affiliations and certain relationships and related transactions" is broadly contractual in nature or defines the nexus of various corporate relationships.

Thus, taken all together, nine sections are aimed principally at defining and requiring the disclosures of the role and responsibilities of transaction parties and eight sections that in general address issues of the transaction structure and transaction agreements directly or indirectly related to the value of the pool assets. This means that there are seventeen sections devoted to detailing the identity of the relevant parties to the ABS transaction, the characteristics of the underlying assets (which are subsumed under particular transaction agreements), and major transaction agreements which have a direct impact on the value of the transaction. The other sections, such as "tax matters," "legal proceedings," and "reports and additional information" could also have substantive impact on the value of the transaction but would apply more generally to value of any securities transaction.

In general, in disclosing information about a transaction party, the information is generally either descriptive or financial. Descriptive information the identity of the party, its organizational form, the general character of its business, the nature of the concentration and the material terms of the relevant contract that may affect the value of the transaction. The financial information required, in general, varies with the level of concentration, with breakpoints representing below 10%, between 10% or more and less than 20%, and more than 20%. The parties requiring financial disclosures according to these breakpoints include: significant obligor, internal and external enhancement, and certain other derivatives.[121] If the breakpoint is up to 10% then a short-form financial disclosure is required as per the specific Item defining the party in Regulation AB. If the breakpoint is 10% up to 20%, then the financial date required by Item 301 of Regulation S-K must be provided. And if the concentration represents 20% or more, then audited financial statements meeting the requirements of Regulation S-X are required.

Major Transaction Parties

The major transaction parties as identified and defined by Regulation AB are as follows:

Sponsors (§1104):

"the person who organizes and initiates an asset-backed securities transaction by selling or transferring assets, either directly or indirectly, including through an affiliate, to the issuing entity;"[122]

[121] See the disclosure items of US Regulation AB relating to "significant obligor" §1112(b)(1)-(2), "internal and external credit enhancement" §1114(b)(2) and "certain other derivatives" §1115(b).

[122] *Id* at 1534.

Depositors (§1106):

"the person who receives or purchases and transfers or sells the pool assets to the issuing entity." If there is no intermediate transfer of assets from the sponsor to the issuing entity, the sponsor is the depositor, and therefore, the issuer.[123]

Issuing Entities (§1107):

"the trust or other entity created at the direction of the sponsor or depositor that owns or holds the pool assets and in whose name the asset-backed securities supported or serviced by the pool assets are issued."[124]

Servicers (§1108):

"any person responsible for the management or collection of the pool assets or making allocations or distributions to holders of the asset-backed securities."[125]

Trustees (§1109):

The Federal rule states that there is no separate definition of trustee and the lawmakers "do not believe that it is necessary to provide one".[126] Although not specifically defined, Item §1109 requires description of the identity of any trustee and actions required of the trustee especially in relation to particular events which require the trustee to provide notice to investors such as events of default or breaches of covenants.[127]

Originators (§1110):

In the same way as trustees, the Federal lawmakers "do not believe it is necessary to provide a separate definition for originators."[128] Given the debacle of the US subprime market in February of 2007, it is important to note that "each originator, apart from the sponsor or its affiliates, that has originated, or is expected to originate, 10% or more of the pool assets must be identified. In addition, for any originator where the percentage is 20% or more, additional information regarding the originator's originator program must be provided, including, if material, information regarding the size and composition of the originator's origination portfolio, as well as information material to an analysis of the performance of the pool assets, such as the originator's *credit-granting* or *underwriting criteria*."[129] (Emphasis added.)

---

123 *Id* at 1534 and 1616, referring to §230.191.

124 *Id* at 1534.

125 *Id* at 1535.

126 *Id* at 1537.

127 *Ibid*.

128 *Id* at 1538.

129 *Ibid*.

Significant obligors of pools assets (§1112):

Information on any particular obligor in a large pool of obligors may not be material. However, where the concentration of a particular obligor, or group of obligors increases, then additional disclosures including financial information are required. A significant obligor is defined as "an obligor or a group of affiliated obligors on any pool asset or group of pool assets if such pool asset or group of pool assets represents 10% or more of the asset pool;

A single property or group of related properties securing a pool asset or a group of pool assets if such pool asset or group of pool assets represents 10% or more of the asset pool; or

A lessee or group of affiliated lessees if the related lease or affiliated lessees if the related lease or group of leases represents 10% or more of the asset pool."[130]

This definition clarifies how separate pool assets or properties underlying pool assets, if they are cross-defaulted and/or cross-collateralized, are to be aggregated and considered together as one in calculating concentration levels. For mortgage-backed securities, if the pool asset is a mortgage, and the obligor does not manage the property and does not own other assets, and has no other operations, then the obligor need not be considered a separate significant obligor.

Having surveyed the structure, identified the transaction parties and listed some of the major transaction agreements of asset-backed securities, we turn now to the specific disclosure requirements for foreign ABS.

3.1.3 Disclosure Requirements for Foreign ABS

The disclosure requirements for foreign ABS are relevant to the purpose of this report since these rules help us understand what types of disclosure rules would lay the basis for mutual compatibility or mutual recognition of ABS disclosures requirements between the US and other jurisdictions. In practical terms, mutual compatibility and recognition provides foreign issuers a potentially large economic benefit from enlarged market participation with deepened liquidity. That is, if other jurisdictions, such as those of the EU and Russia, were to set out regulatory disclosure requirements for ABS issuers that allowed for the mutual compatibility of specific requirements similar to those set out by the US for foreign issuers of ABS then these issuers would be able to take advantage of shelf registration offerings in the US, and thus, gain access to the largest institutional investor pools for ABS in the world.

The concept of mutual compatibility or mutual recognition favours a bottoms-up approach which consolidates an already existing body of best practice (i.e., *lex Juris*) of international practitioners relating to the documentation of risk elements of asset-backed securities. Thus, regulatory regimes around the world need not make large revisions of securities regulations in order to take advantage of mutual compatibility but rather, so long as there as the provisions that allow "shelf-registration" and then foreign asset-backed securities could have the

[130] *Id* at 1547.

same disclosure requirements as domestic issues with the addition that the home factors affecting the value of the pool assets also be disclosed.

The professed motive of the US law relating to foreign ABS is national self-interest in that it intends "to alleviate impediments to the shelf registration of offerings of asset-backed securities by foreign issuers or backed by foreign financial assets,"[131] which would, if not otherwise appropriately amended, prevent US institutional investors from investing in foreign ABS. In brief, the legal mechanics for foreign ABS issuers are that they would register offerings using Forms S-1 or S-3[132]. Form S-1 covers all ABS offerings that are not shelf-registered and Form S-3 covers offerings that are shelf registered.

In essence, the effect of Regulation AB is to add Items 1102 to 1120 to the disclosure requirements of Form S-1 and Form S-3.[133] The difference between Form S-1 and Form S-3 is basically that Form S-3 has additional eligibility requirements such as that asset-backed securities must be investment grade, that leased-backed securities carry additional restrictions, and delinquent pool assets must be specified.[134] Specific instructions are provided for the preparation of each Form: for Form S-1, General Instructions VI; and for Form S-3, General Instructions V.[135]

For purposes of this summary, between non-shelf and shelf registration, we focus on shelf registration since offers a highly effective and efficient mechanism for overcoming the basic information asymmetry problem inherent with public offerings of complex financial instruments.

3.1.4 Advantages of Shelf Registration

The advantages of shelf registration utilizing Form S-3 is the relative ease and convenience of presenting disclosures in the form of a separate base prospectus and then in prospectus supplements that outline the deal specific information that will be disclosed at the time of each takedown.[136] In general, since the reporting history is not required for ABS for Form S-3 eligibility, "…investment grade ABS offerings registered on that form often must present most of their disclosure in the base prospectus and prospectus supplement in lieu of incorporating information by reference."[137] The deal mechanics of shelf registration follows an orderly process that allows the

[131] *Id* at 1508.

[132] "…We are not establishing a separate disclosure regime or requirements for foreign ABS, we continue to believe it is unnecessary to provide separate form types for foreign ABS offerings. These offerings also will be registered on Forms S-1 or S-3, as applicable." *Id* at 1522.

[133] For an outline of the disclosure items of Form S-1, see *Id* at 1522. For the disclosure items of Form S-3, see Table 1 Disclosure Requirements of Form S-3 below.

[134] *Id* at 1522.

[135] For Form S-1, see General Instructions VI which clarifies how the form is to be prepared for an ABS offering at www.sec.gov./about/forms/forms-1.pdf. See also, *Id* at 1522. For Form S-3, see General Instructions V.

[136] *Id* at 1523.

[137] *Id* at 1523.

issuer and the investors to be mutually informed and forewarned of the major features and risks of the transaction and to communicate with each other as to what would be the most appropriate form of securities to be offered, and importantly, to be accepted.[138] As stated in the Final Rule for Asset-Backed Securities,

> … the type or category of asset to be securitized must be fully described in the registration statement at the time of effectiveness. The structural features contemplated also should be disclosed, as well as identification of the types or categories of securities that may be offered, such as interest-weighted or principal-weighted classes (including IO or PO securities), planned amortization or companion classes or residual or subordinated interests. In addition, risks associated with changes in interest rates or prepayment levels should be fully disclosed. The various scenarios under which payments on the asset-backed securities could be impaired also should be discussed.[139]

The shelf-registration-to-supplemental-prospectus process adds flexibility, market timeliness, and the potential for substantial innovations to ABS transactions which together help reduce dysfunctional information asymmetry and thus, increase chances of sustainable market success. Given the importance of shelf-registration, we will focus the following discussion on the disclosure requirements for Form S-3 for Registered ABS Offerings.[140] The disclosure requirements for Form S-3 are as follows:

Table 4: Form S-3 Disclosure Requirements

Item	Title	Required if applicable
1	Forepart of Registration Statement and Outside Front Cover page of Prospectus	✓
2	Inside Front and Outside Back Cover Pages of Prospectus	✓
3	Summary information, Risk Factors and Ratio of Earnings to Fixed Changes	✓
4	Use of Proceeds	✓
5	Determination of Offer Price	✓
6	Dilution	✓
7	Selling Security Holders	✓
8	Plan of Distribution	✓
9	Description of Securities to be Registered	✓
10	Interests of Named Experts and Counsel	✓
11	Material Changes	✓
12	Incorporation of Certain Information by Reference	✓
13	Disclosure of Commission Position on Indemnification for Securities Act Liabilities	✓

[138] "If this approach [shelf registration] is followed, a form of supplemental prospectus is required to accompany the based prospectus in the registration statement at the time of effectiveness that outlines the format of deal-specific information that will be disclosed at the time of each takedown." *Id* at 1523.

[139] *Id* at 1524.

[140] *Id* at 1523.

Item	Title	Required if applicable
14	Other Expenses of Issuance and Distribution	✓
15	Indemnification of Directors and Officers	✓
16	Exhibits	✓
17	Undertakings	✓
	Additional Disclosure Items from Regulation AB Items 1102–1120 of Regulation AB	✓

§1100(e) entitled "Foreign asset-backed securities" sets out the scope and requirements for foreign issuers and for asset-backed securities backed by foreign assets or affected by enhancement or support provided by a foreign entity. Foreign asset-backed securities are subject to the same requirements as domestic issues except that should they intend to take advantage of shelf registration then they will not only have to comply with all the requirements of Form S-3 but also disclose all of the factors required by §1100(e) relating to the foreign issuer's home jurisdiction's legal and regulatory environment. See Table 5 below.

Table 5: Specific Items Required for Foreign Issuers under Regulation AB §1100(e) Foreign Asset-backed Securities

Item	Title	Components
		Securities Act – Registration Statement
1104	Sponsors	
1105	Originators	
1107	Issuing Entities	
1108	Servicers	
1111	Pool Assets	
1114	Credit enhancement and support	
1115	Certain derivative instruments	
1100(e)	Foreign Asset-Backed Securities	(1) Governmental
		(2) Legal
		(3) Regulatory
		(4) Administrative
		(5) Tax
		(6) Exchange controls
		(7) Currency restrictions
		(8) Economic, fiscal or monetary
		(9) Factors affecting payments or performance of Home pool assets
		(10) Factors affecting payments or performance of Asset-backed securities

Item	Title	Components
		Securities Act – Registration Statement
§229.202	Instruction 2	
§229.101(g)		
		Exchange Act Reporting
§249.312	Form 10-D	Report for periodic distribution and pool performance information.[141]
§249.310	Form 10-K	Annual report
§249.308	Form 8-K	Report on "current" events.[142]

Since shelf registration affords issuers the most direct, cost-effective and convenient access to US institutional investors, allowing foreign asset-backed issuers access to this method of registration represents a major step forward in the US regulator's attitude to liberalizing its regulatory regime.

Before Regulation AB, the practice of the US SEC was to first require prospective foreign asset-backed issuers to register one or more offerings under a non-shelf basis on Form S-1 or S-11, which were fully reviewed by the SEC staff, and the foreign issuer would then have to face and overcome additional "steps or conditions" that SEC staff posed. The point of these additional steps was in effect to educate the SEC sufficiently so that the SEC could address "novel or unique questions" raised by the foreign asset-backed securities issue.[143] As the SEC staff learned more about the particular issuer, its asset type and the laws related to the asset-backed securities in the home jurisdiction, the SEC tended to decrease its requirements.[144] However, this rather discretionary attitude no doubt resulted in delays and impediments to foreign issuers looking for access to the U.S. public capital markets,[145] which in a word, made the US regime for shelf registration difficult for foreign ABS issuers to calculate or plan for, and relatively more expensive and difficult to comply with than similar European regulations.

Although not explicitly acknowledged by the SEC, it is not unreasonable to construe the rule change allowing shelf registration for foreign asset backed securities as a direct response to competitive pressure. What's the point of having disclosure rules to protect investors when the very rules become impossibly high barriers to entry? Whilst the SEC had intended §1100(e) on foreign asset-backed securities to help increase foreign access

[141] *Id* at 1565. See also 17 CFR 249.312. As in other Exchange Act reports, Form 10-D is subject to all applicable requirements of the general rules and regulations under the Exchange Act for the preparation, signing and filing of Exchange Act reports, including Regulation 12B(17 CFR 240.12b-1 *et seq.*); Regulation 13A(17 CFR 240.13a-1 *et seq.*); and Regulation 15D (17 CFR 240.15d-1 *et seq.*). The Form 10-D report will be required o be submitted in electronic form in accordance with the EDGAR rules set forth in Regulation S-T.

[142] *Id* at 1564. See Table below on Form 8-K, especially Items 6.01 to 6.05.

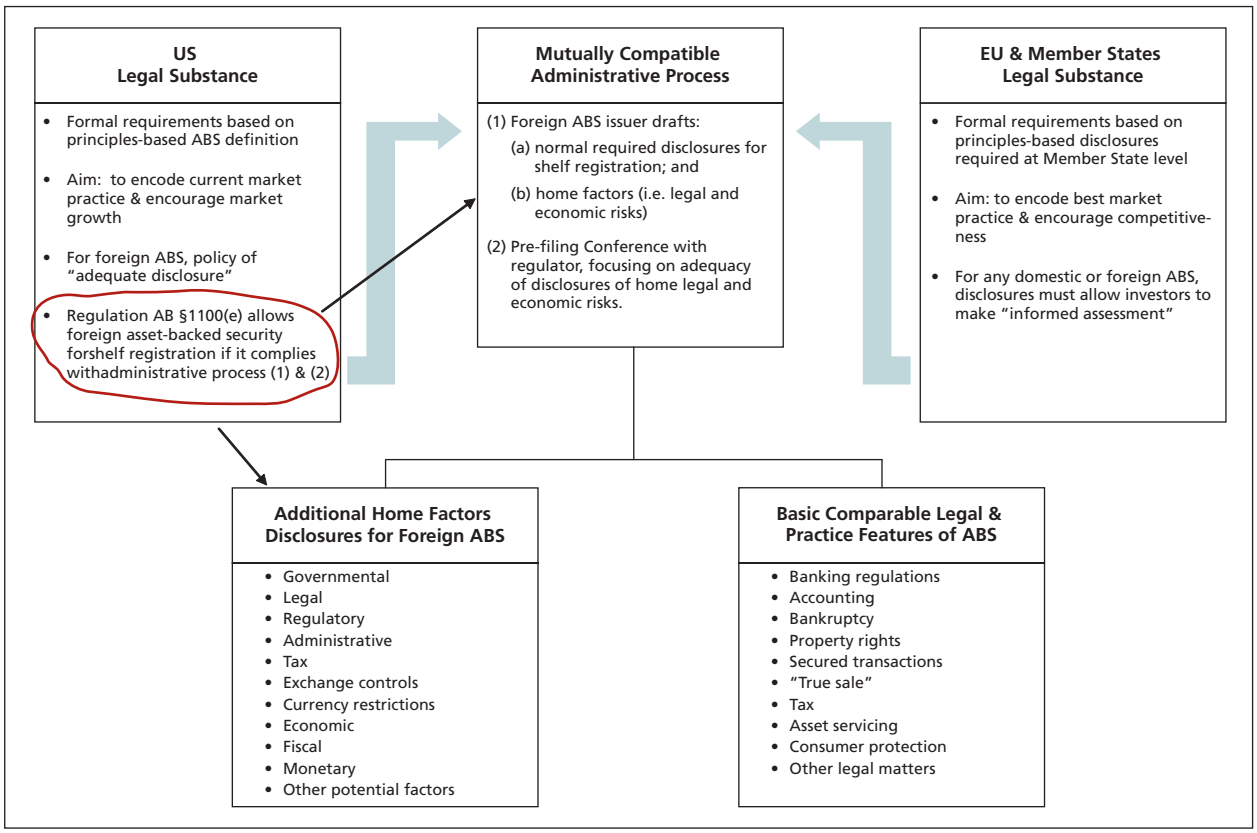
[143] *Id* at 1527.

[144] *Ibid.*

[145] *Ibid.*

to the US markets, from a theoretical perspective, it actually provides *a model for the mutual compatibility* of home-host rules relating to shelf registration of asset-backed securities. See Figure below.

Figure 4: Mutual Compatibility of Home-Host Rules for Foreign ABS



The Figure above illustrates how the additional disclosure requirement for foreign ABS under the US Regulation AB §1100(e) is actually a requirement to disclose the home factors in terms of the legal and economic risks, including, governmental, legal, regulatory, administrative, tax, exchange controls, currency restrictions, and economic, fiscal, monetary and other potential factors.

The additional home factors are similar to the basic legal and practice features common to all ABS transactions with the addition of economic features. This means any jurisdiction which is considering legitimizing and regulating ABS are likely to considering similar substantive legal and regulatory issues. The Figure also illustrates how an administrative process for the discovery of the relevant and material home factors would allow regulators in different jurisdictions (e.g., the US and Member States of the European Union) to come to constructive conclusions of "mutual compatibility" for asset-backed securities transactions. However, it is important to note that whilst this process could be initiated and formalized at the legislative level, each ABS registration will naturally be decided on a case to case basis by the host regulator at the administrative level.

The US approach recognizes that foreign ABS issuers have developed rapidly and that given the early stage of securitization in some foreign markets, ABS may be used not so much as a method for alternative funding but more as a technique for capital management where the aim would be "…to prune a lender's portfolio by off-loading poorly performing assets."[146] Despite this concern, the SEC has become more willing to respond to the competition for international capital. It has stated that it encourages the foreign ABS issuer to a pre-filing conference where the SEC staff will discuss and help the foreign issuer identify the relevant disclosures that will be required.[147] This does not mean that the foreign ABS issuer has any lesser burden than the domestic issuer. In fact, it will be required to report just as a domestic issuer on Forms S-3, 8-K (for current events see below), and in addition, ongoing disclosures in Forms 10-D ("periodic reports") and 10-K (annual fiscal report) regarding any material impact caused by foreign legal and regulatory developments during the time covered by the report which had not been previously identified.[148]

3.1.5 Timing of Disclosures

As a general principle, communications between the issuer and the investor are paramount in order to overcome dysfunctional information asymmetry. Thus, at each point of time when a disclosure is made it goes without saying that the information conveyed is transparent, that is it must be so that it can be relied on by an investor to make appropriate investment decisions. The question of whether the disclosure requirement is relevant to investment decision making is highly dependent on whether the regulatory authorities can formally capture the needs and demands of information hungry investors.

From the mid-1990's, through a series of no-action letters, the SEC condoned the market practice of the issuer communicating with prospective investors during the time between the filing of the registration statement and the final prospectus in the form of three types of basic materials: (1) structural term sheets; (2) collateral term sheets and (3) computational materials.[149] The structural term sheets identified the proposed structure of the securities being offered, including the "parameters of the various types of class offered."[150] The collateral term sheets provided information on the underlying assets. And the statistical term sheets comprised statistical data relating to specific class of asset-backed securities, including the "yield, average life, expected maturity, interest rate, maturity, cash characteristics or other such information under specific prepayment, interest rate, loss or related scenarios."[151] The relevant period for these communications occurred after the filing of the registration statement (Form S-3) and before the delivery of the final Section 10(a) prospectus.

[146] *Id* at 1527.

[147] *Id* at 1527.

[148] *Id* at 1527.

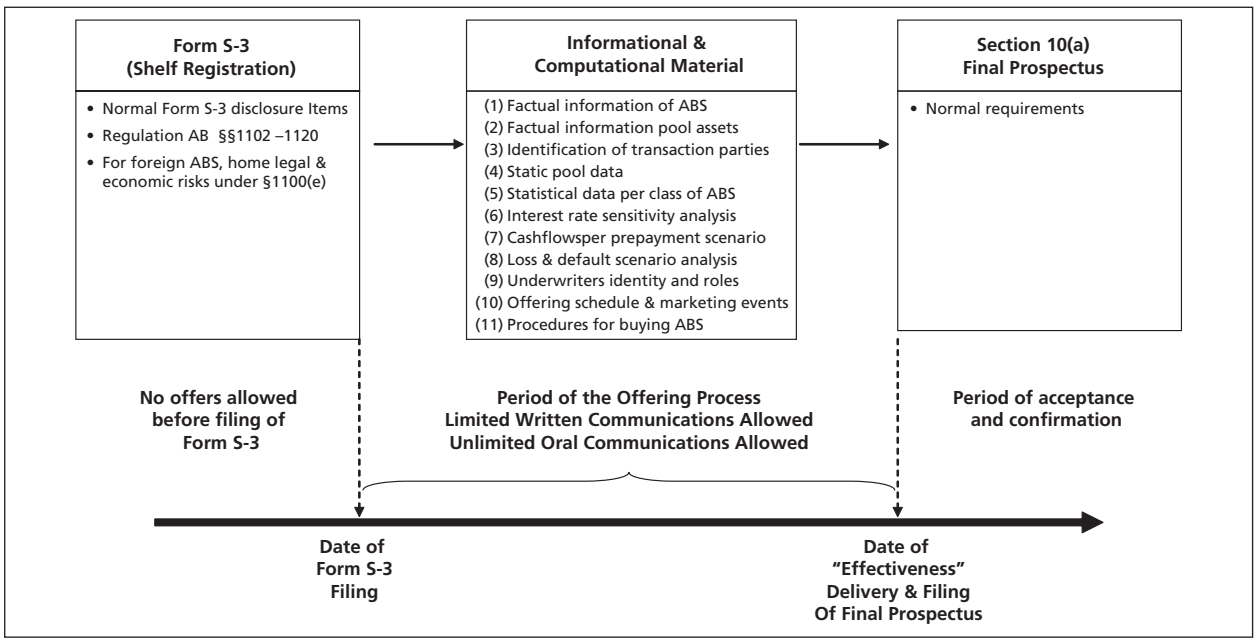
[149] *Id* at 1554.

[150] *Ibid*.

[151] *Ibid*.

It is important to note that the Securities Act restricts the type of communications that a registrant or other parties subject to the Act's provisions (such as underwriters) may use during a registered public offering.[152] Essentially, there are three periods to consider: (1) before the registration statement is filed; (2) after the registration statement is filed and before the final prospectus under Section 10(a) is delivered and filed; and after the final Section 10(a) prospectus is delivered and filed. See Figure below. In the first period, all offers in whatever form are prohibited.[153] In the second period (i.e. "between the filing of the registration statement and its effectiveness"), all offers made in writing by email, internet, radio or television were required to conform to the information requirements of Section 10 of the Securities Act.[154] This is basically in the form of a preliminary prospectus which had to be filed with the Commission. Oral offers are allowed during the second period and do not have to comply with the requirements of Section 10. After the registration statement is declared effective, the issuer is permitted to make written offers but only if a final prospectus that meets the requirements of Section 10(a) precedes or accompanies them.[155] In the third period, the form of written offer must meet all the requirements of Section 10(a). We can sum up the timing of disclosures in the Figure below.

Figure 5: Disclosures during the Offering Process



The complexity of an ABS transaction means that the issuer needs to communicate a large amount of information to prospective investors. For example, the investor will need to analyse the structure of the various

[152] *Id* at 1554. See also Section 5 of the Securities Act (15 U.S.C. 77e) and the Offering Process Release.

[153] *Id* at 1554.

[154] *Ibid*.

[155] *Ibid*.

classes of ABS, which vary from transaction to transaction, as well as the tranching and pool characteristics, including potential cash flow patterns.

Thus, in a shelf registration scenario, the sponsors or underwriters are looking to provide sufficiently detailed information to potential investors in the form of "computational materials and terms sheets identifying the structure and underlying assets prior to finalizing the deal structure and printing the final prospectus."[156] These materials will help the investor analyse the proposed transaction in terms of prepayment assumptions and other issues affecting the yield and flow of funds. The Federal law recognizes that the volume of this information would be impractical to communicate orally and that in the mid-1990s "few investors had the computer resources to prepare these analytics themselves."[157] Today, institutional investors are assumed to have the requisite computer power to do their own analysis of such information. Thus, the final rule provides for an exemption from Section 59(b)(1) of the Securities Act for the use of ABS informational and computational materials in offerings of Form S-3 ABS after the effectiveness of a registration statement but before delivery of the final §230.424 prospectus. This exemption is a step towards overcoming dysfunctional information asymmetry, as the Federal law states:

> …given the current use of these materials [i.e. informational and computational materials] in providing an increased flow of information to investors, the flexibility to tailor materials to specifically identified investor needs, and the liability for false and misleading statements or omissions, we believe permitting the use of ABS informational and computational material for Form S-3 ABS during such period is appropriate in the public interest and consistent with the protection of investors…

The use of ABS informational and computational material is conditioned on complying with Rule 426. This requires a filing under Form 8-K (under Item 6.01 of that Form) under two conditions:

> (1) if a prospective investor has indicated to the issuer or an underwrite that it will purchase all or a portion of the class of asset-backed securities to which such materials relate, all materials relating to such class that are or have been provided to such prospective investor (this condition applies no matter whether the indication to purchase is given before or after the final terms have been established for all classes of the offering); and
>
> (2) for any other prospective investor, all materials provided to that prospective investor after the final terms have been established for all classes of the offering. These materials are required to be filed on Form 8-K and "incorporated by reference into the registration statement, by the later of the due date for filing the final prospectus or two business days after first use."[158] And, all of this informational and computational information to the extent that these communications constitute offers will carry liability under Section 12(a)(2) of the Securities Act. And this liability will apply to all materials considered "prospectuses" subject to Section 12(a)(2) even if not filed.[159]

[156] *Ibid*.

[157] *Ibid*.

[158] *Id* at 1558.

[159] *Id* at 1558.

3.1.6 On-going Reporting

The Federal law subscribes to the general principle that "filing separate annual, periodic and other reports for each issuing entity provides easier access to information on a particular issuing entity and its asset-backed securities, which increases transparency of such information for investors as well as the market for these securities."[160] Thus, after the filing of the self registration Form S-3, the information and computational materials during the offering process, and the filing of a final prospectus according to Rule 10(a), there are on-going or post-issuance reporting requirements under the Exchange Act.

If the ABS are listed on any US national exchange then they must be registered under Section 12 of the Exchange Act and file reports according to Section 13(a) of the Exchange Act. Even without a listing, an ABS under an effective Securities Act registration statement "triggers a reporting obligation under Section 15(d) of the Exchange Act" at least for a period of time.[161] This obligation automatically suspends in any fiscal year except in the fiscal year in which the registration statement becomes effective, if, at the beginning of this fiscal year, "the securities of each class to which the registration statement relates are held of record by less than 300 persons."[162] Since most ABS are not listed and are held by less than 300 persons, most publicly offered asset-backed securities stop reporting with the Commission once they qualify for the automatic suspension.[163]

With regard to shelf registration, a new issuing entity is generally used for the issuance of each separate series of securities and thus, a new reporting requirement is initiated in relation to each of those securities. The suspension of the reporting requirement for the ABS issuing entity occurs if the securities meet the requirements of Section 15(d) of the Exchange Act, that is, the securities are held by less than 300 persons at the beginning of any fiscal year other than the fiscal year in which the takedown occurred. The suspension of one reporting obligation does not affect any separate reporting obligation with respect to any other takedown.[164] This rule applies even if other issuing entities of the same sponsor issue additional asset-backed securities during the initial fiscal year.[165]

Since the reporting requirements of normal operating companies are not relevant to ABS, the filings for on-going reporting of ABS are typically based on the frequency of distributions of the ABS (usually monthly) which "generally match the payment frequency of the underlying pool assets."[166] These filings are typically on Form 8-K and include a copy of the servicing or distribution report required by the ABS transaction agreements. These contain un-audited information about the performance of the assets, payments on the asset-

[160] *Id* at 1564.

[161] *Id* at 1561. "If the duty to report is suspended, a Form 15 is required to be filed 30 days after the beginning of the first fiscal year it is suspended. See Exchange Act Rule 15d-6 (17 CFR 240.15d-6). See also Exchange Act Rule 12h-3 (17 CFR 2409.12h-3)." Note 432, id at 1561.

[162] *Id* at 1561.

[163] *Ibid*.

[164] *Id* at 1563.

[165] *Id* at 1561.

[166] *Ibid*.

backed securities and any other material developments that affect the transaction, including what normally is seen on the quarterly Form 10-Q, e.g., legal proceedings, material uncured defaults and matters submitted to a vote of security holders. Besides these "periodic" filings on Form 8-K, Form 8-K are also used for "current" filings required for a narrow list of events.[167]

In addition to the periodic and current filings on Form 8-K, an annual report for ABS is required to be filed on Form 10-K. This is a shortened version of the normal 10-K required for operating companies and does not include the requirement of audited financial statements. Instead, the ABS issuer must file as exhibits to the Form 10-K, a servicer compliance statement[168] and a report by an independent public accountant.[169]

The servicer compliance statement evaluates and provides an opinion as to how well a servicer has complied with its obligations under the servicing agreement for the reporting period. The accountant's report is an attestation that the duties required of the servicer under the transaction agreements have been complied with according to particular servicing criteria.

Whilst ABS are exempted from §404 Sarbanes Oxley Act regarding internal control over financial reporting,[170] they are still required to file a certification as per Section 301 of that Act as part of the Form 10-K filing. This must be signed by either a CEO or CFO, or where they are missing as in most ABS transactions, then by a designated officer of the depositor, servicer or trustee.[171] It is important to note that "a natural person must sign the [Section 302] certification in his or her individual capacity, although the title of that person in the organization of which he or she is an officer may be included under the title."[172] This means that if the statement turns out to be false, then the person may be held personally liable for civil and criminal penalties of up to $5 million and 20 years imprisonment per violation.[173]

In terms of signatories for on-going reporting purposes, the depositor for a particular issuing entity created for the first takedown under a shelf registration statement will be deemed to be a different "issuer" than that depositor acting as depositor for a subsequent issuing entity created for a subsequent takedown under the same registration statement.[174] However, although the depositor remains the main designated signatory to on-going reports under Section 15(d) of the Exchange Act, the servicer is permitted to sign on behalf of the issuing entity as an alternative.[175]

---

167 *Ibid.*

168 *Id* at 1561. See also §229.1123.

169 See, Regulation AB, §229.1122(b).

170 *Id* at 1510 and see Exchange Act Rules 13a-15 and 15d-15.

171 *Id* at 1562.

172 *Id* at 1570.

173 See, Tanega, J. (2005) "Sarbanes Oxley Litigation – Employee Liability and Protection," *ICCLR*, at 204-209.

174 US Final Rule on Asset-backed Securities, at 1562.

175 *Ibid.*

The general principle is that each takedown of ABS by a new issuing entity triggers a new reporting obligation under Exchange Act 15(d). This means that separate electronic filing and access codes for EDGAR need to be set up for each new issuing entity for each takedown "to ensure that Exchange Act reports related to these AB-S are filed under a separate file number from other ABS or from the depositor's or sponsor's own securities."[176]

In terms of when on-going reporting obligations begin, for shelf registration, there is no asset pool or securities to report about until the first takedown and thus, no Exchange Act reporting requirement until the first takedown.[177] Thus, the operative event triggering the reporting requirement under Section 15(d) for ABS is the first bona fide sale in a takedown of securities under the registration statement. This is important since this date sets the clock for both starting and suspension dates for any reporting obligation relating to a takedown of ABS. The reporting period for each takedown of the ABS lasts through the fiscal year of that particular takedown and ends in the fiscal year where it has less than 300 holders.

3.1.7 Form 8-K Current "Event" Reporting

Form 8-K is used to report on current events that "unquestionably or presumptively have such significance that timely disclosure should be required."[178] Under our risk symmetric framework, such new events if left unreported would tip the balance towards a dysfunctional asymmetry in favour of the seller and therefore, the disclosure of these items at a certain point of time, near the events in question, help rebalance the situation towards information symmetry. The reporting deadline for reporting most events under Form 8-K is four business days. The existing items and the additional items under Regulation AB under Form 8-K are listed on the following table.

Table 6: Form 8-K Disclosures[179]

Item	Existing Form Items	Required if applicable	May be omitted
1.01	Entry into a Material Definitive Agreement	■	
1.02	Termination of a Material Definitive Agreement	■	
1.03	Bankruptcy or Receivership	■	
2.01	Completion of Acquisition or Disposition of Assets		■
2.02	Results of Operations and Financial Condition		■
2.03	Creation of a Direct Financial Obligation or an Obligation under an Off-Balance Sheet Agreement of a Registrant		■
2.04	Triggering Events that Accelerate or Increase a Direct Financial Obligation or an Obligation under an Off-Balance Sheet Arrangement	■	

[176] *Id* at 1562.

[177] *Ibid*.

[178] *Id* at 1578.

[179] See, Table "Disclosure fo Form 8-K for ABS", *id* at 1577.

Item	Existing Form Items	Required if applicable	May be omitted
2.05	Costs Associated with Exit or Disposal Activities		■
2.06	Material Impairments		■
3.01	Notice of Delisting or Failure to Satisfy a Continued Listing Rule or Standard; Transfer of Listing		■
3.01	Unregistered Sale of Equity Securities		■
3.03	Material Modifications to Rights of Security Holders	■	
4.01	Changes in Registrant's Certifying Accountant		■
4.02	Non-Reliance on Previously Issued Financial Statements or a Related Audit Report or Completed Interim Review		■
5.01	Changes in Control of Registrant		■
5.02	Departure of Directors or Principal Officers. Election of Directors. Appointment of Principal Officers		■
5.03	Amendments to Articles of Incorporation or Bylaws. Change in Fiscal Year	■	
5.04	Temporary Suspension of Trading Under Registrant's Employee Benefit Plans		■
5.05	Amendments to the Registrant's Code of Ethics, or Waiver of a Provision of the Code of Ethics		■
7.01	Regulation FD Disclosure	■	
8.01	Other Events	■	
9.01	Financial Statements and Exhibits	■	
	Additional Items added to Form 8-K for ABS		
6.01	ABS Information and Computational Material	■	
6.02	Change of Servicer or Trustee	■	
6.03	Change in Credit Enhancement or Other External Support	■	
6.04	Failure to Make a Required Distribution	■	
6.05	Securities Act Updating Disclosure	■	

Items 6.01 to 6,05 are the additional items for ABS. These items stretch over the period covered by the Securities Act, i.e., between the registration statement and the final prospectus for a takedown, and the Exchange Act, i.e. the period after the final prospectus for a takedown. You will note that Item 6.01 comes under the Securities Act Rule 426 and refers to the materials that are disclosed from the issuer to potential investors during the offering process, that is, between the filing of the shelf registration statement with Form S-3 and a final prospectus under section 10(a) of the Securities Act. Section 6.02 Change of Servicer or Trustee requires disclosure of any replacement of the servicer or trustee and the circumstances surrounding the change.[180] Section 6.03 requires the disclosure of any loss, addition or material modification of any material credit enhancement or other support provided by a third party.[181]

[180] *Id* at 1578.

[181] *Id* at 1578.

For both Section 6.02 and 6.03, if the information is not entirely available, then the registrant must file a statement in the filing and then file an amendment to the Form 8-K filing containing information without four business days after the information is determined or becomes available.[182] The events constituting Items 6.02 or 6.03 can occur either before or after the final prospectus. For Item 6.04 Failure to Make a Required Distribution, this obviously covers an event after the final prospectus when a required distribution to holders of the ABS is not made as of the required distribution date under the transaction agreements, and such failure is material. In this case, disclosure of the failure to pay is required as well as explanation for the nature of the failure. This report of failed payment under Form 8-K does not replace the required periodic disclosure under Form 10-D.

Item 6.05 Securities Act Updating Disclosure covers the situation where the composition of the actual asset pool at the time of issuance of the ABS differs from the composition of the pool described in the final prospectus for the offering. Any material pool characteristic of the asset pool at the time of issuance that differs by 5% or more (other than as a result of the pool assets converting into cash in accordance with their terms[183]) from the description of the asset pool in the final prospectus filed for the takedown pursuant to Securities Act Rule 424 is required to be disclosed. This includes any new significant obligors, servicers or significant originators.[184] In order to reduce unnecessary reporting, "no report is required if substantially the same information is provided in a post-effective amendment to the Securities Act registration statement or in a subsequent Rule 424 prospectus."[185] However, the underlying principle of Item 6.05 is that in order for the investor to make a proper assessment of the investment, the investor is entitled to "disclosure of the actual asset pool that the investor is primarily dependent on for repayment."[186]

3.1.8 Form 10-D: Periodic Reporting of Distribution and Performance

In order to improve the distinction between "periodic" and "event" reporting, the new final rule for asset backed securities sets out a new Form 10D specifically covers periodic distribution and pool performance information.[187] Form 10-D applies to all ABS subject to Exchange Act reporting, which means that that will apply to mainly shelf registration ABS. They are required to be filed 15 days after each required distribution date on the ABS as specified in the governing documents of such securities and with a possible five day extension period under Exchange Act Rule 12b-25.[188] The permitted signatories for Form 10-D are those who are

[182] *Id* at 1578.

[183] "If a revolving period was in effect, while this proviso would exclude asset paydowns, it would not exclude additional assets acquired into the pool with the proceeds of the paydowns." Note 555, *id* at 1579

[184] *Id* at 1579.

[185] *Id* at 1579.

[186] *Id* at 1579.

[187] *Id* at 1564 and 1565.

[188] "Under Rule 12b-25, the issuer must file a Form 12b-25 no later than one business day after the due date for the Form 10-D filing if all or any portion of the Form 10-D report is not filed in a timely manner. To obtain the filing extension, the Form 12b-25 must contain certain representations by the registrant, including why the inability to file timely could not be

in the best position with respect to the possession, responsibility and awareness of the information that would need to be reported on Form 10-D, namely, the depositor or servicer.

The content of Form 10-D consists of distribution and pool performance information for the distribution period and certain non-financial disclosure similar to those found in Form 10-Q. The table below sets out the disclosure items of Form 10-D.

Table 7: Form 10-D Disclosures[189]

Item 1	Distribution and pool performance information (Item 1121 of Regulation AB)
Item 2	Legal proceedings (Item 1117 of Regulation AB)
Item 3	Sales of Securities and Use of Proceeds (Item 2 of Part II of Form 10-Q)
Item 4	Defaults Upon Senior Securities (Item 3 of Part II of Form 10-Q)
Item 5	Submission of matters to a vote of Securities Holders (Item 4 of Part II of Form 10-Q)
Item 6	Significant obligors of pool assets (Item 1112(b of Regulation AB)
Item 7	Significant enhancement provider information (Items 1114(b)(2) and 1115(b) of Regulation AB).
Item 8	Other information
Item 9	Exhibits (Item 601 of Regulation AB)

Item 1 Form 10-D: Distribution and Pool Performance Information

This item relates to Item 1121 of Regulation AB relating to the information for distribution and performance of the asset pool during the distribution period. Since the types of information can substantially vary from issue to issue, Item 1121 sets out only illustrative examples of the types of information that may be included. The issuer is to provide "appropriate introductory and explanatory information…to introduce material terms, parties and abbreviations used…and statistical information should be presented in tabular and graphical formats, if such presentations will aid understanding."[190] The types of information that may be relevant might be thought of as any particular characteristic or fact which would effect an investor's calculation of the value of the asset-backed securities in question.

The illustrative items include amongst other things, the applicable dates, the cash flows received and their sources, distribution of the flow funds for the period itemized by type and priority of payment, including fees and expenses, payments with respect to enhancement, distributions to security holders and excess cash flows and so on. See Table 8 below.

eliminated without unreasonable effort or expense and that the subject Form 10-D filing will be made not later than the fifth calendar day following its original due date." If it is filed within the five days, then "it will be deemed to be filed on its original due date, including for purposes of Form S-3 eligibility." *Id* at 1565.

189 See, table entitled "Disclosure for Form 10-D," *id* at 1566.

190 *Id* at 1566.

Table 8: Distribution and Pool Performance Information – Item 1121(a)

(1) Applicable record dates: accrual dates, determination dates and distribution dates;

(2) Cash flows received and their sources (including portfolio yield, if applicable);

(3) Calculated amounts and distribution of the flow of funds for the period itemized by type and priority of payment, including fees and expenses, payments with respect to enhancement, distributions to security holders and excess cash flow and disposition of excess cash flow (e.g. excess cash flow released to the residual holder or other disposition, such as deposit into a transaction account[191]);

(4) Interest rates applicable to the assets and the asset-backed securities, as applicable, and interest rate information for pool assets in appropriate distributional groups or incremental ranges;

(5) Beginning and ending principal balances of the ABS;

(6) Amounts drawn on any credit enhancement or other support, and amounts still available (e.g. for internal credit enhancement or other support, this would not include application of subordination among classes, but would include use of reserve accounts[192]);

(7) Updated pool composition information for the period, such as the number and amount of pool assets at the beginning and ending of each period, weighted average coupon, weighted average life, weighted average remaining term, pool factors and prepayment amounts (e.g., for asset-backed securities backed by leases where a portion of the securitized pool balance is attributable to the residual value of the physical property underlying the leases, this information would include turn-in rates and the residual value realization rates[193]);

(8) Delinquency and loss information for the period (i.e., this would include "any material changes to how delinquencies, charge-offs and uncollectible accounts are defined or determined, including re-aging policies"[194];

(9) Amount, terms and general purpose of any advances made or reimbursed during the period;

(10) Material modifications, extensions or waivers to pool asset terms, fees, penalties or payments during the distribution period or that have cumulatively become material over time'

(11) Material breaches of pool asset representations or warranties or transaction covenants; and

(12) Information on ratio, coverage or other tests used for determining any early amortization, liquidation or other performance trigger and whether the trigger was met.[195]

---

[191] Note 474, *id* at 1566.

[192] Note 475, *id* at 1566.

[193] Note 476, *id* at 1566.

[194] Note 477, *id* at 1566.

[195] *Id* at 1566-1567.

These illustrative examples show the expansive nature of the types of disclosures that may be deemed material to the on-going reporting requirements of the issuer. However, the nature of these disclosures should be considered exceptional to the original precise definition of asset-backed securities as being discrete self-liquidating pool assets. That is, whatever event may cause the investor to have a different assessment of the value of the ABS, this should be disclosed. This concept is allied to the "transparency" requirement "…in those instances where the pool is changing not as a result of the assets converting into cash in accordance with their terms, but instead through external administration via an exception to the basic principle that the asset pool is discrete."[196]

It is important to note that "if the addition, substitution or removal of pool assets had materially changed the composition of the asset pool as a whole, full updated pool composition information required by Items 1110, 1111 and 1112 of Regulation AB would be required to the extent such information had not been provided previously."[197] Again this reporting requirement is allied to the basic principles-based definition of ABS such that if the value of the ABS is affected not by their conversion into cash, but by changes in external administration, then the disclosure of such changes is required.[198] In order to ease this rather burdensome disclosure requirement, updating the pool composition will be required only at set times when "a pre-funding or revolving period is in effect or new issuances have occurred from a mater trust and, in each instance, only if the information has materially changed form that previously provided."[199]

Table 9: Form 10-K ABS Disclosures[200]

Item	Existing Form Items	Required if applicable	May be omitted
1	Business		■
2	Properties		■
3	Legal proceedings		■
4	Submission of Maters to a Vote of Security Holders		■
5	Market for Registrant's Common Equity and Related Stockholder Matters		■
6	Selected Financial Data		■
7	Management's Discussion and Analysis of Financial Condition and Results of Operations		■
7A	Quantitative and Qualitative Disclosure About Market Risk		■
8	Financial Statements and Supplementary Data		■
9	Changes in and Disagreements with Accountants on Accounting and Financial Disclosure		■

[196] *Id* at 1567.

[197] *Id* at 1567.

[198] *Id* at 1567.

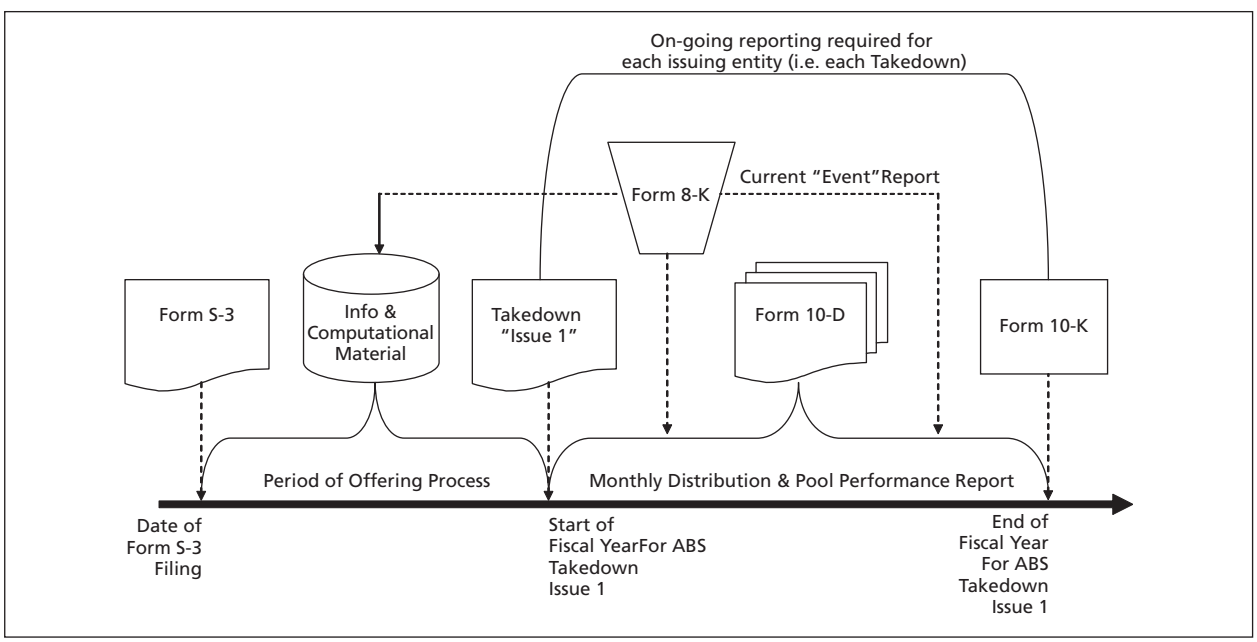
[199] *Id* at 1567.

[200] See *id* at 1569.

Item	Existing Form Items	Required if applicable	May be omitted
9A	Controls and Procedures		■
9B	Other Information	■	
10	Directors and Executive Officers of the Registrant		□
11	Executive Compensation		□
12	Security Ownership of Certain Beneficial Owners and Management		□
13	Certain Relationships and Related Transactions		□
14	Principal Accountant Fees and Services		■
15	Exhibits and Financial Statement Schedules	■	
	Additional Disclosure Items from Regulation AB	■	
1112(b)	Significant Obligor Financial Information	■	
1114(b)(2) & 1115(b)	Significant Enhancement Provider Financial Information	■	
1117	Legal Proceedings	■	
1119	Affiliations and Certain Relationships and Related Transactions	■	
1122	Compliance with Applicable Servicing Criteria	■	
1123	Servicer Compliance Statement	■	

A summary of the major disclosures required over a timeline from the filing of the shelf registration on Form S-3 to the annual report required for each takedown is illustrated in the Figure below.

Figure 6: Major Disclosures for ABS



3.1.9 Schematic Summary

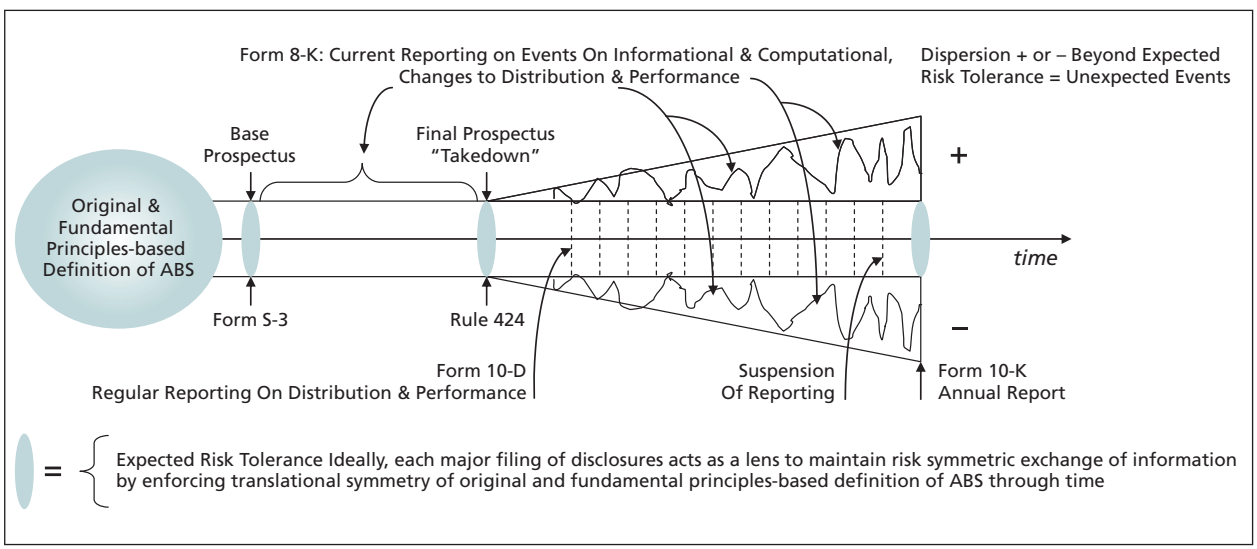
The filing of Form S-3 initiates the period of the offering process during which time the issuer may provide informational and computational materials to potential investors. At the time of the first takedown, the fiscal year of that particular issue begins and the issuer is then responsible to produce periodic reports on Form 10-D. These periodic reports are filed within 15 days of distribution which normally occur on a monthly basis.

These periodic reports on Form 10-D are supplemented with current reports concerning events which represent material changes to previous filings. Finally, at the end of the year for a particular takedown issue, a Form 10-K annual report is filed. If there are less than 300 holders of the security then the duty to report is "suspended" and there will be no need to file any other reports.[201]

3.1.10 Towards a Theoretical Comparative Benchmark for ABS Regulations

Given the range and depth of disclosures for ABS under the US approach, one would be forgiven for getting lost amongst the hideously sprawling mess, 97 pages of 8-point type that purportedly attempts to simplify "the process of registering an offering of asset-backed securities"[202] and forgetting that there is an underlying overall pattern in which the dense canopy of rules appear. That is, if we step back, it is possible to see that the entirety of the US ABS framework in terms of translational and bilateral symmetries, where the original definition of asset-backed security is preserved through time by the action of various disclosure requirements. See Figure below.

Figure 8: Schematic of US ABS Regulatory Approach – Lensing of Disclosures



[201] *Id* at 1561. "If the duty to report is suspended, a Form 15 is required to be filed 30 days after the beginning of the first fiscal year it is suspended. See Exchange Act Rule 15d-6 (17 CFR 240.15d06). See also Exchange Act Rule 12h-3 (17 CFR 240.12h-3)." Note 432, *id* at 1561.

[202] *Id* at 1591.

In the Figure above, we see the US set of disclosures for an ABS shelf registration through time. In this highly simplified figure, the original principles-based definition of asset backed security[203] is preserved through disclosures that exhibit a translational symmetry of the original ABS definition at specific points in time. In other words, each set of disclosures should be ideally an application of the original definition. On the left of the Figure, the original and fundamental principles-based definition of asset backed securities is the ultimate source for the regulations of ABS. This is not to say the definition itself is not fraught with numerous special conditions.[204] However, it is clear that the general principles-based definition of asset-backed securities including its special conditions[205] is the ultimate test for determining whether any particular item is required to be reported.

The principles-based definition guides the lawmakers in establishing a set of laws which are aimed at, amongst other things, overcoming dysfunctional information asymmetry.[206] Through time this original and fundamental definition of asset backed securities is preserved by a set of filings which might be considered "lenses" for the sake of analogy. That is, the "lenses" focus on the expected or the unexpected risks of the transaction at particular moments in time which should have the effect of reducing dysfunctional informational asymmetry. These expected risks are reported on a periodic basis and the unexpected risks are reported on a "current" basis so that the overall integrity of the transaction structure is maintained over time.

The major disclosures in a shelf registration Form S-3 forms the base prospectus which acts as an initial lens that defines the possible types of ABS tranches in the future and the disclosures therein define the expected risk tolerance of the transaction for the transacting parties. During the offering process, after the filing of the Form S-3 and before a successful takedown where a final prospectus is filed pursuant to Rule §230.424,[207] the issuer provides large amounts of statistical information concerning the quality of the underlying assets to potential investors for analysis. This informational and computation material is provided under Item 6.01 on Form 8-K which is filed by the issuer.

After a takedown, periodic reporting on the distribution of the pool and performance of pool assets are reported on Form 10-D. Since by definition, the discrete pool of self-liquidating assets determines the pool, the reporting on Form 10-D constitute the expected risk tolerance of the transaction. Similarly, exceptional

[203] See Regulation AB, §229.1101(b) that sets out the definition of an asset backed security: "*Asset-backed security* means a security that is primarily serviced by the cash flows of a discrete pool of receivables or other financial assets, either fixed or revolving, that by their terms convert into cash within a finite time period, plus any rights or other asset designed to assure the servicing or timely distributions of proceeds to the security holders; provided that in the case of financial assets that are leases, those assets may convert to cash partially by th cash proceeds from the disposition of the physical property underlying such leases."

[204] See, Regulation AB, Item 1101(c) *et seq*.

[205] See, Regulation AB, Item 1101(c)(2) *et seq*.

[206] In referencing to the effect of requiring in-depth criteria concerning servicing criteria, the Federal Law states: "This should promote investor confidence and market efficiency by decreasing information asymmetries and promoting more efficient pricing and valuation of the securities." US Final Rule Asset-Backed Securities, at 1592.

[207] *Id* at 1579.

reporting in the form of changes to distribution and performance are made on Form 8-K under Items 6.02 through 6.04. These events would represent unexpected risk events, that is, beyond the expected risk tolerance defined in the risk lens of a final takedown prospectus and previously filed Form 10-Ds. Along the same lines, if the changes affect the definition or scope of the transaction itself, then the issuer would be required to file a amendment to the Form S-3 in order to re-set the original risk tolerance.

As per Securities Exchange Act of 1934, the reporting requirements are put into suspension at the end of any fiscal year where the number of security holders is less than 300. Since most takedowns have significantly less than 300 security holders, most will stop reporting at the end of the first fiscal year and the last filing will be in the Form 10-K which will require exhibits on the servicing compliance and an attestation relating to servicing criteria by a registered public accountant.

The figure on lensing of disclosures helps us visualize some of the major features of an asset backed securities transaction in terms of not only overcoming information asymmetry at specific points in time but also preserving the integrity of the transaction through time in terms of translating the original definition of asset-backed security into disclosures of expected risk tolerance and unexpected risk events. We will use this model to help us define for comparative purposes some of the essential aspects of asset-backed securities disclosure requirements in the EU and Russia. Before we turn to the ABS disclosure regimes in the EU and Russia, let us examine some of the competitive issues relating to regulatory disclosures.

3.1.11 Policies for Establishing ABS Regulation: Competition, Promotion of Efficiency and Capital Formation

Under US securities law, new rules need to be justified in terms of their competitive impact. Thus, if a proposed rule were "to impose a burden on competition not necessary or appropriate in furtherance of the purposes of the Exchange Act,"[208] it would be prohibited. The test under Section 2(b) of the Securities Act and Section 3(f) of the Exchange Act is that the law makers in determining whether an action is necessary or appropriate in the public interest should consider four factors: (1) protection of investors, (2) efficiency, (3) competition and (4) capital formation.[209] These factors could also be treated as objectives of the regulation.

The argument is that since the new ABS rules are formal codifications of numerous informal industry and staff practices,[210] the rules should enhance capital formation by simplifying the process of ABS registration. Despite literally hundreds of new disclosures rules, establishing clear and transparent disclosure requirements should lower the barriers to entry for ABS, and at the same time, enhance efficiency and increase the competitiveness of the U.S. capital markets for asset-backed offerings.[211] Despite these positive benefits, the US lawmakers'

[208] *Id* at 1591, citing Section 23(a)(2) of the Exchange Act.

[209] *Ibid.*

[210] *Ibid.*

[211] *Ibid.*

attitude towards the issue of competition for capital formation appears rather hopeful or wishful rather than persuasive.

With the advantage of hindsight, the major unintended consequence of the new ABS regulations is that the costly burden of increased periodic and current reporting has provided investors a firm basis for making short term decisions about ABS, increasing short-term volatility within the first year of issuing the final prospectus. Thus, sub prime debacle starting from February 2007 could ironically be a direct consequence of increased reporting required under the new ABS regulations.

This was completely unanticipated by the lawmakers since they considered the only "indirect negative effects" of the new ABS regulation to be potentially the migration of ABS markets to private or foreign markets having a comparatively lesser burden of disclosure than under the new ABS regulations.[212] The lawmakers do not really give any good reasons against the cost-based argument except to state in a rather *non sequitur* fashion that the "large size of the U.S. registered ABS market and potential regulatory or investment restrictions on the ability of investors to purchase non-registered ABS"[213] would make the unintended consequence of losing market share rather unlikely. Ironically, the point of the cost-based argument is the very fact that the U.S. market is so large makes it vulnerable to competition and loss of market share should other jurisdictions offer efficient and transparent processes at less cost to the issuer.

The U.S. lawmakers believe that anything less than the U.S. requirements would be seen as inferior or lacking in transparency and therefore would suffer from decreased investor confidence and presumably, be thought less worthy from an investors' perspective.[214] We must point out that other jurisdictions with less developed asset-backed securities markets are likely to want less burdensome regulatory disclosures in order to spur capital formation. Moreover, given the large number of issues of ABS in Europe, the US lawmakers' argument appears presumptuously overstated. Given the reality of competition at a global level for ABS, it would appear that the cost-based argument is an important factor in a comparative analysis of ABS regulatory regimes.

However, our studies reveal that the US regulatory approach offers a complete set of disclosures for overcoming dysfunctional asymmetry through an extended time-frame. This completeness of disclosures not only at specific points in time, but also through time, makes the US shelf registration process for ABS an exemplar for transparency and governance. We shall use an abstracted version of this set of complete disclosures as a model (see "Lensing of Disclosures" Figure above) and the basis of comparison for the EU and Russian regulations relating to asset-backed securities.

212 *Id* at 1592.

213 *Ibid.*

214 *Ibid*.

3.1.12 Overcoming Dysfunctional Information Asymmetry — Technical Information

In general, there are two critical periods for determining the value of the asset-backed securities: (1) during the offering process, after the base prospectus and before the takedown, or more specifically, during the negotiations period before the acceptance of the takedown prospectus; and (2) after the takedown prospectus during the first year period. The US Final Rule on Asset-Backed Securities sets out detailed disclosure requirements for both periods. Whilst there are numerous potential disclosures required, the Federal law is keen to emphasize that such items should be disclosed only if material to the investor's decision making.

The approach of the regulation is based on a principles-based concept of having an original definition of asset-backed security and then illustrating various types of specific disclosures that might be deemed material to an investor. It is then within the discretion of the issuer to use these exemplars of disclosure to formulate its own set of disclosures that fall within the definitional ambit of the specific disclosure item of Regulation AB. Obviously, the difficulty with this approach is that it appears to require the issuer to second-guess the information needs of potential investors. However, this approach also allows a formal consolidation of previous market practice as well as a certain amount of flexibility for market participants to determine appropriate material disclosures for future market instruments.

We will not prise all of the technical details for pre-takedown disclosures or all of the possible reporting in the post-takedown period since these can be found by a close reading of Regulation AB. However, given our theoretical benchmark model (see Figure xx above), we assume that the most relevant and material information to potential investors outside that required for the business identification purposes of the transaction parties and the financial information required to evidence their financial credibility is information relating to the underlying assets of the pool and the servicing of these assets.

The actual form and performance of the asset-backed securities themselves, howsoever agreed, including their "waterfall" characteristics or priority of payments, specific conditions and embedded options are themselves specific legal and financial features of particular securities that ultimately depend on the payment characteristics of the underlying pool assets. Therefore, for purposes of establishing a theoretical comparative benchmark for what might be deemed the major material risk items for the determination of the value of the transaction, the investors will mainly rely on:

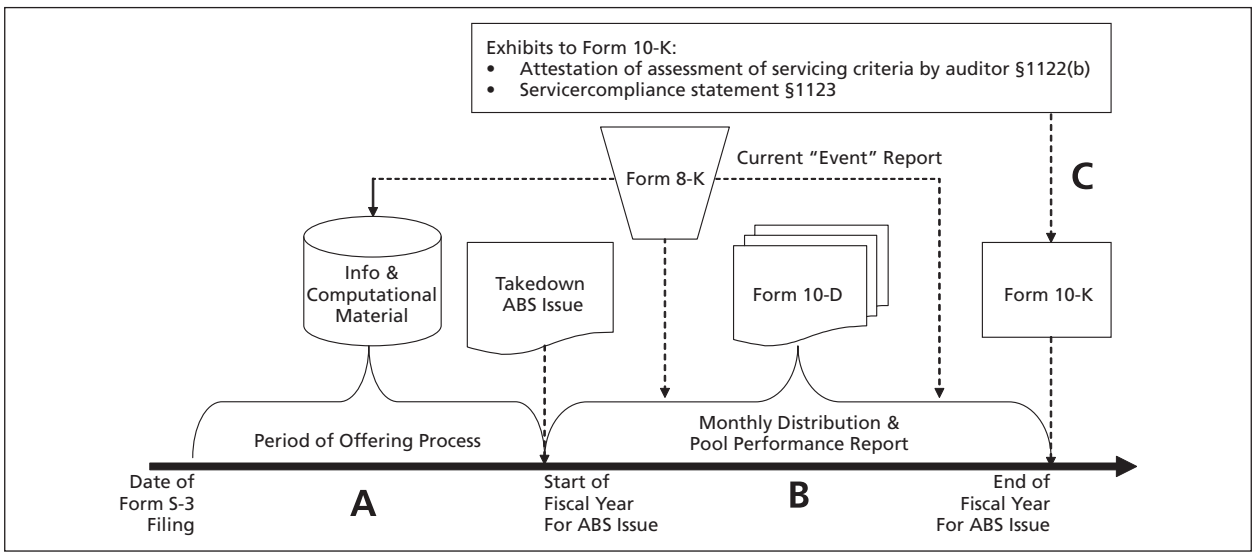
(A) the Informational and Computational Material of Item 1101(a) for the offering process period;

(B) the Distribution and Pool Performance Information of Item 1121 for the post-takedown period; and

(C) the servicing criteria contained in Item 1122 on Compliance with Applicable Servicing Criteria.

This set of technical disclosures form a triad that are most likely to affect investor decision making in the most direct and dramatic manner.

Figure 9: Major Disclosures to Overcome Dysfunctional Information Asymmetry



A failure in reporting or drastic changes to the disclosures provided in (A), (B) or (C) is likely to result either in transaction failure or catastrophic meltdown of the value of the securities in question. Again referring to our comparative benchmark model, the integrity (or more specifically, the translational symmetry) of the transaction through time should be reflected in a consistency of disclosures between (A), (B) and (C). In order to establish a basis for a comparative benchmark of technical disclosures of ABS, we have re-formulated disclosure items of (A), (B) and (C) within the STRIDE questionnaire with a very brief commentary on some of the items.

We hope that this checklist may be helpful to those engaged in international asset-backed securities. This triad of disclosures will also be helpful in making a comparative analysis of the technical disclosures required under EU and Russia regulations. The following tables set out high-level summary of the disclosure items of (A), (B) and (C) that are extracted from relevant sections of Regulation AB and which may be used as a basis for international comparison.

Table 10: Summary of Informational and Computational Materials — Item 1101(a) (1)–(5)

The "Information and Computational Materials" contains factual statements relating to:

- the measurement parameters and legal characteristics of the asset-backed securities;
- the origination and contractual characteristics of the pool assets underlying the asset-backed securities;
- identification of the key transaction parties,
- static pool data relating to the sponsor's and/or servicer's portfolio, prior transactions or asset pools; and
- Statistical data on particular classes of asset-backed securities.

Table 11: Summary of Distribution and Performance Information — Item 1121

The "Distribution and Performance Information" sets out the type of information required relating to the asset pool during the distribution period. The presentation of this information may be in tabular or graphical format. This includes amongst other things:

- relevant dates for recordation of accrual, determination and distribution
- cash flow
- flow of funds
- applicable interest rates
- amounts drawn on credit enhancement or other support
- pool composition information such as weighted average coupon, weighted average life, weighted average remaining term, pool factors and prepayment amounts
- delinquency and loss data
- any advances or reimbursements during the period
- any material modifications, extensions or waivers
- any material breaches to pool asset terms
- information on ratio tests relating to early amortization, liquidation or other performance triggers

Table 12: Summary of Compliance with Servicing Criteria — Item 1122

The compliance report on the servicing criteria contains:

- Statement of responsibility for assessing compliance with servicing criteria;
- Statement that party used the specific items stated in §1122(d) relating to "applicable servicing criteria";
- That the period covered is the fiscal year stated in the annual report Form 10-K and any non-compliance over that period;
- That a registered public accounting firm has issued an attestation report covering the servicing criteria over the stated fiscal year period.

Servicing Criteria (Item 1122(d)) covers:

- *General servicing considerations*

  These define the capability of the servicer to monitor the performance, triggers and events of default in accordance with the transaction agreements, including outsourced servicing contracts, back-up servicer agreements and fidelity bond and errors and omissions policies.

- *Cash collection and administration*

  This sets out details for the payments on the pool assets, their accounts, disbursements, advances or guarantees, related accounts to the transactions such as cash reserve and overcollateralization and reconciliations.

- *Investor remittances and reporting*

  This provides for reports to investors as per transaction agreements and filed with the SEC and contains amounts due to investors.

- *Pool asset administration*

  This section relates to collateral or security on pools assets, additions, substitutions or removals to the asset pools and details relating to payments on the pool assets.

In comparing the information required for (A), (B) and (C), we note that in all three periods the focus is on the factors affecting the payments of the pool assets (the assets underlying the asset-backed securities) and the assets pool (the asset-backed securities). In the negotiation (called the "offering process period post-filing of the Form S-3 registration statement), the five components concern the asset-backed securities, the pool assets, the key transaction parties, the static pool relating to the servicer and/or sponsor, and statistical data relating to particular classes of asset-backed securities. This information, especially that relating to the cash flow of the underlying assets and the pool, enables the investor to make a calculation as to the value of particular classes of asset-backed securities. According to our risk symmetry model, if there is sufficient information to overcome the dysfunctional information asymmetry barrier, then the investor will make a positive decision to invest in the asset-backed security. This also creates a situation where there is an expected risk tolerance during the life of the asset-backed securities.

In the post-takedown period, the reporting should allow the investor to monitor the actual performance of the pool assets against the expected pay out from the asset-backed securities. The disclosures in this period should facilitate an assessment of how well particular asset-backed securities are performing in relation to previous expectations.

Finally, at the time of the annual report with the filing of the Form 10-K, the provenance of the figures from the period are confirmed by virtue of the assessment report that the servicer has complied with the applicable servicing criteria. One of the key features, which reduces the risk of fraud or erroneous practices is the attestation report signed by the registered public accountant that the servicing criteria have been complied with.

This is a real concern of investors who would otherwise have no choice of verifying valuation statements except by sponsors who may also be originators. This type of fraud by the servicer/sponsor has been alleged in a Parmalat case[215] where the amount collected by the servicer was overstated over a period of four years. The purported fraud was discovered only after the Parmalat bankruptcy trustee instructed auditors to investigate the self-audited Citigroup securitization programme.

[215] See, *Bondi v Citigroup*, Complaint filed July 29, 2004, Superior Court of New Jersey, County of Bergen.

3.2 EU approach

3.2.1 Introduction

The regulatory approach of the European Union for asset-backed securities comes under the framework Level I EU Prospectus Directive[216] (PD) and the more specified Level II EU Prospectus Directive Regulation[217] (PD Regulation) and the specific Level III implementation the PD Regulation in each of the Member States. The Level III is usually a direct lift of the Level II language, and therefore, we shall confine our discussion to the EU Level II, wherein most of the references will be to the PD Regulation or the PD. Since Regulations must be implemented by Member States, there is a theoretical legal necessity for consistency between Member States regarding the form of disclosures required for asset backed securities. Whilst the reporters have not compared all Member States level III laws relating to asset backed securities, we realize that the legal authorities and regulatory structure governing asset-backed securities in Europe vary widely.

However, for purposes of comparison to the US Regulation AB, we will focus mainly on the PD Regulation's Annex VII and VIII which set out the disclosure requirements for the "registration document" and "securities note". Since we have already discussed why US asset-backed securities are most likely to conform to the requirements of shelf registration,[218] we will compare the formal requirements of shelf registration between the US and EU regulations. Our aim is to analyse the broadly similar principles and elements of disclosure common to both the US and EU regulatory regimes with the aim of determining a principles-based and risk aware framework that is consistent with our overall view of encouraging regimes towards convergence.

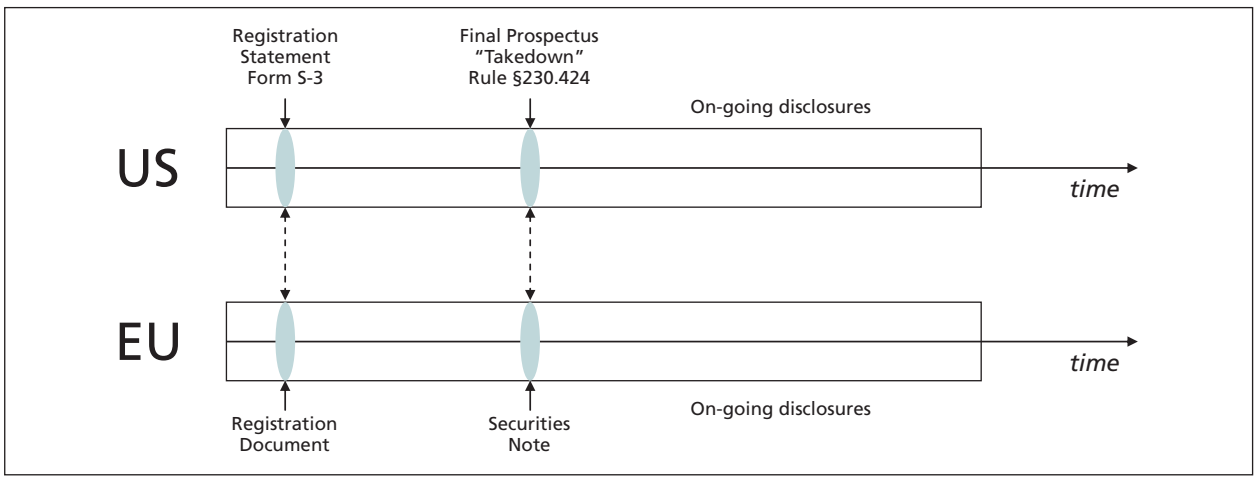
In very broad terms, one parallel can be drawn between the US Form S-3 for shelf registration and the registration document required under the PD Regulation and another parallel can be drawn between the US final takedown prospectus and EU securities note. Using our comparative benchmark model, we have the following figure.

[216] See, EU Prospectus Directive 2003/71/EC.

[217] See, Commission Regulation (EC) No. 809/2004, EU Prospectus Directive Regulation.

[218] Basically, the shelf registration process provides an efficient method for the issuer to overcome dysfunctional information asymmetry and to achieve a risk symmetric position.

Figure 10: Similarities of Shelf Registration for US and EU ABS



But how similar are (1) the disclosure requirements of the EU registration document and the US registration statement and (2) the subsequent EU securities note and the US takedown? To determine the similarities for registration, we can compare the specific line items required under PD Regulation Annex VII "Minimum Disclosure Requirements for Asset Backed Securities Registration Document" with the items required under the US Form S-3, the registration statement. For a summary of the major items required for the EU registration document and the US registration statement, see the two tables below.

Table 13: Summary of EU PD Regulation Annex VII Minimum Disclosure Requirements for ABS Registration Document

Section	Title
1	Persons responsible
2	Statutory auditors
3	Risk factors
4	Information about the Issuer
5	Business overview
6	Administrative, management and supervisory bodies
7	Major shareholders
8	Financial information concerning the Issuer's assets and liabilities, financial position, and profits and losses
9	Third party information and statement by experts and declarations of any interest
10	Documents on display

Table 14: Summary of US Form S-3 Disclosure Items

Item	Title
1	Forepart of Registration Statement and Outside Front Cover page of Prospectus
2	Inside Front and Outside Back Cover Pages of Prospectus
3	Summary information, Risk Factors and Ratio of Earnings to Fixed Changes
4	Use of Proceeds
5	Determination of Offer Price
6	Dilution
7	Selling Security Holders
8	Plan of Distribution
9	Description of Securities to be Registered
10	Interests of Named Experts and Counsel
11	Material Changes
12	Incorporation of Certain Information by Reference
13	Disclosure of Commission Position on Indemnification for Securities Act Liabilities
14	Other Expenses of Issuance and Distribution
15	Indemnification of Directors and Officers
16	Exhibits
17	Undertakings
Additional Disclosure Items from Regulation AB Items 1102 – 1120 of Regulation AB	
1102	Forepart of registration statement and outside cover page of the prospectus
1103	Transaction summary and risk factors
1104	Sponsors
1105	Static pool information
1106	Depositors
1107	Issuing entities
1108	Servicers
1109	Trustees
1110	Originators
1111	Pool assets
1112	Significant obligors of pool assets
1113	Structure of transaction
1114	Credit enhancement and other support, except for certain derivative instruments
1115	Certain derivatives instruments
1116	Tax matters
1117	Legal proceedings
1118	Reports and additional information
1119	Affiliations and certain relationships and related transactions
1120	Ratings

From the two tables above, it may appear that the US requires more disclosures for ABS transactions than the EU. However, the difference is more subtle.

That is, whilst the US may appear to require more items of disclosure, it is important to note that many of the disclosures are left to the discretion of the issuing entity to determine whether and to what extent they may be material to an investor's decision making. In a similar vein, the EU requires the issuer to make disclosures that are sufficient enable investors to make an informed assessment. The question is the whether the US doctrine of material information is for all intents and purposes the same as the EU doctrine of sufficient information when it comes to practitioners being allowed to determine the types and extent of disclosures.

It is arguable that the US regulation merely provides *more guidance* to the practitioners as to what types of disclosures may be relevant than does the EU regulation. Whilst it may be argued that they are differences at the margins, the fundamental principle both share is that they are both aimed at closing the information gap between the issuer and investor, and reducing dysfunctional information asymmetry. Both regimes assume that the issuer can anticipate the information needs of the investor and explicitly fulfil these needs with the requisite disclosures. At the margins, outside the set of simply identifying the parties or transaction agreements, the explicit disclosure items are stated either in general catch-all terms which is the preferred method of the EU or by way of specific illustrations which is the preferred way of the US.

In both instances the underlying hope and belief is that market practitioners will find the appropriate disclosures. In effect, the EU method allows market practitioners to determine what later may become market conventions for specific types of "sufficient information". The US approach recognizes that market practice has already been developed and is looking to help consolidate already existing practices. In both jurisdictions, the regulatory intent is to encourage innovation with regulations that may be flexibly interpreted.

Without making a detailed comparison of how these regulatory disclosures are implemented in practice in each jurisdiction and examining only the regulatory requirements themselves, it would appear that there is a rich commonality between the disclosure requirements for the registration of ABS in the US and the EU. Major disclosure items such as the identification of the transaction parties and the transaction agreements are part and parcel of both regimes as well as a description of the risk factors that may be relevant and material to the transaction. However, there are significant differences between the two regimes in terms of apportioning liability and the formalities or administrative rules relating to specific disclosures for transaction parties and agreements.

Even on a cursory reading, the US provides more explicit definitions of the transaction parties that the EU, as well as more specific illustrations of the types of disclosures relevant to the pool assets and has a stricter regime relating to the reliability and history of the reporting of the reporting agents, requiring them to refer previous reporting disclosures or disallowing them to qualify should they be delinquent in other related asset-backed securities filings.[219] Most importantly, the U.S. disclosure regime provides for significant new reporting

[219] Regulation AB, Item 1104 on "Sponsors", 1106 on "Depositors", 1107 on "Issuing entities", 1108 on "Servicers", 1109 on "Trustees", 1110 on 'Originators", Item 1111 on "Pool assets", 1118 on "Reports and additional information".

of "static data",[220] "on-going reporting",[221] servicing criteria compliance by the servicer,[222] and attestation by an external auditor of servicing compliance.[223]

In terms of apportioning liability, it is critical for would-be foreign issuers who wish to take advantage of the US securities system by registration to understand that they would have to submit to the potential criminal and civil liabilities of the US Sarbanes Oxley Act in their personal capacity. This is because whilst the US Final Rule on Asset-backed Securities dismisses the need to have the issuing entity comply with Section 404 internal control requirements,[224] which is a boon since it poses substantial auditing and consulting fees, the Final Rule nevertheless requires the issuing entity to comply with Section 302 of Sarbanes Oxley.[225] This means that senior officers of the servicer and originators (either depositors or sponsors) will be required to sign in their individual capacity and face not only potential liability for knowing violations of Sarbanes Oxley of $1 million and up to 10 years imprisonment per violation, but also for wilful violations, of $5 million and 20 years imprisonment per violation.

In terms of the formalities or administrative rules relating to the transaction parties and transaction agreements, we note that the EU does not positively list or define the major transaction parties while the US does. The EU focuses mainly on disclosures required of the issuer. We may say that the EU has an "issuer-centric" view of ABS disclosures where practically all of the disclosure requirements are the responsibility of the issuer to execute. In sharp contrast, the awareness and responsibilities relating to relevant information for US transactions is distributed amongst the transaction parties.

Thus, the US provides substantial guidance on the pivotal actors in an asset-backed transaction, identifying: (1) "asset-backed issuer";[226] "issuing entity";[227] "sponsor";[228] "depositor";[229] "obligor";[230] "significant obligor";[231]

220 Regulation AB, Item 1105 on "Static pool information".

221 Regulation AB, Item 1121 on "Distribution and pool performance information".

222 Regulation AB, Item 1123 on "Servicer compliance statement" and Item 1122(d) "Servicing criteria".

223 Regulation AB, Item 1122(b) "Registered public accounting firm attestation reports".

224 See, Final Rule on Asset-backed Securities (2005) at 1510.

225 An issuer of asset-backed securities is required to file a Section 302 certification. *Ibid.*

226 §229.1101(a)(8).

227 See, §229.1101(f); and §229.1107 which sets out the specific disclosure requirements.

228 See, §229.1101(l); and §229.1104 which sets out the specific disclosure requirements.

229 See, §229.1101(e) where the "*Depositor* means the depositor who receives or purchases and transfers or sells the pool assets to the issuing entity. For asset-backed securities transactions where there is not an intermediate transfer of the assets from the sponsor to the issuing entity, the term depositor refers to the sponsor."

230 See, §229.1101(i) for the definition of an obligor.

231 See, §229.1101(k) for definition of significant obligor and the substantial disclosure obligations under §229.1112.

"trustee";[232] "originator";[233] "servicer";[234] and the "nationally recognized statistical rating organization" or "NRSRO" commonly known as a credit rating agency.[235] As a general recommendation, which we shall return to later, a regulatory regime for ABS which defines the roles of the potential transaction parties is more likely to provide for the types of disclosures which allow investors to overcome dysfunctional information asymmetry because the disclosures are aligned to the functional requirements of the parties in the ABS transactional structure.

As there are practically no definitions of the relevant parties to transaction under the EU law, our comparative analysis of the relevant regulations for transaction parties is narrowly focused on the duties of the concept of the Issuer as found under the EU Prospectus Regulation versus the concept of "issuing entity" and "issuer" under the US Regulation AB.

Again it is important to emphasize that whilst the EU is silent on the definition of the numerous parties in an ABS transaction, it does require that disclosures be made of "all persons responsible for the information given in the Regulation Document." Of course, being disclosed as a party responsible for certain information on a Registration Document is a completely different level of potential liability to someone who signs a Section 302 Certification for reporting under the US securities laws.

3.2.2 The Issuer

The issuer ideally is the legal entity that owns the pool assets and has the legal authority to transfer the title and rights of the pool to investors. Superficially, the US appears to downplay the importance of the issuer in the eyes of the presumed investor, since the issuer is merely a passive holder and is not necessarily the party who will have the information on the underlying assets which the investors need in order to make an informed decision.

[232] Regulation AB does not have a definition of "trustee" but has disclosure requirements for it under §229.1109.

[233] Regulation AB does not provide a definition of "originator" but does require identification of any originator or group of affiliated originators apart from the sponsor or its affiliates that originate or expect to originate 10% or more of the pool assets" and a business description for originators that originate or expect to originate 20% or more of the pool assets. §229.1110 Originators.

[234] See, §229.1101(j) for a definition of servicer; §229.1122 for the assessment of the servicing criteria; and §229.1123 for the "Servicer compliance statement".

[235] See, §229.1101(h) for the definition of NRSRO which refers to §240.15c3-1(c)(2)(vi)(F) The important point of the ratings is found in §229.1120, which requires disclosure on "whether the issuance or sale of any class of offered securities is conditioned on the assignment of a rating by one or more rating agencies, whether or not NRSROs." If this is the case, then the issuer must "identify each rating agency and the minimum rating that must be assigned" and to "describe any arrangements to have such rating monitored while the asset-backed securities are outstanding." *Id* at §229.1120. Given the importance of contingent ratings to the valuation of practically all asset backed securities, this provision may provide some indication of the moral hazard of the dependency on the rating agency's "advise" to determine the ultimate credibility of the transaction to investors. However, there is no explicit ground for holding the credit rating agency liable for such information. Perhaps, a Section 302 Sarbanes Oxley certification would be too much to impose on credit rating agencies, but something along the lines of "servicing criteria compliance" or "credit rating criteria compliance" should be developed for the sake of investor protection, especially, for the reporting period after a final prospectus during which there may be a strong secondary market reliance on stale credit rating opinions.

Where the issuing entity is the owner of the assets then a substantial amount of information is required to be disclosed about the business nature of the issuing entity and its solvency.[236] However, in keeping with downplaying the substantive importance of the issuing entity in an ABS transaction, the US rule does not require audited financial statements for the issuing entity under either the Securities Act or Exchange Act filings.[237]

Under the EU law, the issuer is considered one of the persons responsible for giving information in the registration document[238] and will need to state on the Registration Document whether it is a special purpose vehicle or entity for the purpose of issuing asset backed securities."[239] The EU disclosure requirements for the ABS Registration Document focuses on a number items relating to the Issuer including "information about the issuer" including its: legal and commercial name;[240] place of registration and registration number;[241] date of incorporation and length of life;[242] domicile and legal form, legislation under which it operates, country of incorporation and address and telephone numbers;[243] amount of authorised and issued capital, and the amount of any capital agreed to be issued, number and classes of the securities of which it is composed.[244] The Registration Document also requires a description of the business overview of the issuer,[245] including its principal activities, and a global overview of the parties to the securitisation program including information on the direct or indirect ownership or control between those parties,[246] its administrative management and supervisory bodies, major shareholders and a long disclosure item on financial information concerning the issuer's assets and liabilities, financial position, and profits and losses.[247] Comparing the EU disclosure requirements for the issuer to those of the US Regulation AB, we see that there is a substantial overlap between the two jurisdictions.

The US Federal Law on the Final Rule on Asset-backed Securities recognizes the pivotal role of the issuing entity to asset-backed securities since it is functionally required to accomplish the legal transfer of pool assets. The issuing entity is usually a trust or other corporate entity established "at the direction of the sponsor or depositor that owns or holds the pool assets and in whose name the asset-backed securities supported or

236 See, §229.1107 on issuing entities.

237 Final Rule Asset-Backed Securities, at 1533.

238 PD Regulation, Annex VII, section 1.1.

239 *Id* at section 4.

240 *Id* at section 4.2.

241 *Id* at section 4.3.

242 *Id* at section 4.4.

243 *Id* at section 4.5.

244 *Id* at section 4.6.

245 *Id* at section 5.

246 *Id* at sections 5.1 and 5.2.

247 *Id* at section 8.

serviced by the pool assets are issued."[248] The US disclosure requirements for the issuing entity are similar to the EU's in that the issuer's permissible activities, restrictions on activities and capitalization need to be revealed.[249] And "if the issuing entity has its own executive officers, board of directors or persons performing similar functions," then disclosures under Items 401, 402, 403 and 404 of Regulation S-K will be required.[250] Other disclosures items include:

(1) governing documents[251] of the issuing entity filed as an exhibit to Form S-3 or incorporated by reference as a filing on Form 8-K, which includes all the transaction documents where the issuing entity is a signatory, e.g. the pooling and servicing agreement, the indenture and related documents, and the management or administration agreement of the issuing entity;[252]

(2) a narrative of the sale or transfer of the pool assets and a graphical representation or flow chart depicting the transaction structure "if it will aid understanding";[253]

(3) discussion of creation and perfection and priority status of any security interests for the benefit of the transaction;[254]

(4) any expenses relating to the selection and acquisition of the pool which are payable from the offering proceeds;[255] and

(5) the amounts paid or to be paid for the pool assets limited to instances where the pool assets are securities as per the Securities Act and "requiring disclosure of the market price of the securities and the basis on which the market price was determined."[256]

Importantly, the US approach also provides discretion to the issuing entity to disclose to the extent material the legal and structural complexities of the ABS transaction,[257] including:

248 *Id* at 1534.

249 *Id* at 1534.

250 *Id* at 1534 and §229.1107(e).

251 *Id* §229.1107(a).

252 *Id* at 1535.

253 *Id* at 1535 and §229.1107(h).

254 *Ibid* and §229.1107(k)(1).

255 *Id* at 1535 and §229.1107(j).

256 *Id* at 1535. The Final Rule of Asset-backed Securities (2005) states that it "continues to support disclosure of such information in those securitizations, such as corporate debt securitizations or ABS repackaging." These types of instruments are theoretically close to OTC instruments such as collateralized debt obligations.

257 *Id* at 1535.

(a) The legal status of any security interests granted in relation to the transaction, whether perfected, maintained or enforced;[258]

(b) Any declaration of bankruptcy, receivership or similar proceeding that can be made against the issuing entity;[259]

(c) In case of a bankruptcy, receivership or similar proceeding with respect to the sponsor, originator, depositor or other seller of the pool assets, the issuing entity's assets will become part of the bankruptcy estate or subject to the bankruptcy control of a third party[260]

(d) In case of a bankruptcy, receivership or similar proceeding with respect to the issuing entity, the issuing entity's assets become subject to the bankruptcy control of a third party.[261]

Although all of the above are technical legal issues, the US Final Rule on ABS does not require the filing of any expert report or opinion regarding any of the above but does allow the registrants to file such voluntarily subject to applicable consents.[262]

The EU's disclosure requirements for transaction parties are found in general terms for the Registration Document (Annex VII) and in more specific terms for the securities note (Annex VIII). In Annex VII, the relevant sections relating to transaction parties are as follows:

Table 15: Transaction Parties Implied by EU Prospectus Regulation, Annex VII for Registration Document

Section	Language relating to Transaction Party	Type of Transaction Party
1.1	"All persons responsible for the information given in the Registration Document and, as the case may be, for certain parts of it, with, in the latter case, an indication of such parts. In the case of natural persons including members of the issuer's administrative, management or supervisory bodies indicate the name and function of the person; in case of legal persons indicate the name and registered office."	Any and all parties who provide information in the Registration Document
2.1	Names and addresses of the issuer's auditors for the period covered by the historical financial information (together with any membership of any relevant professional body).	Statutory auditors

[258] §229.1107(k)(1).

[259] §229.1107(k)(2).

[260] *Id* at 1535 and §229.1107(k)(3).

[261] *Id* at 1535 and §229.1107(k)(4).

[262] For applicable consents, see Securities Act Rule 436 (17 CFR 230.436).

Section	Language relating to Transaction Party	Type of Transaction Party
4	Information about the Issuer	Issuer
5.2	"A global overview of the parties to the securitisation program including information on the direct or indirect ownership or control between those parties."	▪ Any and all parties directly involved in the securitisation program ▪ Parties who own and control such parties
6.1	"Names, business addresses and functions in the issuer of the following persons, and an indication of the principal activities performed by them outside the issuer where these are significant with respect to that issuer: (a) members of the administrative, management or supervisory bodies; (b) partners with unlimited liability, in the case of a limited partnership with a share capital.	▪ Members of administrative, management or supervisory bodies ▪ General partners and limited partners
7.1	"To the extent known to the issuer, state whether the issuer is directly or indirectly owned or controlled and by whom, and describe the nature of such control and describe the measures in place to ensure that such control is not abused."	Owners and controllers of the issuer
8.3	Legal and arbitration proceedings Information on any governmental, legal or arbitration proceedings (including any such proceedings which are pending or threatened of which the company is aware), during a period covering at least the previous 12 months, which may have, or have had in the recent past, significant effects on the issuer and/or group's financial position or profitability, or provide an appropriate negative statement."	Parties having a legal claim against the issuer
9.1	"Where a statement or report attributed to a person as an expert is included in the Registration Document, provide such person's name, business address, qualifications and material interest if any in the issuer. If the report has been produced at the issuer's request a statement to that effect that such statement or report is included, in the form and context in which it is included, with the consent of that person who has authorised the contents of that part of the Registration Document.	Any expert opinion, e.g. legal expert or credit rating agency

Under Annex VII, the Registration Document contains several catch-all disclosure requirements relating to transaction parties, including: (1) all persons providing information in the Registration Document;[263] (2) a global overview of all parties involved in the securitisation program;[264] and (3) the parties having ownership or control interests of the parties involved in the securitisation program.[265] The fulfilment of these general disclosure requirements are left to the issuer. However, there is an open question of whether all the parties identified in Annex VIII for the securities note should be identified in Registration Document. It is arguable that both Sections 1.1 and 5.2 refer to not only all the parties specifically identified under the requirements of the securities note in Annex VIII but also any other parties not mentioned in Annex VIII and who are directly or indirectly involved in the asset backed securities transaction.

In other words, a close statutory construction wherein we would look to guidance on what constitutes the persons responsible for any information in the Registration Document and all parties involved in the securitisation programme would include those parties specifically identified in the securities note under the requirements of Annex VIII since they are the types of parties by definition of Annex VIII involved in the securitisation programme. We will turn to those parties when we examine Annex VIII. The parties that are specifically identified for disclosure under Annex VII include:

- Statutory auditors of the issuer;[266]
- The issuer;[267]
- Members of the issuer's administrative, management, supervisory bodies and the general partners and limited partners who may have ownership interests in the issuer;[268]
- Owners and parties having a controlling interest in the issuer;[269]
- Parties with a legal claim against the issuer;[270] and
- Parties providing expert opinion or report at the request of the issuer.[271]

263 PD Regulation, Annex VII, Section 1.1.

264 PD Regulation, Annex VII, Section 5.2.

265 *Ibid.*

266 PD Regulation, Annex VII, Section 2.1.

267 *Ibid*, Section 4 *et seq.*

268 *Ibid*, Section 6.1.

269 *Ibid*, Section 7.1.

270 *Ibid*, Section 8.3.

271 *Ibid*, Section 9.1.

Having identified the transaction parties required for disclosure under the Registration Document, we turn now to the parties required for disclosure under the securities note of Annex VIII.

We have listed in the Table below the specific sections and relevant language of Annex VIII that identify the parties who must be disclosed. Although there is no specific reference to the "securities note" in the Annex itself, it is generally known that the VIII refers to the requirements of a securities note which is published after the Registration Document and serves to specify the offering terms to prospective investors.

Table 16: Transaction Parties Implied by Annex VIII Minimum Disclosure Requirements for the Asset Backed Securities Additional Building Block (Securities Note)

#	Language relating to Transaction Party	Type of Transaction Party
1.1	"Where information is disclosed about an undertaking/obligor which is not involved in the issue, provide a confirmation that the information relating to the undertaking/obligor has been accurately reproduced from information published by the undertaking/obligor. So far as the issuer is aware and is able to ascertain from information published by the undertaking/obligor no facts have been omitted which would render the reproduced information misleading. In addition, identify the source(s) of information in the Securities Note that has been reproduced form information published by an undertaking/obligor."	Party to an undertaking or obligor not involved in the issue
2.2.2	"(a) In the case of a small number of easily identifiable obligors, a general description of each obligor. (b) In all other cases, a description of: the general characteristics of the obligors; and the economic environment, as well as global statistical data referred to the securitised assets."	▪ Obligors – small number, general description of each ▪ All other obligors – general description, economic environment and statistical data
2.2.8	"an indication of significant representations and collaterals given to the issuer relating to the assets"	Collateral provider
2.2.9	"any rights to substitute the assets and a description of the manner in which and the type of assets which may be so substituted; if there is any capacity to substitute assets with a different class or quality of assets a statement to that effect together with a description of the impact of such substitution."	Substitute collateral provider
2.2.10	"a description of any relevant insurance policies relating to the assets. Any concentration with one insurer must be disclosed if it is material to the transaction."	Insurance provider

#	Language relating to Transaction Party	Type of Transaction Party
2.2.11	"Where the assets comprise obligations of 5 or fewer obligors which are legal persons or where an obligor accounts for 20% or more of the assets, or where an obligor accounts for a material portion of the assets, so far as the issuer is aware and/or is able to ascertain from information published by the obligor(s) indicate either of the following: (a) information relating to each obligor as if it were an issuer drafting a Registration Document for debt and derivative securities with an individual denomination of at least EUR 50 000; (b) if an obligor or guarantor has securities already admitted to trading on a regulated or equivalent market or the obligations are guaranteed by an entity admitted to trading on a regulated or equivalent market, the name, address, country of incorporation, nature of business and name of the market in which its securities are admitted."	▪ Obligor – 5 or fewer legal persons or more than 20% of assets ▪ Obligor with securities already admitted for trading ▪ Guarantor with securities already admitted for trading
2.2.12	"If a relationship exists that is material to the issue, between the issuer, guarantor and obligor, details of the principal terms of that relationship."	▪ Issuer ▪ Guarantor ▪ Obligor
2.2.15	"Where more than ten (10) per cent of the assets comprise equity securities that are not traded on a regulated or equivalent market, a description of those equity securities and equivalent information to that contained in the schedule for share Registration Document in respect of each issuer of those securities."	Issuers of previously issued securities that represent 10 per cent of the pool assets
2.2.16	"Where a material portion of the assets are secured on or backed by real property, a valuation report relating to the property setting out both the valuation of the property and cash flow/income streams. Compliance with this disclosure is not required if the issue is of securities backed by mortgage loans with property as security, where there has been no revaluation of the properties for the purpose of the issue, and it is clearly stated that the valuations quoted are as at the date of the original initial mortgage loan origination."	Valuation provider

#	Language relating to Transaction Party	Type of Transaction Party
2.3 and 2.3.2	"In respect of an actively managed pool of assets backing the issue: "The parameters within which investments can be made, the name and description of the entity responsible for such management including a description of that entity's expertise and experience, a summary of the provisions relating to the termination of the appointment of such entity and the appointment of an alternative management entity, and a description of that entity's relationship with any other parties to the issue."	▪ Asset manager ▪ Alternative asset manager ▪ Any other party to the issue with which the asset manager has a relationship
3.2	"Description of the entities participating in the issue and description of the functions to be performed by them."	Any and all participants in the issue
3.3	"Description of the method and date of the sale, transfer, novation or assignment of the assets or of any rights and/or obligations in the assets to the issuer or, where applicable, the manner and time period in which the proceeds from the issue will be fully invested by the issuer."	Parties to a sale, transfer, novation or assignment of the assets
3.4.2	"Information on any credit enhancements, an indication of where material potential liquidity shortfalls may occur and the availability of any liquidity supports and indication of provisions designed to cover interest/principal shortfall risks	▪ Credit enhancement providers ▪ Liquidity support providers ▪ Derivative providers covering interest or principal shortfall risks
3.4.3	"without prejudice to item 3.4.2. details of any subordinated debt finance"	Subordinated debt finance provider
3.4.4	"an indication of any investment parameters for the investment of temporary liquidity surpluses and description of the parties responsible for such investment"	Asset managers of excess liquidity
3.4.5	"how payments are collected in respect of the assets"	▪ Collection agents
3.5	"the name, address and significant business activities of the originators of the securitised assets"	▪ Originators

#	Language relating to Transaction Party	Type of Transaction Party
3.6	"where the return on, and/or repayment of the security is linked to the performance or credit of other assets which are not assets of the issuer, items 2.2 and 2.3 are necessary"	See above for all parties listed under subsections of items 2 and 3
3.7	"the name, address and significant business activities of the administrator, calculation agent or equivalent, together with a summary of the administrator's/calculation agent's responsibilities, their relationship with the originator or the creator of the assets and a summary of the provisions relating to the termination of the appointment of the administrator/calculation agent and the appointment of an alternative administrator/calculation agent"	▪ Administrator ▪ Calculation agent ▪ Originator
3.8	"The names and addresses and brief description of: (a) any swap counterparties and any providers of other material forms of credit/liquidity enhancement; (b) the banks with which the main accounts relating to the transaction are held	▪ Swap counterparties ▪ Credit enhancement provider ▪ Liquidity enhancement provider ▪ Banks holding accounts
4.1	"Indication in the prospectus whether or not it intends to provide post-issuance transaction information regarding securities to be admitted to trading and the performance of the underlying collateral. Where the issuer has indicated that it intends to report such information, specify in the prospectus what information will be reported, where such information can be obtained, and the frequency with which such information will be reported."	Information providers of ongoing reporting

The most general reference to the relevant transaction parties in Annex VIII is found in Section 3.2 which requires a: "Description of the entities participating in the issue and description of the functions to be performed by them." The phrase "entities participating in the issue" by itself is a bit vague since there is no explicit principle which may guide the reader to determine which entities are "participating" in the issue or what constitutes participation. Theoretically, if we relate the concept of participation to the underlying principle of disclosure which is to overcome dysfunctional information asymmetry, then parties who "participate" in the transaction are those parties who are likely to affect the risk and potential value of the transaction, and therefore, fall under the most general principle of disclosure of material facts for the sake of investor protection.

Disclosure of all relevant and material transaction parties is part of the discovery process of high probability, high adverse impact effects. Specific identification of such parties in asset backed securities regulation serves

as guidance on the risk management monitoring and detection system which investors should have in place. The specific types of parties required to be disclosed under Annex VIII are as follows:

Table 17: Transaction Parties Implied by EU Prospectus Regulation, Annex VIII

- Parties and undertaking
- Obligors: five or less or representing more than 20% of pool assets; obligors of securities that are already trading
- Collateral provider
- Substitute collateral provider
- Insurance provider
- Guarantor
- Issuer
- Valuation provider
- Asset manager
- Alternative asset manager
- Parties related to the asset manager or having a contractual relationship
- Parties to a sale, transfer, novation or assignment of the pool assets
- Credit enhancement providers
- Liquidity support providers
- Liquidity enhancement providers
- Derivative providers covering interest rate or currency risk
- Subordinated debt finance provider
- Asset managers of excess liquidity
- Collection agents
- Originators
- Administrator
- Calculation agent
- Swap counterparties

Comparing this list of transaction parties under the EU Prospectus Regulation, Annex VIII, to the parties that are identified under the requirements of the US Regulation AB, we can say that there is substantial overlap. See comparative Table below. However, one of the large differences between to the two regimes is that the EU appears to have almost no specific disclosure requirements for the servicer, while the US provides for a substantial amount of disclosure of the servicer, not only in terms of requiring a compliance servicing state-

ment (§1123) but also an attestation statement by an independent registered public accountant that the actual servicing conforms to the servicing criteria. Indeed, in order for a foreign issuer or foreign assets comply with Regulation AB requirements, full disclosure of the servicer is required for the registration statement in Form S-3 (§1108) and servicer compliance statement and attestation by auditor are required as exhibits to the annual report in Form 10-K. [See Tables for Form S-3 and Form 10-K above.]

Table 18: Comparison of Major Transaction Parties Required to be Disclosed Under EU Prospectus Regulation and US Regulation AB

EU Prospectus Regulation	Type of Transaction Party	US Regulation AB
Annex VII, §1.1 Annex VII, §5.2	General description of any or all parties relevant or material to the transaction, asset-backed securities programme	§1100(d)(1) §1101(a)(3)
Annex VIII, §3.2	Determination of such parties left to the discretion of the issuer "additional or intermediary parties not specifically identified in Regulation AB"	§1103(a)(1) ["summary" "participants in the transaction"] §1100(d)(1)
Annex VII, §4 *et seq.* Annex VIII, §2.2.12	Issuer Issuing entity (owner or purchaser of pool assets) Affiliate or related party to issuing entity Trustee of master trust	§1101(b) §1107(a); §1101(f); §1102(a); §1102(d); §1103(a)(1) ["summary"] §1107 "Issuing entities" main provisions §1120(a) §1101(c)(3)(i)
Annex VII, §6.1(b) and §7.1	Issuer's owners and holders of controlling interest	§1107(g)
Annex VII, §6.1 Annex VIII, §3.7	Issuer's management and administration	§1107(c); §1107(f)
Annex VIII, §2.2.15	Issuers of previously issued securities	§1100(d)(2)

EU Prospectus Regulation	Type of Transaction Party	US Regulation AB
	Affiliates or related parties to sponsor, depositor or issuing entities	§1119(a)(6)
	Underwriters to the issue Underwriting syndicate	§1101(a)(6) §1101(a)(8)
Annex VII, §8.3	Legal claimants against issuer	§1117
Annex VIII, §1.1; §2.2.2; §2.2.11; §2.2.12	Obligors	§1101(i)
Annex VIII, §2.2.11	Significant Obligor Significant obligor is affiliate or related party of sponsor, depositor or issuing entity	§1100(c)(2) §1101(k) §1112 "Significant obligors" main provisions §1119(a)(4)
Annex VIII, §3.3	Parties to the sale, novation or transfer of the assets	
Annex VIII, §3.5 Annex VIII, §3.7	Originators Originator is an affiliate or related party of sponsor, depositor or issuing entity	§1103(a)(1) ["summary"] §1110 "Originators" main provisions §1119(a)(3)
	Depositor (purchases or transfers pool assets to issuing entity)	§1101(e) §1102(a) §1103(a)(1) ["summary"] §1106 "Depositors" main provisions
	Sponsor Affiliate or related party of sponsor	§1101(l) §1102(a) §1103(a)(1) ["summary"] §1104 "Sponsors" main provisions §1119(a)

EU Prospectus Regulation	Type of Transaction Party	US Regulation AB
	Servicers	§1101(j) §1103(a)(1) ["summary"]
	Alternative or back-up servicer	§1108 "Servicers" main provisions
	Servicer is an affiliate or related party of sponsor, depositor or issuing entity	§1119(a)(1)
	Servicer compliance statement	§1123
	Assessor of servicing criteria	§1122(a)
Annex VIII, §2.2 and §2.3.2	Asset manager	§1107(c) – administration of pool assets
	Alternative asset manager	§1107(c)
	"Pool asset administrator"	§1122(d)(4)
Annex VIII, §3.4.4	Asset manager of excess liquidity	See §1113(d) "excess cash flow"
Annex VII, Sec. 1.2	Auditors	§1122(b) auditor "attestation report"
Annex VIII, §2.2.8 and §2.2.9	Collateral provider	Implied by §1100(e) referring to §1107 which is §1107(h); §1108(c)(5); §111(b)(7)(iv) "e.g. occupancy type for residential mortgages or industry sector for commercial mortgages"); §1111(b)(10); §1122(d)(2)(iv) "collateral is maintained as required by the transaction agreements"
	Cash collateral accounts	§1113(a)(2); §1114(a)(4)
	Cross-collateralization	§1111(f); §1113(a)(10)

EU Prospectus Regulation	Type of Transaction Party	US Regulation AB
	Overcollateralization Undercollateralization	§1113(a)(2); §1113(a)(9); §1114(a)(4); §1122(d)(2)(iv) §1113(a)(9)
Annex VIII, §2.2.10	Insurance provider	See, §1114(a)(1) "bond insurance"; Instruction to §1101(c)—in relation to residual value §1111(d)(2)(ii); §1121(a)(4)(ii) relating to "distribution and pool performance"; §1122(d)(4)(xi)
	Credit rating agencies "nationally recognized statistical rating organization" (NRSRO)	§1101(h) §1120
Annex VIII, §2.2.11(b); §2.2.12	Guarantors	§1114(a)(1) and §1114(b)
Annex VIII, §3.4.2 Annex VIII, §3.8	Credit enhancement providers Internal credit enhancement	§1102(h); §1103(a)(3)(ix) §1114(b) §1114(a)(4)
Annex VIII, §3.4.2 Annex VIII, §3.8	Liquidity providers	§1103(a)(3)(ix) §1114(a)(2) §1114(b)
Annex VIII, §3.4.2 Annex VIII, §3.8	Derivative providers Swap interest rate counterparty Swap currency counterparty	§1115 "Certain derivative instruments"; §1115(a) and (b)
Annex VIII, §3.4.3	Subordinated debt provider	§1113(a)(1) "subordinated interests"

EU Prospectus Regulation	Type of Transaction Party	US Regulation AB
	Trustee Trustee is affiliate or related party of sponsor, depositor or issuing entity	§1109 "Trustees" main provisions §1119(a)(2)
Annex VIII, §3.4.5 Annex VIII, §3.7	Collection agent "cash collection and administration"	 §1122(d)(2)
	Paying agent	§1122(d)(3) "investor remittances and reporting"
Annex VII, §9.1	Experts	No such term.
Annex VIII, §2.2.16	Valuation provider Residual value Loan-to-value "Dollar value of commercial loan"	No such term §1101(c)(2)(v); Instructions to 1101(c)1, 3 and 4; Instructions to 1101(k)1; §1111(d)(2);§1121(a)(8) §1105(a)(3)(iii); §1111(b)(7)(iii) §1111(b)(9)(ii)
Annex VII, §8.3	Legal claimants against issuer	§1117 "Legal proceedings"
Annex VIII, §4.1	Information providers of on-going reporting	See, §1118; See requirements for Form 10-D, Form 8-K and Form 10-K
	Legal expert – tax	§1116 "Tax matters"
	Affiliates and related parties	§1119

A cursory glance at the above table shows that most, if not all, of the major parties to an ABS transaction are covered by both the EU and US regulations except for one glaring exception of the servicer. Of course, one

would expect that investors would want detailed information relating to the servicer's credibility and servicing record especially regarding the pool assets of the relevant asset-backed security transaction. Indeed, in the EU Regulation's definition of asset backed securities, the specific rights of the issuer to servicing are specifically mentioned.[272] The general provisions of the EU Prospectus Regulation Annex VII and Annex VII, namely, Annex VII, §1.1, Annex VII, §5.2, Annex VIII, §3.2, would naturally entail the disclosures of such information in some limited fashion.

From a theoretical risk symmetric perspective, information relating to the servicing criteria and servicing performance is critical in overcoming the dysfunctional information asymmetry between what the security holders expect in terms of certainty in payments and the promised payment from the pool assets. In essence, the parties who originate the asset-backed securities have a large potential conflict of interest in efficiently performing under a servicing agreement and this conflict may only be anticipatorily remedied by requiring the servicer to disclose relevant details relating to the servicing function, and having such assessment verified by a reliable and independent third party.

Without the assessment and verification of this servicing function, investors who are wholly dependent on the operational efficiency and veracity of the servicer would be unable to determine whether the performance of the pool assets or distribution terms are being properly complied with. Without assessment and verification, the investors would be apprised of the actual situation of the distribution and pool performance only when there was a statutory requirement or court order for an independent audit of the servicer, which in most instances would occur only when default declared and administration pursued.

Given the structure of many notes relating to second tier or subordinated tranches, or where payment on a tranche is dependent on particular default provisions, it is conceivable that certain asset-backed securities holders would never know whether a default had occurred if the fraud were committed by a servicing institution which had no third party vetting of its servicing function.

Another obvious observation relating to the transaction parties specified under the EU and US regulations is that there appears to be much greater details for disclosures under the US law. However, it must be remembered that the US regulations are borne with a serious limitation on the scope of disclosures which is fully within the discretion of the issuing entities and that is, that most the disclosures are required only if they are material.

This US doctrine of materiality is similar to that of the EU relating to information sufficient to make an informed investment decision where the issuer in effect hazards an empathy with the investor and mirrors the information needs of the investor in the disclosures. This subjective discretion in favour of the issuer is much wider under the current EU regulations than under the relevant US regulations.

One final observation about the differences in rules relating to ABS transaction parties in the EU and the US is that the difference between the two may be explained in terms of market maturity. In the US, one

[272] PD Regulation, Art. 2(5)(a).

of the major aims of the Final Rule on Asset-backed Securities was to consolidate a large body of informal rule making (i.e. "no action letters" issued by the SEC for particular transactions) in order to reach a level of consistency which would allow transaction parties to determine which rules should be applied for their particular transactions.

This body of informal rule making could be thought of as instances where market participants were able to determine transaction structures which allowed them to overcome dysfunctional information asymmetry, and grew into a large body of practices which only a few highly knowledgeable specialists were able to take advantage of. The consolidation of informal rule making also gave the US authorities to eradicate inconsistencies and broad guidance for future innovations in the market by giving market participants a greater sense of regulatory certainty. In contrast to the US's mature stage of needing a consolidating ABS regulation, the EU is just beginning to establish its own securities regulations for a large swath of traditional (non-ABS) and specialized risk management instruments (ABS and derivatives). Given its relative early stage development in the ABS markets, the regulatory experience in ABS is also inchoate.

We cannot say that the EU development path will be same as the US, but given the guiding principles of investor protection, proper disclosures in aid of valuation transparency and risk management, we would expect that overcoming the initial barriers to dysfunctional information asymmetry will be driven by investor demands and, no doubt, corporate frauds and bursting market bubbles which will demand regulatory response. Fraud may never be completely eradicated by disclosure requirements. However, disclosures relating to the underlying transaction agreements may at least give the investor an understanding of what risks are attendant to the transaction.

The names of the transaction parties are only indicative of the types of legal relations which the parties may have with other parties engaged in the establishment and completion of the asset-backed securities transaction. In order to determine the legal risk or the potential legal liability of the transaction parties, it would be necessary to examine the transaction agreements in which these parties appear as signatories. For the purposes of this analysis, this is not possible. However, many of the disclosure requirements in both the EU and US regimes are based on recitals, terms and conditions, and exhibits of the transaction agreements.

The disclosure requirements help establish a set of objective facts and expectations that both seller (issuer) and buyer (investor) tolerate over the life of the asset-backed securities. Thus, whilst the disclosure requirements do not explicitly require the recitation or replication of the effective legal language of the transaction agreements for the final prospectus, in a strong sense, the legal risks of the transaction are dependent on specific legal rights and duties set out in the transaction agreements.

To illustrate this concept, consider section of 3.4.2 of EU Prospectus Regulation, Annex VIII, that provides, as a minimum disclosure, the securities note should include:

> information on any credit enhancements, an indication of where material potential liquidity shortfalls may occur and the availability of any liquidity supports and indication of provisions designed to cover interest/principal shortfall risks.

This language implies that if there is any credit enhancement agreement or liquidity support agreement then it should be revealed, which means that, in effect, the parties to the transaction would need to be disclosed as well as their functions relative to the transaction. Another example is that generality of the phrase "entities participating in the issue and description of the functions to be performed by them" (Annex VIII, Section 3.2) cannot be properly understood without reference to the legal relations embedded within the contracts that define the type, extent and conditionality of participation of particular parties.

Thus, whilst a listing and glossary of particular types of participating entities may be helpful, the labels would not be sufficient to identify the particular legal rights or duties that these parties might have in contracts where such rights and duties might be deemed unique. Finally, disclosure of the types of transaction parties is only the first step in understanding what might be the genuine legal risks in a transaction, and therefore, the next level of scrutiny for the investor would be to understand the functions of such parties within the complex web of transaction agreements.

3.2.3 Interim Conclusion

For purposes of comparative analysis, the legal liability of transaction participants is related not only to whether they are required signatories to disclosures mandated under asset-backed securities regulations, but also, whether they have any residual contractual or tortuous liability under the set of legal relationships created by virtue of: (1) their contractual relations and (2) communications (non-communications, as the case may be) with any members of the set of transaction parties.

We would hypothesize that in the development of asset-backed securities regulations, which is, in fact, relatively immature in both the US and the EU, although the US regulations are much more directed at the specific legal relations and risks of asset-backed securities than the EU, the focus of a normative set of regulations should be in determining "who should be made liable" for purposes of ensuring that reliable and accurate revelations be made to: (1) overcome dysfunctional asymmetry and (2) enhance market confidence.

These are high-level kite-marks which should be considered as continually aspirational goals rather than as problems that can be resolved in one fell-swoop. In a word, an asset-backed securities regulatory regime that focuses on the correct parties to hold liable for purposes of public disclosures requires deep insight into asset-backed structures and the risk transfer mechanisms involving the non-issuing parties.

It would therefore be natural to provide an analysis of the transaction agreements underlying asset-backed securities and their required disclosures. However, given the rather large number of various transaction agreements underlying asset-backed securities and their resultant complexity for purposes of cross-jurisdictional comparative analysis, the authors feel that arriving at certain conclusions relating to the liability of transaction parties are sufficient for purposes of this Report.

We would recommend that in a future investigation of asset-backed securities a more complete analysis of contractual disclosures may help not only regulators, but also investors, genuinely understand what types

of information should be kept confidential and which may be more useful for the public development of market confidence. It is our observation that required factual disclosures made publicly available are helping overcome dysfunction asymmetry at the individual investor (deal-to-deal) level, but our hypothesis is that these same rules completely ignore the effect of how such information could be accessed to overcome general market dysfunctional asymmetry which appears to be concomitant to serial speculative bubbles in what should theoretically be rather stable, transparent, and low-risk tradable instruments. This is a concern for regulators who not only wish to promulgate capital formation but also to avoid and mitigate systemic contagion.

We offer the rest of this truncated analysis as part of a long-term process of developing genuinely complete markets with broad-based market participation and hope that the following comparative analysis of Russian mortgage-backed securities law based on the comparative framework of US and EU regulatory formalities which have been not too hastily drawn provides sufficient impetus for improvements.

3.3 Russian Approach

3.3.1 Introduction

Russian approach towards securities differs from common law countries. Historically, Russian legislation belongs to so-called Roman-Germanic jurisdictions.[273] Unlike the common law jurisdictions, the Roman-Germanic group advocates *legal formalization* methodology to securities, which means that usually legislation strictly limits the types of securities by providing an exhaustive list of the documents that can be called as a security. This also means that legislation explicitly provides certain rights and obligations of the parties involved in securities transactions. Thus, the Roman-Germanic jurisdictions deny granting the same level of flexibility for securities as it is granted by common law jurisdictions.

This principle led to another distinction in the theory of securities. Since there is a certain and exhaustive list of the securities and each of the allowed security exists in a highly regulated framework, the effectiveness of information disclosure is diminished though it is still considered an important tool for investor protection. Information disclosure tends to be considered by the government authorities as a *formal* way to protect the investors together with close state supervision.

The principle of close state supervision justifies numerous legal norms that prescribe the types of minimum disclosures required of the Issuer and other relevant parties. However, the issuer is allowed the discretion to provide additional information to the potential investors but it must be stressed that the minimum volume of information prescribed by the legislation must be presented. Otherwise, failure to provide the prescribed volume justifies the state authority in rejecting registration of the issuance resulting in the securities being prohibited from offering to investors.

[273] Wood, P.R. (Sep 2005) *Maps of World Financial Law 5th Edition*, Allen & Overy LLP.

Recent history shows that legislation tends to be one step behind market needs with existing Russian regulations on disclosures requiring some information to be presented even if it is completely irrelevant for securitization transactions. We will draw attention to this kind information in our analysis and explain where it is not readily obvious, how such information is demonstrably irrelevant to the concerns of investors. In the next section, we shall describe the framework for disclosures relating to a specific type of Russian security which has legal features that are most closely related to asset-backed securities in the US and EU.

Given that the principles-based approach of Regulation AB avoids the specification of asset-backed securities by the asset type, we find that comparing Russian disclosure rules on mortgage-backed securities with relevant regulations in developed jurisdictions may offer some guidance on the specification of disclosures for a specific asset class. Consequently, in our report we focus our commentary on the existing legal framework for Russian MBS, including the existing disclosure requirements.

3.3.2 MBS

As previously mentioned, under the Russian legal framework, the only instruments that are allowed issuance are those which are explicitly referred to in the legislation as securities. Among the other types of ABS, Russian legislation contains norms only on mortgage backed securities. The Russian Federal Law "On Mortgage-Backed Securities" (herein, "the MBS Law") was adopted in December 2003.

The primary major purpose of this law was to create a sustainable source for funding of primary residential mortgage lending in Russia. As a consequence, the lawmakers, taking into account the US housing finance system, proposed that the main investors in MBS would be state and private pension funds whose investments are protected within a highly regulated environment. This conservative protective regulatory environment is reflected in the way MBS issuance and structures are prescribed by the laws, which are aimed at protecting MBS investors.

According to the MBS Law, there are two types of securities that can be called MBS: mortgage-backed bonds and mortgage participation certificates. A mortgage backed bond is a debt security which is backed by mortgage pool.[274] This security is allowed to be offered publicly and its issuance is subject to registration.

A mortgage participation certificate is a non-publicly offered equity security which represents the undivided ownership right of its holder in the mortgage pool. This security is fairly similar to the unit in mutual investment funds. The issuance of mortgage participation certificate is not subject to state registration.

For the purposes of this analysis, we consider the specific disclosure requirements for mortgage-backed bond, since its legal characteristics come closest to the common law to those of MBS structures. These characteristics include:

[274] Describe the general characteristics of Mortgage pool and its distinction towards US definition of ABS

- Mortgage backed bonds can be issued by a "Mortgage agent" which share some features that are fairly typical to Special Purpose Vehicles (SPV) in securitizations;[275] and
- Mortgage backed bonds are securities that can be sold publicly through the registration of issues and prospectuses,

Moreover, as of the date of this Report, all domestic MBS have been issued in the form of Mortgage Backed Bonds. Mortgage Backed Bonds, therefore, are the most important current form of mortgage backed securities in Russia. For purposes of analysis, the acronym "MBB" is used to refer to this type of bonds. Below is a brief description of the main characteristics of Russian MBS.

Definition

In accordance with the MBS Law, a Mortgage Backed Bond is the bond backed by mortgage pool. Mortgage pool (collateral pool) serves as collateral to MBB.

Mortgage Agent

The MBS Law introduced the concept of the mortgage agent which was aimed to serve as the SPV in domestic securitization transactions. Thus, the mortgage agent has some distinctive features that allows originator to isolate the pool of assets from its own bankruptcy, and, therefore, decrease the mortgage agent's credit risks. The MBS law presents a certain set of requirements for the establishment of the mortgage agent and its activities.

The mortgage agent can be established in the form of closed joint-stock company for the sole purpose of purchasing claims secured by mortgages or mortgage notes. The mortgage agent is managed by an external company and is not allowed to have any personnel. The mortgage agent's by-laws shall explicitly state the number of issuances planned for mortgage agents. This number cannot be amended and mortgage agents are subject to liquidation after fulfilment of its obligations under issued MBS. There is also a set of specialized norms in the Tax Code providing special taxation treatment for the mortgage agent.

Mortgage Pool

The legislation on MBB introduced a definition of mortgage pool which shall be understood as a pool of claims secured by mortgages. Moreover, the legislation also allows other types of assets to be included in the mortgage pool. Thus, mortgage pool can include cash both in national and foreign currency as well as other securities and immovable property.

The MBS Law provides very detailed requirements as to the assets that can be included in the mortgage pool. Mainly, these requirements are related to the quality of assets or claims to be included to the mortgage pool. Hence, the MBS Law contains the following minimum requirements for mortgage loans:

275

- LTV not less than 70%;
- The mortgage agreement shall prohibit substitution or alienation of the mortgaged immovable property without the consent of mortgagee;
- The mortgaged immovable property shall be insured and the creditor must be stated as a primary beneficiary of such insurance; and
- The outstanding amount on mortgage loans and other loans secured by secondary mortgages shall not exceed 70% from the market price of the mortgaged property.

The legislation also presents some cases when some of the claims shall not be used in the calculation determining the mortgage pool size including:

- Six month past due;
- Mortgaged property has been lost, including declaration of the mortgage as invalid via court decision or other grounds;
- Loans under which there is an acting court decision on declaring the claim as invalid or its termination due to other grounds;
- If the borrower has been declared bankrupt; and
- If there is no property insurance under mortgage loans for more than a 6 month period.

Importantly, the general approach towards the mortgage pool differs from the approach for pool assets in other developed jurisdictions. The Russian MBS law, as well as legislation on securities including acts on information disclosure, tends to segregate and separate the mortgage claims included in mortgage pool.

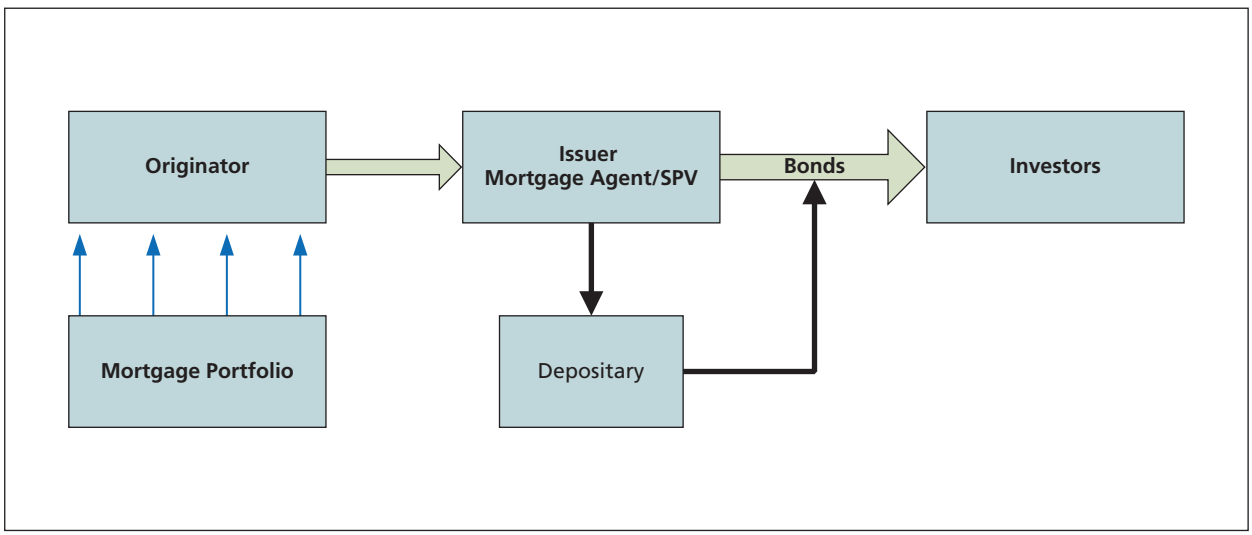
From the analysis of the existing legislation, it is clear that lawmakers tend to place attention on the legal form rather than the legal substance of mortgage pool. For example, the legislation requires the Issuer to provide separate documentation proving the existence of each claim as well as proof of their compliance with legal requirements. Consequently, the Issuer is obliged to present volumes of documentation to prove the existence of legal claims.

Moreover, there is a requirement to maintain a specialized register of claims included in the mortgage pool (the so-called "mortgage register"). The mortgage register must contain information on all mortgage loans included in the mortgage pool. Due to the cumbersome requirements for information presented on the mortgage registers (e.g., outstanding balance of each loan, address, terms, mortgaged properties' market price, etc.), its size is usually enormous[276] and the copy of this register shall be included in the mortgage portfolio.

[276] In our analysis of the prospectuses of Russian domestic transactions, the information on mortgage registers exceeds 1000 pages.

These requirements requiring voluminous filings reflect rather negatively on the degree of flexibility within the Russian MBS system. Russian law provides a strict set of rules and a highly regulated framework for MBB, which means that the sole practical legal solution for MBB issuance via SPVs is rather burdensome in terms of disclosure. The MBB transaction under Russian MBS law is as follows:

Figure 9: MBB Transaction structure under Russian MBS law



3.3.3 Issuance process

The MBS issuance process is regulated under the general framework for all types of securities which are allowed to be publicly offered.

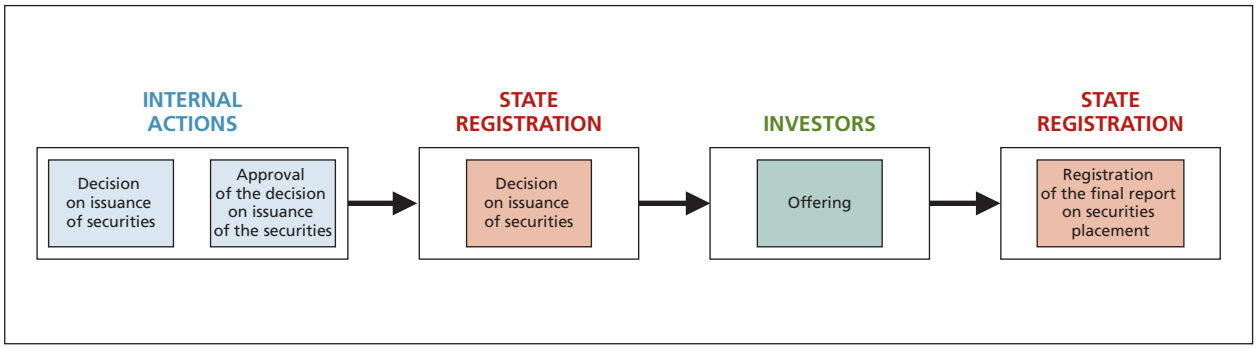
According to the Law "On Securities Market" the issuance process consists of 5 stages:[277]

1. Decision on issuance of securities
2. Approval of the decision on issuance of the securities
3. State registration of the decision on issuance and prospectus
4. Offering
5. Final report on securities placement

From the issuer's perspective, interactions with the various parties relating to the transaction are illustrated as follows:

[277] Federal Law on Securities Market, FZ-39, Art 19, Section 5.

Figure 10: Russian securities issuance process



In the Figure above, the activities in the first and second stages are clearly internal matters undertaken by the issuer. However, current legislation also requires certain disclosures relating to these stages. In essence, these norms are aimed at protecting the rights of the shareholders of the Issuer in case the securities are invalidated.

One critical stage in the issuance process is the registration of the issuance decision by the state authority – Federal Service of Financial Markets. During this registration, the issuer is obliged to provide a completed application along with a number of documents prescribed by the legislation. This decision usually contains specific types of the information prescribed by the legislation. Moreover this stage is normally accompanied by the registration of the prospectuses.[278] In terms of the general characteristics of an initial filing, this registered decision is comparable to the US Registration Statement (Form S-3) and Registration Document as per EU Prospectus Regulation Annex VII.

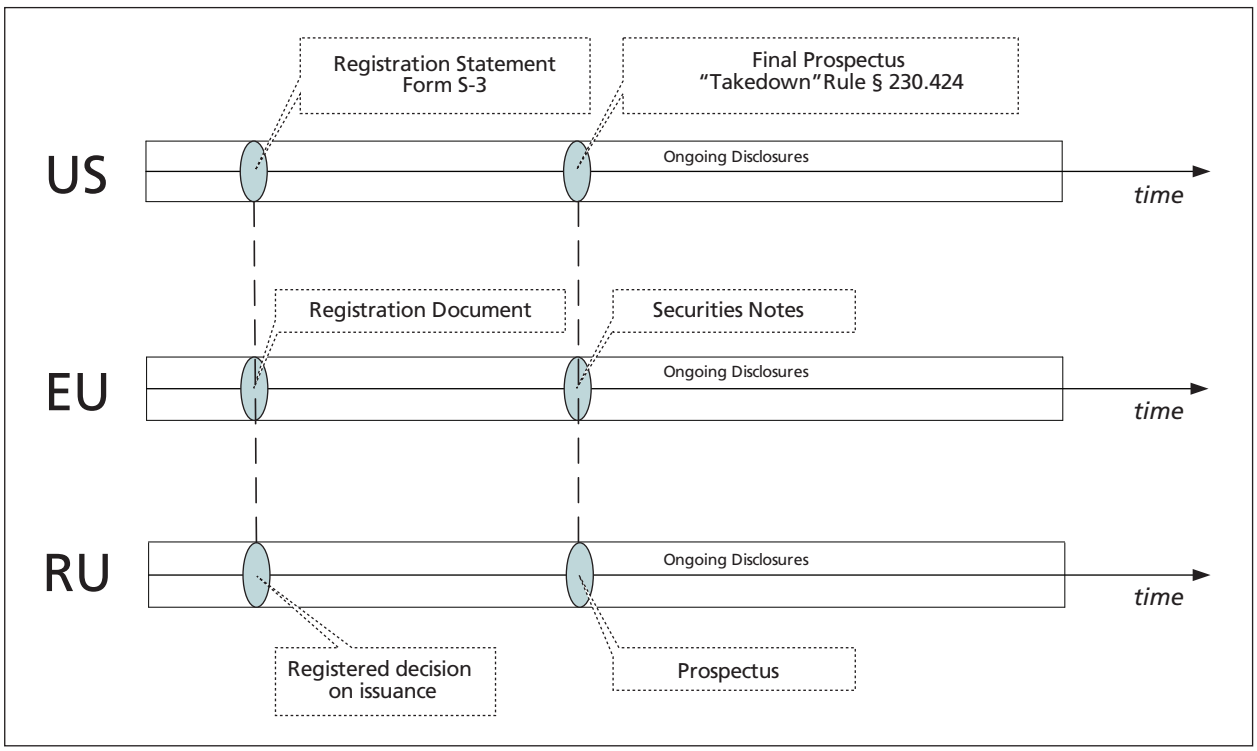
After the completion of the state registration of the issuance decision, the Issuer is allowed to offer the securities to investors. In order to provide investors with time to evaluate the decision on the offered securities, the law prescribes that the securities can be sold two weeks after the information on the state registration of issuance has been published.

In terms of the timeline of disclosures, Russian regulations relating to the issuance process share some common features with the EU and US models. Thus, the Russian "Registration of decision on issuance" is analogous to the US Form S-3 for shelf registration and the registration document required under the EU Prospectus Regulation Annex VII. The Registration of issuance actually includes the registration of the decision on issuance as well as any prospectuses.

Using our comparative benchmark model, we illustrate the common features across the three jurisdictions below.

[278] Prospectuses are not required in all issuances and are excepted in those where the securities are publicly placed and in case if the number of investors in private placement exceeds 500. In addition, prospectuses can be registered after the placement of the securities.

Figure 12: Similarities of Shelf Registration for US/EU and Russian Regulations



3.3.4 Information disclosure

The main legal Act governing the disclosure of information in securities offerings is the Regulation on Information Disclosure by the Issuers of Securities, approved by the Order of Federal Service on Financial Market no. 07-4/pz-n on 25.01.2007 (herein referred to as the "Regulation on Information Disclosure"). This regulation provides for information disclosure for all types of securities issued by private entities. In addition, this regulation contains sample documentation to be issued during securities issuance process.

The four main types of documents containing the most significant disclosure information are as follows:

- Decision on issuance of securities
- Prospectus
- Issuer's quarterly reports
- Significant fact reports

All of the above documents are aimed at providing potential investors with relevant information on the securities being offered. It must be noted that all of these documents shall also be presented to the FSFM for

consideration. The latter is a state authorized securities agency with the responsibility of checking the compliance of each document against the legislative requirements. In the next section, we review the details of each disclosure required for each of the four types of disclosure documents.

3.3.5 Decision on issuance

Decision on issuance of securities (or "the decision on issuance") is a document which contains major information relevant to investor decision making.. In legal theory, the decision on issuance can be compared to a legal proposal made by the issuer to potential investors to purchase the securities being offered. The decision on issuance is presented to FSMF as an official document which is based on the issuance of the securities. In addition to this documentation, the Issuer usually provides other documents prescribed by the legislation. In general, the other documentation provided along with the decision on issuance serves as evidentiary support for the representations made in the latter.

The decision on securities issuance contains information regarding the subject of the agreement and the decision, including, the securities themselves and the essential descriptions of the securities, issuer, and other parties involved in the transaction. Thus the decision must contain further information:

Security

- Type and form of the securities.
- Nominal price.
- Amount of the securities offered under the issuance (In case of tranching, information on the number of tranches as well as the order of identification of the number of tranches and general information on each tranche. In case of previous issuances, the same information shall be disclosed for each.)
- Description of the rights of the owners of the securities.
- All main features of the securities offer including:
    - Conditions and description of the way how investors can buy the securities
    - Method
    - Term
    - Price and method of payments for purchasing securities
    - Identification of the minimum portion of the securities which must be sold in order to declare that the issuance has occurred
    - Conditions and form of payments under the security
    - Terms of payments under the securities
    - Method of income calculation over the securities
    - Method and term of payments under each coupon
    - Conditions of prepayment of the income gained under the securities
    - Other relevant information.

- Information about the rights of bondholder and the method of communication in case of default under the bonds, including a description of the actions to be undertaken by the bond holders in case of default and a description of the disclosures in case of default.
- The order of information disclosure:
  - Method of disclosures
  - Description of information disclosure on each stage of the issuance
  - Where and through what medium the information shall be placed (internet, mass media, etc.)

Issuer

- Information about the issuer and person who provides the mortgage pool, i.e., the number of issuances which are allowed to the Issuer acting as the "mortgage agent", and information on issuances undertaken previously by the mortgage agent.

Transaction parties

- Payment agents, their names, their main functions as paying agents and information on the method for nominating paying agents.
- Special depository which is responsible for maintaining the register of the mortgage pool.
- Insurance provider, if any.
- Service agents, a description of the servicer's functions, its identification data as well as main features of the servicing agreement.

Underlying assets (Information on mortgage pool)

- Size.
- Structure by type of the property included.
- Compliance with the legislation requirements.
- Statement that issuer is a pledger.
- Statement that pledged rights of the bond holder accrue from the moment of the bond purchase.
- Rights of the bond holders and pledgees in case of default.
- Order of enforcement under the pledge.
- Method of pooling the mortgages in the mortgage pool. This information shall include grounds for exclusion of the property from the mortgage pool and the order of substitution of the property in the mortgage pool.
- Other relevant information.

The decisions shall also contain attachments with documentation providing information on the mortgage register. Thus, the attachment shall contain information on each mortgage loan included in the mortgage pool. Usually this attachment consists of thousands of pages. However, its relevance for future investors is not clear.

3.3.6 Prospectus

Prospectus issuance is required when the securities are offered via public subscription or in case of private placement if the number of investors exceeds 500. In all other cases, the prospectus can be registered by the Issuer on a voluntary basis.

The distinction between the prospectus and decisions on issuance is that the prospectus is not considered a legal agreement or proposal to investors to buy the securities. The prospectus is an informational source for the investors rather than an offer to buy the securities. In theory, a prospectus must contain all relevant information for potential investors that will protect the latter and allow them to identify the possible purchase price for the securities.

Unlike other jurisdictions considered in this report, the prospectus structure and sections is strictly fixed by the legislation. This means that the issuer is not given very much flexibility in terms of the form and substance of the information to be presented in the prospectuses. Even where the disclosure requirement is patently irrelevant for various types of the securities, the Issuer must state in the section in question that it has no relevance to the type of the securities offered.

In general, the prospectus has the following structure:

- Table of content
- Introduction

1. Brief information on management of the issuer, its banking accounts, auditors, appraisers, financial consultants and other persons who signed the prospectus.
2. Brief information on the size, terms order and conditions of the securities issuance.
3. General information on current financial state of the Issuer.
4. Detailed information relating to the Issuer.
5. Financial results of the Issuer's activity.
6. Detailed information on the Issuer's management bodies, its financial controlling bodies and the Issuer's personnel.
7. Information on the Issuer's shareholder structure, and transactions undertaken by the Issuer with shareholders.
8. Financial reporting of the Issuer.

9. Detailed information on the order and conditions of placement of the securities.
10. Supplementary information on the Issuer and the securities being offered.

In the next section, we describe the details of the above disclosure requirements for the prospectus.

3.3.7 Security

The prospectus shall contain detailed information on the security being offered. It shall clearly state all features of the security including, its type, amount of tranches, size and other identifying descriptive details. In addition to the description of the main features of the security, the prospectus shall clearly state how the offered securities can be purchased.

3.3.8 Issuer

As in the EU, Russian regulations impose the obligation to disclose all information in the prospectuses primarily on the Issuer. In addition, the rules tend to concentrate the scope of disclosures on the activities of the Issuer. The prospectuses as well as other disclosure documentation contain occasionally detailed information about the activity of the Issuer on such aspects as:

- Management of the Issuer
- Financial conditions of the Issuer
- Outstanding liabilities
- Foundation history
- Main activities undertaken of the Issuer
- Future plans
- Financial reporting documentation.

As previously mentioned, only two types of organizations are permitted to be Issuers of MBS, commercial banks and mortgage agents acting as SPVs. For the purposes of our comparative analysis, we consider disclosure requirements for the issuer which was established in the form of mortgage agents.

Most of the information required in the prospectuses has little or no relevance for SPVs involved in asset-backed securities. For example, disclosure requirements on the SPV's foundation history and detailed information on management structure are not material for investors because SPVs are not allowed to have any staff and management is outsourced to special companies. The other requirements relating to its financial conditions, outstanding liabilities and so on are also largely irrelevant because the SPV is unlikely to have any business rationale separate from its passive role in the asset-backed securities transaction.

In contrast, these regulations contain the requirements on specific information for disclosure by mortgage agents. Thus, mortgage agents are obliged to describe the way in which the mortgage pool was obtained by the mortgage agent, which should also include a description of the agreements concluded for purchasing or obtaining such assets. In addition, information relating to mortgage agents required by law shall also be disclosed. In particular, the legislation requires that the number of issuances allowed to SPV be disclosed.

3.3.9 Transaction Agreements

The prospectus shall contain some information on the transaction agreements. Specifically relating to the mortgage agent, information is required on the agreements that form the basis for the Issuer obtaining the pool of assets backing the MBS. For that particular item, the Issuer must provide specific disclosures on the way in which the mortgage loans have been obtained by the mortgage agent. In addition, the description of the transaction agreements shall be given together with information on the transaction parties.

3.3.10 Transaction parties

The prospectuses shall also contain certain information on the transaction parties. However, in comparison to US and EU regulations, the information required under Russian law relating to the transactions agreement is not as detailed. Generally, the Russian regulations require the Issuer to provide data identifying each party (e.g., in terms of license, name, place of business, etc.) involved in the transaction and a brief description of their main functions.

The following sets out the disclosures required per transaction party:

- **Depositary**
  The prospectus shall contain information regarding depositaries who are in charge of maintaining the mortgage registry.

- **Servicers**
  The issuer shall disclose information about the servicers who are authorized to receive payments from the mortgage borrowers, whose loans are included in the mortgage pool. The following information shall be disclosed:

  - Name of the servicer;
  - Main functions of the service in accordance with servicing agreement concluded between servicer and issuer.

- **Insurer**
  Information on the insurance covering the Issuer's liability relating to investors shall be disclosed. This disclosure shall identify the insurance provider, the insured event, the amount of insurance premium, and a narrative description of the insurance agreement. In case there is no insurance, this shall be explicitly stated in the prospectus.

- **Rating agencies**
  If there are any credit ratings obtained by the issuer, this shall be clearly disclosed in the prospectus. In addition, the name and other data identifying the rating agency shall be provided.

- **Paying agent**
  If there is any paying agent, its name and other identical data shall be disclosed in the prospectus. In addition there shall be a description of the main functions of paying agent and the order of appointment of the new paying agents and the way how information shall be disclosed in case of appointment of new paying agents.

3.3.11 The Underlying Assets

Information on the pool of assets shall be disclosed in the prospectuses. The issuer shall disclose the structure, size and composition of outstanding assets in the mortgage pool. As is it has been already indicated the information regarding mortgage pool, lacks statistical data and shall be disclosed in form of table that contains mainly static information on the mortgage pool. Thus, the issuer is obliged to provide tables that segregate the structure of the mortgage pool, such as registration data of mortgages included in the pool (number, registering body, dates of registration) as well as information on the amount of the claims and interest rates on each mortgage loan. However, from the practical point of view static information appears not as important as information on the historical portfolio performance and dynamics. Taking into account that portfolio backing ABS is in most cases amortizing pool of assets, it is important for investors to understand the future risks related to portfolio by analyzing its historical behavior by applying certain methodology to historical data and projecting forecasts in the future. Therefore, it is crucial for ABS prospectuses to contain the description of historical performance of the portfolios backing ABS.

3.3.12 General Risks

The risks relating to the securities shall be presented in the prospectus and are required to cover the following risk categories:

- Industry risks
- Country and regional risks
- Financial risks
- Legal risks
- Risks related to the Issuers activity
- Banking risks.

3.3.13 Ongoing reporting

Quarterly reports represent a big part of the reporting duties of the Issuer. These reports must be disclosed to all investors who bought the securities as well as to the FSFM where the Issuer has registered the prospectuses.

The quarterly reports are prepared and signed by the CFO and CEO of the issuer. Moreover, the report may be signed by external consultants, auditors and appraisers who are party to the information presented in the report. Quarterly reports must be provided within 45 days from the last day of the quarter. The obligation to provide the quarterly report expires when Issuer fulfill its outstanding liabilities to owners of a security.

The quarterly reports have almost the same structure as the prospectuses and have to contain a lot of information that have been disclosed in the prospectuses. Thus, in theory the quarterly report can be referred as updated prospectuses, with some exception related to information on placement procedures etc.

The quarterly report on MBS shall also contain updated information on the underlying assets. In fact the same static information on assets shall be disclosed along with the information on outstanding delinquency level the whole portfolio.

Significant Fact Reports

The Issuer (SPV) is also responsible for reporting on significant facts. The reporting on significant facts means that the Issuer or other responsible parties are obliged to provide a specific report to all interested parties in case of the occurrence of facts that have the characteristics prescribed by the legislation.

According to the legislation, the following facts shall be considered "significant" and therefore, shall be disclosed in a report:

- General
  - Reorganization of the issuer and/or its branches;
  - Facts that caused one-time increase or decrease of the assets costs of more than 10%;
  - Facts that cause one-time increase of Issuers net profit or net loss of more than 10%;
  - Fact relating to the transactions undertaken by Issuer, the amount of which is more than 10% of the Issuers' assets by the date of the transaction;
  - Facts relating to the stages of issuance, suspension and recommencement of the securities issuance, and on the invalidation of the issuance;
  - Any change in Issuer's shareholders' structure which caused a change of more than 5% in the ownership;
  - Decisions in the shareholders meetings, dates of shareholders register closure, terms of Issuer's fulfillment of its obligations to its owners;
  - Facts relating to the calculated and (or) paid income on securities

- Significant facts specifically relating to the Mortgage agent
  - Facts relating to events that give rise to the right of MBS owners to call for prepayment on the MBS;
  - Facts on the removal of the violations that justified the right of MBS owners to call for early repayment;
  - Facts on undertaken substitution of claims included in the mortgage pool if and substitution of other property included in the mortgage pool in case if the substituted property's price comprise more than 10% of mortgage pool;
  - Facts on the inclusion to the mortgage pool of any claim that is secured by unfinished construction mortgage;
  - On changes in rating status of the MBS, by a rating agency, acknowledged in accordance with Russian legislation, or a rating agency that has concluded an agreement on providing services on rating services;
  - On substitution or change in the data identifying the special depositary which is responsible for maintaining the mortgage registry; and
  - On court decisions to foreclose the property included in the mortgage pool as well as on court decisions not to foreclose.

3.3.14 Final report on the results of issuance

The final report on the results of issuance ("final report") is the document that is provided to the FSFM for the purpose of presenting the information on the process of the offering of the securities as well as the information on its results. Thus, the information in the final report must contain the following items:

- Start and end dates of the offering process;
- Actual price of the placed securities;
- Amount of the securities sold
- Share of the securities which had not been sold during the placement process;
- The amount of received funds for sale of securities;
- On transactions considered by the federal law as a significant transactions in which the Issuer has an interest undertaken during placement process.

3.3.15 Comparative table

The table below contains summary of disclosed information on transaction parties in the table. Red cells meant that the legislation does not contain any requirement to disclose such information.

Table 19: Comparing Disclosures of Transaction Parties under Relevant US, EU and RU Asset-backed Securities Regulations

Type of Transaction Party	US Regulation AB	EU Prospectus Regulation	RU regulation on information disclosure
General description of any or all parties relevant or material to the transaction, asset-backed securities programme	§1100(d)(1) §1101(a)(3)	Annex VII, §1.1 Annex VII, §5.2	Annex 8, sections 1.3 – 15
Determination of such parties left to the discretion of the issuer	§1103(a)(1) ["summary"]	Annex VIII, §3.2	Annex 8, section 1.6
Issuer	§1101(b)	Annex VII, §4 *et seq.* Annex VIII, §2.2.12	Annex 8 section IV Annex 8 section V
Issuing entity (owner or purchaser of pool assets)	§1101(f); §1102(a); §1102(d); §1103(a)(1) ["summary"] §1107 "Issuing entities" main provisions		Annex 8 section X, 10.1
Trustee of master trust	§1101(c)(3)(i)		
Issuer's owners and holders of controlling interest		Annex VII, §6.1(b) and §7.1	Annex 8 section VII
Issuer's management and administration		Annex VII, §6.1 Annex VIII, §3.7	Annex 8 section I, paragraph 1.1. Annex 8 section VI
Issuers of previously issued securities	§1100(d)(2)	Annex VIII, §2.2.15	
Underwriters to the issue Underwriting syndicate	§1101(a)(6) §1101(a)(8)		Annex 8 section IX, 9.8
Legal claimants against issuer		Annex VII, §8.3	
Obligors	§1101(i)	Annex VIII, §1.1; §2.2.2; §2.2.11; §2.2.12	
Significant Obligor	§1100(c)(2) §1101(k) §1111 "Significant obligors" main provisions	Annex VIII, §2.2.11	
Parties to the sale, novation or transfer of the assets		Annex VIII, §3.3	
Originators	§1103(a)(1) ["summary"] §1110 "Originators" main provisions	Annex VIII, §3.5 Annex VIII, §3.7	

Type of Transaction Party	US Regulation AB	EU Prospectus Regulation	RU regulation on information disclosure
Depositor (purchases or transfers pool assets to issuing entity)	§1101(e) §1102(a) §1103(a)(1) ["summary"] §1106 "Depositors" main provisions		Annex 8 section IX, 9.1.5.1.
Sponsor	§1101(l) §1102(a) §1103(a)(1) ["summary"] §1104 "Sponsors" main provisions		
Servicers Alternative or back-up servicer	§1101(j) §1103(a)(1) ["summary"] §1108 "Servicers" main provisions		Annex 8 section IX, 9.1.5.4.
Asset manager Alternative asset manager		Annex VIII, §2.2 and §2.3.2	
Asset manager of excess liquidity		Annex VIII, §3.4.4	
Auditors	§1122(b) auditor "attestation report"	Annex VII, Sec. 1.2	Annex 8, sections I, 1.3
Collateral provider		Annex VIII, §2.2.8 and §2.2.9	
Insurance provider		Annex VIII, §2.2.10	Annex 8 section IX, 9.1.5.1
Credit rating agencies "nationally recognized statistical rating organization" NRSRO	§1101(h)		Annex 8 section X, 10.1.7
Guarantors		Annex VIII, §2.2.11(b); §2.2.12	
Credit enhancement providers Derivative counterparties	§1102(h); §1114(b) §1115(a) and (b)	Annex VIII, §3.4.2 Annex VIII, §3.8	
Liquidity providers		Annex VIII, §3.4.2 Annex VIII, §3.8	
Derivative providers Swap interest rate counterparty Swap currency counterparty	§1115 "Certain derivative instruments"	Annex VIII, §3.4.2 Annex VIII, §3.8	

Type of Transaction Party	US Regulation AB	EU Prospectus Regulation	RU regulation on information disclosure
Subordinated debt provider		Annex VIII, §3.4.3	
Trustee	§1109 "Trustees" main provisions		
Collection agent		Annex VIII, §3.4.5 Annex VIII, §3.7	
Paying agent			Annex 8 section IX, 9.1.2
Experts	§1118 "Reports and additional information"	Annex VII, §9.1	Annex 8 section I, 1.5
Valuation provider		Annex VIII, §2.2.16	Annex 8 section I, 1.4
Legal claimants against issuer	§1117 "Legal proceedings"	Annex VII, §8.3	
Information providers of on-going reporting		Annex VIII, §4.1	

It is obvious from a glance at the table above that using the US and EU as benchmarks for mandatory disclosures of asset backed securities relating to transaction parties, the current Russian regulatory regime may need some adaptation in order to meet the standards of disclosure of the more-detailed and qualitative different requirements of the US and EU regimes. In the next section, we provide a summary of the recommendations which we believe would contribute towards a parity of international disclosure requirements and thereby, ensuring that the Russian as well as US and EU asset-backed securities regulations head towards an optimal regime of full disclosure that overcomes information asymmetry both at the transactional level and at the market level.

4 CLOSING THOUGHTS

In this broad review of the current regulations relating to asset-backed securities in the US, EU and RU, and given the severe testing of the mortgage-backed market in 2007, an important philosophic point has been raised with regard to asset-backed securities in general and with regard to the types of disclosures and accessibility of information to the general public.

The general point is that complex financial instruments which may overcome the initial dysfunctional asymmetry at the transactional level may fail to overcome the dysfunctional asymmetry at the secondary market level because the design of the asset-backed securities regulations themselves fail to sufficiently address the market level dysfunctional asymmetry. Unfortunately, whilst there are literally millions of pages of data disclosed about asset-backed securities in the mature markets of the US and EU, almost all of this data is merely noise, not readily accessible or not readily manipulable by the general public.

Thus, the distrust and the disconnection between the initial buyers who have the provenance of information and computational information (i.e., term sheets) and the benefit of fresh supplemental final prospectuses and the secondary market players who may not know where to access delinquency and loss information and other relevant data which would be material to their investment decisions.

Thus, as a primary recommendation to all regulators concerned with asset-backed securities, we would humbly implore that the regulatory regimes take account of the secondary market first and foremost in drafting any new legislation or rules relating to disclosures, transparency or the risk management of asset-backed securities. As we have learnt in the subprime crisis of 2007, the entire capital markets, equity markets and financial system itself, can be held to hostage to rumours and hearsay when they are not quelled by recognized authority which could have simply pointed to where the actual facts relating to valuation are actually posted for all to see.

If the disclosure regime is designed to overcome dysfunctional asymmetry at the transactional level then we will have encouraged capital formation. But if the disclosure regime fails to overcome dysfunctional asymmetry at the market level then all we have actually encouraged is serial asset-bubble making.

The second recommendation is actually a set of recommendations relating to improving the disclosure regimes of the EU and Russia. It is fairly obvious that one of the biggest gaps in the regulatory reporting regime of both the EU and Russia is the lack of any transparency relating to the servicer function. The US Regulation AB specifically provides for not only a servicer compliance statement that must comply with explicit disclosure items[279] but that an auditor must file an attestation report relating to the servicer complying with specific regulatory standards.[280]

[279] Regulation AB §1123.

[280] Regulation AB §1122(b).

We hope that these two major recommendations, one that is fundamental and addresses how regulators should address systemic risk for complex financial instruments and the other at improving risk management standards for the on-going reporting of asset-backed securities will enable the asset-backed securities markets to weather future storms.

REFERENCES AND SOURCES

Alexander, Kern, Ferran, Eilis, Jackson, Howell E. and Moloney, Niamh, *A Report on the Transatlantic Financial Services Regulatory Dialogue,* Harvard Law and Economics Discussion Paper No. 576 (2007), available at SSRN: http://ssrn.com/abstract=961269.

Akerloff, G., *The Market for Lemons: Quality Uncertainty and The Market Mechanism,* Quarterly Journal of Economics, August 1970.

Bartlett, K.T. and Douglas, B.T., *Symposium: International Securitization and Structured Finance: Foreword,* 12 Duke J. Comp. & Int'l L. 281. (2002).

Basel Committee on Banking Supervision, *International Convergence of Capital Measurement and Capital Standards, A Revised Framework Comprehensive Version*, (June 2007), available at: http://www.bis.org/publ/bcbs107.pdf.

Bruce, R., *As a rule principles should dominate,* Financial Times, Surveys REC1, (29 March 2007).

_____, *Sarbanes-Oxley, Emphasis on Rules May Go in the Dustbin of History*, FT Compliance Special Report, Financial Times, (March 29, 2007).

Cameron L. Cowan Partner, Orrick, Herrington, and Sutcliffe, LLP, *Notes from speech before the Subcommittee on Housing and Community Opportunity Subcommittee on Financial Institutions and Consumer Credit United States House of Representatives Hearing on Protecting Homeowners: Preventing Abusive Lending While Preserving Access to Credit*, (November 5, 2003), available at: http://financialservices.house.gov/media/pdf/110503cc.pdf

Cao, H.H., *Asset Securitization: Is it a Resolution Option for China's Non-Performing Loans?*, 28 Brooklyn J. Int'l L. 565 (2003).

Chibundu, M.O., *Structure and Structuralism in the Interpretation of Statutes,* 62 U. Cin. L. Rev. 1439, (1994).

Claire A. Hill, *Securitization: a low-cost sweetener for lemons*, 74 Wash. U. L. Q. 106, (Winter, 1996).

Cohn, S.R., *The Impact of Securities Laws on Developing Companies: Would The Wright Brothers Have Gotten Off The Ground?,* 3 J. Small & Emerging Bus. L. 315. (1999).

Cox, Hillman, Langevoort, *Securities Regulation*, 3rd 3d., (2001).

Cunningham L.A., *A prescription to Retire the Rhetoric of "Principles-Based Systems" in Corporate law, Securities Regulation and Accounting***,** Boston College Law School, Legal studies research paper series, Research Paper 127, (March 13, 2007).

Dalhuisen, J.H. *Legal Orders and Their Manifestation: The Operation of the International Commercial and Financial Legal Order and Its Lex Mercatoria*, 24 Berkeley J. Int'l L. 129. (2006).

Dasgupta, P., *Securitization: Crossing Borders and Heading Towards Globalization,* 27 Suffolk Transnat'l L. Rev. 243, (2004).

Davidson, A. Sanders, A., Wolff, L., Ching, A., *Securitization, Structuring and Investment Analysis,* (2003).

Dvorak, Y.A., *Transplanting Asset Securitization: Is the Grass Green Enough on the Other Side?,* 38 Hous. L. Rev. 541, (2001).

European Commission, *A Stronger E.U.-U.S. Partnership and More Open market for the 21st Century,* **(**2005).

_____**,** *Directive 2003/71/EC*, available at: http://ec.europa.eu/internal_market/securities/prospectus/index_en.htm.

_____, *Regulation (EC) No. 809/2004,* specific reference to "Annex VII Minimum Disclosure Requirements for Asset Backed Securities Registration Document (Schedule)" and "Annex VIII Minimum Disclosure Requirements for the Asset Backed Securities Additional Building Block," available at: http://ec.europa.eu/internal_market/securities/isd/mifid2_en.htm.

European Securitization Forum (ESF), *Framework for European Securitization,* (2002), available at: http://europeansecuritization.com/ESFDataTEMPLATEv2FINAL.pdf.

_____, *Securitization Data Report* , (Winter 2007).

US Federal Register, Part II Securities and Exchange Commission, 17 CFR Parts 210, 228, et al. *Asset-Backed Securities; Final Rule*, January 7, 2005, available at: http://www.sec.gov/rules/final/33-8518fr.pdf

Ford, C.L. *New Governance, Compliance, and Principles-Based Securities Regulation*, American Business Law Journal, Forthcoming Available at SSRN: http://ssrn.com/abstract=970130. (March 11, 2007).

Frankel, T., *Cross-Border Securitization: Without Law, But Not Lawless*, 8 Duke J. Comp. & Int'l L. 255. *(*1998).

_____, *The Law of Cross-Border Securitization: Lex Juris*, 12 Duke J. Comp. & Int'l L. 475 (2002).

Gololobov, D., Tanega, J. *Sham SPEs, Part I: The Legal Issues of International Accounting Standards on the Consolidation of Special Purpose Entities*, International Company and Commercial Law Review**,** Vol. 17, Issue 11, at 304-317, Nov. 2006.

_____, *Sham SPEs, Part II: The Regulatory Gaps of International Accounting Standards Concerning the Consolidation of Special Purpose Entities*, International Company and Commercial Law Review, accepted for publication in Vol. 17, Issue 12, at 369-380, Dec. 2006.

Grant, J., *Bernanke Calls for UK-Stye Regulation*, (May 15, 2007).

Hazen, T.L., *Disparate Regulatory Schemes for Parallel Activities: Securities Regulation, Derivatives Regulation, Gambling, and Insurance*, 24 Ann. Rev. Banking & Fin. L. 375 (2005).

Hazen, T.L., *The Law of Securities Regulation (Hornbook Series), 4th Edition*, West Group Publishing (2002).

_____, *Disparate Regulatory Schemes for Parallel Activities: Securities Regulation, Derivatives Regulation, Gambling, and Insurance*, 24 Ann. Rev. Banking & Fin. L. 375. (2005).

Healy, Paul M., Palepu, Krishna, *Information Asymmetry, Corporate Disclosure and the Capital Markets: A Review of the Empirical Disclosure Literature* (2000). JAE Rochester Conference April 2000 available at SSRN: http://ssrn.com/abstract=258514.

Humphreys P., Mulligan H., *Lease Securitization: New Challenges for Issuers* (2005), available at://www.mwe.com/index.cfm/fuseaction/publications.nldetail/object_id/6edcc18b-81bb-4675-aad6-9c15e60ac8dd.cfm.

Iacoboucci E. M., Winter R. A., *Asset Securitization and Asymmetric Information*, Journal of Legal Studies, vol. 34, (2005).

International Financial Corporation's Technical Working Group on Securitization, *Securitization In Russia: Ways To Expand Markets And Reduce Borrowing Costs,* Position Paper (2005).

Irish Stock Exchange, *Listing and Admission to Trading -- Guidelines for Asset Backed Securities,* (2005), available at http://www.ise.ie/?locID=145&docID=162.

Jersey Laws, *The jersey Protected Cell Company and the Incorporated Cell Company (ICC)*, The Companies (Jersey) Law 2005 (Amendment No. 8), (February 1, 2006).

Jopson, B., *Dominance of the Big Four Under Attack*, Financial Times Special Report, FT International Accountancy, Financial Times, (26 Feb 2007).

Julia Patterson Forrester, *Still Mortgaging The American Dream: Predatory Lending, Preemption, And Federally Supported Lenders,* 74 U. Cin. L. Rev. 1303 (2006).

Lauren E. Willis *Decisionmaking And The Limits Of Disclosure: The Problem Of Predatory Lending: Price,* 65 Md. L. Rev. 707 (2006).

Lubben, S.J., *Beyond True Sales: Securitization and Chapter 11*, 1 N.Y.U. J.L. & Bus. 89. (2004).

MOODY'S Investor Service, *Pre-sale Report: Russian Mortgage Backed Securities 2006-1 S.A.,* (8 June 2006).

MOODY'S Investor Service, *EMEA New Markets Structured Finance: Record Issuance in 2006 While Further Growth and Asset Class Diversification Expected for 2007,* Structured Finance Research, (22 January 2007).

Prasad E.S., Rogoff K., Wei Shang-Jin, and Kose A., *Effects of Financial Globalization on Developing Countries: Some Empirical Evidence***,** international

Rouwenhorst, K. G., *The Origins of Mutual Funds*, Yale ICF Working Paper No. 04-48, (Dec 12, 2004) , available at: SSRN http://ssrn.com/abstract=636146

Rutsaert, Q., *Protected Cell Companies – A New Trend in the Securitisation Industry Analysed From a Luxembourg and International Perspective*, Journal of International Banking Law and Regulation, (2007).

Schwarcz, S.L. *International Securitization and Structured Finance: The Universal Language of International Securitization*, 12 Duke J. Comp. & Int'l L. 285. (2002).

_____, *The Parts are Greater Than the Whole: How Securitization of Divisible Interests Can Revolutionize Structured Finance and Open the Capital Markets to Middle-Market Companies,* Columbia Business Law Review, Vol. 1993, (1993), available at SSRN: http://ssrn.com/abstract=868532

_____, *International Securitization and Structured Finance: The Universal Language of International Securitization*, 12 Duke J. Comp. & Int'l L. 285 (2002).

_____, *Threats to Secured Lending and Asset Securitization: Panel 1: Asset Securitization and Secured Lending: Securitization Post-Enron,* 25 Cardozo L. Rev. 1539 (2004).

_____, *Threats to Secured Lending and Asset Securitization: Panel 1: Asset Securitization and Secured Lending: Securitization Post-Enron,* 25 Cardozo L. Rev. 1539 (2004).

_____, *Rethinking The Disclosure Paradigm In A World Of Complexity,*2004 U. Ill. L. Rev. 1, (2004).

Simensen, I., Atkins, R., *Not Uncritical' Subprime Exposure Drags Down German Banks,* Financial Times, (22 Aug 2007).

Stachel, D.W., *SEC Regulation AB, What an ABS Investor Wants for Christmas*, (2004), available at: http://www.ssga.com/library/povw/danstachelsecregulationab20041101/page.html

Tanega, J., *Sarbanes Oxley Litigation – Employee Liability and Protection*, ICCLR, (2005).

_____**,** *Letter to the Editor*, Financial Times, (24 August 2007).

Titus, R.B., *Asset Securitization: Marvel of the Marketplace, But Should We be Uneasy?* Book Review of *Securitization: Structured Financing, Financial Assets Pools, and Asset-Backed Securities by Tamar Frankel (1991)*, 73 B.U.L. Rev. 271. (1993).

UK FSA, *Financial Risk Outlook*, (2006), available at: http://www.fsa.gov.uk/pubs/plan/financial_risk_outlook_2006.pdf.

Uri Geiger, *Harmonization Of Securities Disclosure Rules In The Global Market - A Proposal* 66 Fordham L. Rev. 1785 (1998).

US Federal Register, *Part II, Securities and Exchange Commission*, 17 CFR Parts 210, 228, et al. "Asset-Backed Securities; Final Rule, January 7, 2005, available at: http://www.sec.gov/rules/final/33-8518fr.pdf.

Varvel, E., *Plenty of listing options for every need*, Corporate Finance Financial Times Special Report, May Edition, Financial Times, (May 30, 2007).

Waldman, A.R., *OTC Derivatives & Systemic Risk: Innovative Finance or The Dance Into The Abyss?,* 43 Am. U.L. Rev. 1023 (1994).

Wander, H.S., Cope, J.I., and Dariyanani, J., *Developments in Disclosure: Special Problems in Public Offerings – Forward-Looking Information, Including The Private Securities Litigation Reform Act of 1995,* 33 San Diego L. Rev. 1027. (1996).

Weiner, D.J., *Assignee Liability In State Predatory Lending Laws: How Uncapped Punitive Damages Threaten The Secondary Mortgage Market,* 55 Emory L.J. 535 (2006).

Wood, P.R, *Maps of World Financial Law*, 5th Edition, Allen & Overy LLP, (September 2005).

2121 Pennsylvania Avenue, N.W., Washington, D.C. 20433

www.ifc.org

First printing, September 2008

IFC
International
Finance
Corporation
World Bank Group

IFC Russia Primary Mortgage Market Development Project

Additional information about IFC Russia Primary Mortgage Market Development Project is available at:
+7 495 411 75 55
www.ifc.org/russia_mortgage

International Finance Corporation (IFC)
Regional office in Russia, 36, build.1, Bolshaya Molchanovka Street, Moscow, 121069, Russia.
+7 495 411 75 55

EVD
international
business and cooperation

Schweizerische Eidgenossenschaft
Confédération suisse
Confederazione Svizzera
Confederaziun svizra

Federal Department of Economic Affairs FDEA
State Secretariat for Economic Affairs SECO