

The Securities and Exchange Commission (SEC) has decided to not include “synthetic securitizations” in adopting its definition for Asset-Backed Securities (ABS). This stems primarily from the SEC claiming that these forms of securitizations actually create exposure to an asset that is not transferred to, or part of, the actual asset pool. Moreover, synthetic transactions utilize derivative elements, such as credit default and total return swaps.

In its final ruling, *Securities and Exchange Commission 17 CFR Parts 210, 228, et al. Asset Backed Securities: Final Rule*, the SEC specifically states several reasons why synthetic securitizations do not meet the basic definition of ABS:

Payments on securities in synthetic securitizations can comprise of payments based on the value of a referenced asset, which is unrelated to the value of or payments in the pool. A common example would be a transaction where the asset pool would consist of securities but also derivative elements under which payments are based on value. Time and time again, the SEC has stated that payments on ABS must be based primarily on the performance of the financial assets in the pool. ⁽¹⁾

The SEC further points out differences between synthetic transactions and ABS transactions in its final ruling, *Securities and Exchange Commission 17 CFR Parts 210, 228, et al. Asset Backed Securities: Final Rule*, by giving examples on the use of interest rates or currency swaps.

⁽¹⁾ *Securities and Exchange Commission 17 CFR Parts 210, 228, et al. Asset Backed Securities: Final Rule*

Some in the industry objected to the SEC for not making any accommodations in the definition of ABS for synthetic securitizations, and understandably so. Synthetic securitizations, though they may not meet some of the core principles of the ABS definition, are still structured securities that should be treated under the Securities Act and Exchange Act, with the same benefits as Asset-Backed Securities.

The SEC, in its final ruling, states that the basic definition of ABS should be looked upon for establishing “parameters” for the types of securities that are appropriate. This language would lead some to believe that synthetic transactions and structured securities could be interpreted as being a part of the basic ABS definition, thus falling under the ABS requirements. However, the SEC states that “...The definition [ABS] does not mean or imply in any way that public offerings of securities outside of these parameters, such as synthetic securitizations, may not be registered with the commission...” ⁽²⁾

As of the final ruling, the SEC is still seeking additional comments on whether “...we should consider an alternative scheme for these kinds of securities... We will evaluate comments received in determining whether it is appropriate to issue additional proposals or take other additional action.” ⁽³⁾

⁽²⁾ *Securities and Exchange Commission 17 CFR Parts 210, 228, et al. Asset Backed Securities: Final Rule*

⁽³⁾ *Securities and Exchange Commission 17 CFR Parts 210, 228, et al. Asset Backed Securities: Final Rule*



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