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23 June 2003

## By Email

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Dear Mr Maher

### Australian Securitisation Forum FSR submission

Thank you for agreeing to meet with representatives of the Australian Securitisation Forum ("**ASF**") tomorrow in relation to the ASF's submission of 15 May 2003 on financial services reform.

As you are aware, this meeting follows a meeting we have had with representatives of the Australian Securities and Investments Commission (Mark Adams, Director Regulatory Policy; Alan Worsley, Senior Lawyer Regulatory Policy; Michael Wall, Legal Adviser FSRA; Pamela McAlister, Director Legal and Technical Operations; and Jennifer Lewis, Manager Licensing and Business Operations).

In general ASIC was sympathetic to the ASF's concerns, but concluded that some of the changes requested (or, alternatively, any general relief) were matters of policy to be determined by Treasury.

As background to our meeting I have:

- set out below a summary of the ASF's position and objectives as discussed with ASIC;
- attached some example diagrams of securitisation transactions for discussion;
- attached a draft general exemption for discussion.

### Why should the securitisation industry be granted licensing relief ?

The ASF considers that it is appropriate that the securitisation industry obtain some relief from the licensing requirements of FSR for the following reasons.

- **Wholesale.** The securitisation industry operates almost entirely in the wholesale market (there have been a handful of transactions where notes have been issued to retail investors but these are rare and the ASF is not seeking licensing relief in relation to these transactions). The ASF acknowledges that it is the intention of the FSR changes that participants in the wholesale financial services market obtain a financial services licence. The ASF is not suggesting that no-one in a securitisation transaction be licensed, but merely that the number of licences required for a single securitisation transaction be limited. Otherwise, because of the nature of securitisation transactions (see *New Entities* below), the licensing regime will have an ongoing and negative impact on the securitisation industry.
- **Sold through Licensed Dealers.** The end product of a securitisation transaction, a note (or, less commonly, a unit in a trust), is invariably sold to investors through licensed dealers. The relief

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proposed by the ASF would not change this position. The ASF's concern is with the many financial services that are provided by and to participants in the transaction (being wholesale clients) in the course of manufacturing the securitisation instrument that is sold to investors. It is the ASF's view that so long as the end product is sold to investors by a person who has a licence there should be no need for each entity in a securitisation transaction to also hold a licence.

- ***New entities.*** It is the nature of securitisation transactions that they often involve the creation of new entities to fulfil different roles in the transaction. If a new entity in a securitisation transaction is required to hold a licence this could delay the transaction for a considerable period (consisting of the time spent in preparing an application for the licence and the time required to have it approved by ASIC) and could add significant additional costs to the transaction. It will often be the case that these new entities will have related entities that do hold a licence (for example an ADI must set up a subsidiary to manage a securitisation vehicle as APRA does not allow ADIs to manage securitisation vehicles themselves).
- ***Existing exemptions appear intended to provide relief in most areas.*** As noted in the ASF's submission, many entities in securitisation transactions are already, or are close to being, exempt under the current law. However the existing exemptions do not provide sufficient relief for many securitisation entities because of:
  - technical drafting issues; and
  - particularly in the case of securitisation managers, the sunset provision (regulation 7.6.01(6)) that applies to regulation 7.6.01(1)(r).
- ***Transactions are pre-determined.*** Securitisation transactions of their nature are established with very strict parameters leaving little discretion for the participants in the transaction once it has been established (absent the approval of investors). The assets securitised are usually all acquired at the start of the transaction and are described in detail to investors (in some cases the assets are also acquired during a transaction but subject to strict parameters either as to the nature of the assets or their credit rating).

## **Who would benefit from licensing relief ?**

The following entities in securitisation transactions would benefit from the licensing relief proposed by the ASF.

- ***Trustees of Trust SPVs.*** Under the current law trustees of trust special purpose vehicles ("**SPVs**") will certainly require a licence as they will not have the benefit of the self-dealing exception in section 766C(3) in relation to the various financial products acquired on behalf of the trust. Generally trustees of securitisation trusts are independent trustee companies who will in any event be obtaining a licence. However this is not always the case (particularly in relation to sub-trusts that do not have a direct legal relationship with the ultimate investors) and the ASF does not consider that trustees should be required to have licence for a securitisation transaction. Even trustees who do have a licence will obtain benefit from the proposed exemptions since they are having difficulties in relation to the width of the licence required as a result of securitisation transactions (in which they have very little discretion) and would also be able to utilise unlicensed subsidiaries in transactions (an important consideration given the

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complexity of some securitisation structures and the need to avoid trustee companies contracting with themselves).

- **Corporate SPVs.** These are "off-balance sheet" companies established to acquire assets and issue notes to investors. Under the current law they generally do not require a licence (as they have the benefit of the self-dealing exception in section 766C(3) and issue notes through licensed dealers). However there are technical difficulties with some of the exemptions (particularly the hedging exemption in regulation 7.6.01(m) and the issuing exemption in section 911A(2)(b)) that cause problems for corporate SPVs.
- **Managers.** In a large proportion of cases the manager of a securitisation vehicle is a subsidiary of an ADI or an investment bank. This is not always the case, however, and the managers of some very large programs (such as RAMS and Wizard) are independent entities. Managers of securitisation vehicles already have the benefit of a number of exemptions in relation to their activities but many of these have technical difficulties and, the most important exemption, in regulation 7.6.01(r), ceases to have effect on 11 March 2004. Even absent the expiry of regulation 7.6.01(r), law firms are generally advising securitisation managers to obtain licences because the technical problems with the existing exemptions (including regulation 7.6.01(r)) are such that ongoing compliance in the absence of a licence would be onerous.
- **Others.** There are also a variety of other entities fulfilling less central roles in securitisation transactions who would benefit from relief including: paying agents; issuing agents; note trustees; security trustees; and owners of corporate SPVs.

Note also that the proposed general exemption (which is attached and is discussed below) would also benefit others in the wholesale capital markets outside the securitisation industry. In particular it would assist participants in "vanilla" debt issuances and in syndicated loans who have technical difficulties in relation to FSR similar to those of the securitisation industry.

## What sort of relief should be granted ?

Our submission of 15 May 2003 sets out, in general terms, a number of proposed amendments to the regulations that, together, would provide significant relief to the securitisation industry largely through clarifying the scope of existing exemptions.

An alternative would be to create a general exemption for wholesale funders. A possible form of general exemption is attached. Note however that this is an early draft and has not yet been circulated within the industry for comment (you should also note that it differs from a similar proposed exemption provided to ASIC at our meeting with them - as a result of the discussion at that meeting and further consideration of its scope).

The ASF would be happy with either a general exemption or the changes requested in our submission. The advantages of a general exemption are that it would provide greater clarity, both for the industry and the regulator, as to the scope of the exemption. From the regulator's point of view, it would clearly limit the exemption to circumstances where only wholesale clients are being dealt with and where the ultimate investor is dealing with a licensee.

I should also comment on a significant issue which the ASF believes should be addressed as it was discussed at length with ASIC. This is the issue of obtaining an exemption for the provision of "general advice" in

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relation to wholesale funding instruments (see paragraph 9.2(b) of our submission). Under the current law it appears that an issuer of its own securities (excluded from "dealing" under section 766C(4)) will nevertheless require a licence as a result of taking responsibility for an information memorandum issued in the wholesale capital markets (as this will usually involve the provision of general advice - although this is not necessarily the case in a securitisation transaction). This clearly has a wider impact than merely on the securitisation industry as it would apply equally to corporate issuers. The only existing exemption that may assist is regulation 7.1.33B which arguably provides relief if the information memorandum is prepared by an issuer and circulated by a licensed dealer. However:

- ASIC has advised us that they do not believe that this was the intention, or is the effect, of this regulation; and
- in any event the regulation does not assist for securitisation transactions since it generally the manager of the securitisation transaction, rather than the issuer of the notes, that takes responsibility for the information memorandum.

We look forward to discussing these issues with you tomorrow.

Yours sincerely

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Proposed regulation or exemption under Section 911A(2)(l):

A person is exempt from the requirement to hold an Australian financial services licence for a financial service they provide to a wholesale client which is:

- (a) dealing in a financial product (including arranging for a person to deal in a financial product);
- (b) providing a custodial or depository service; or
- (c) providing general advice in relation to a Wholesale Funding Instrument where the advice is prepared by that person but is given by a financial services licensee whose financial services licence covers the provision of the advice,

under or in relation to a transaction, or a series of transactions, a primary purpose of which is raising funds, directly or indirectly, by way of Wholesale Funding.

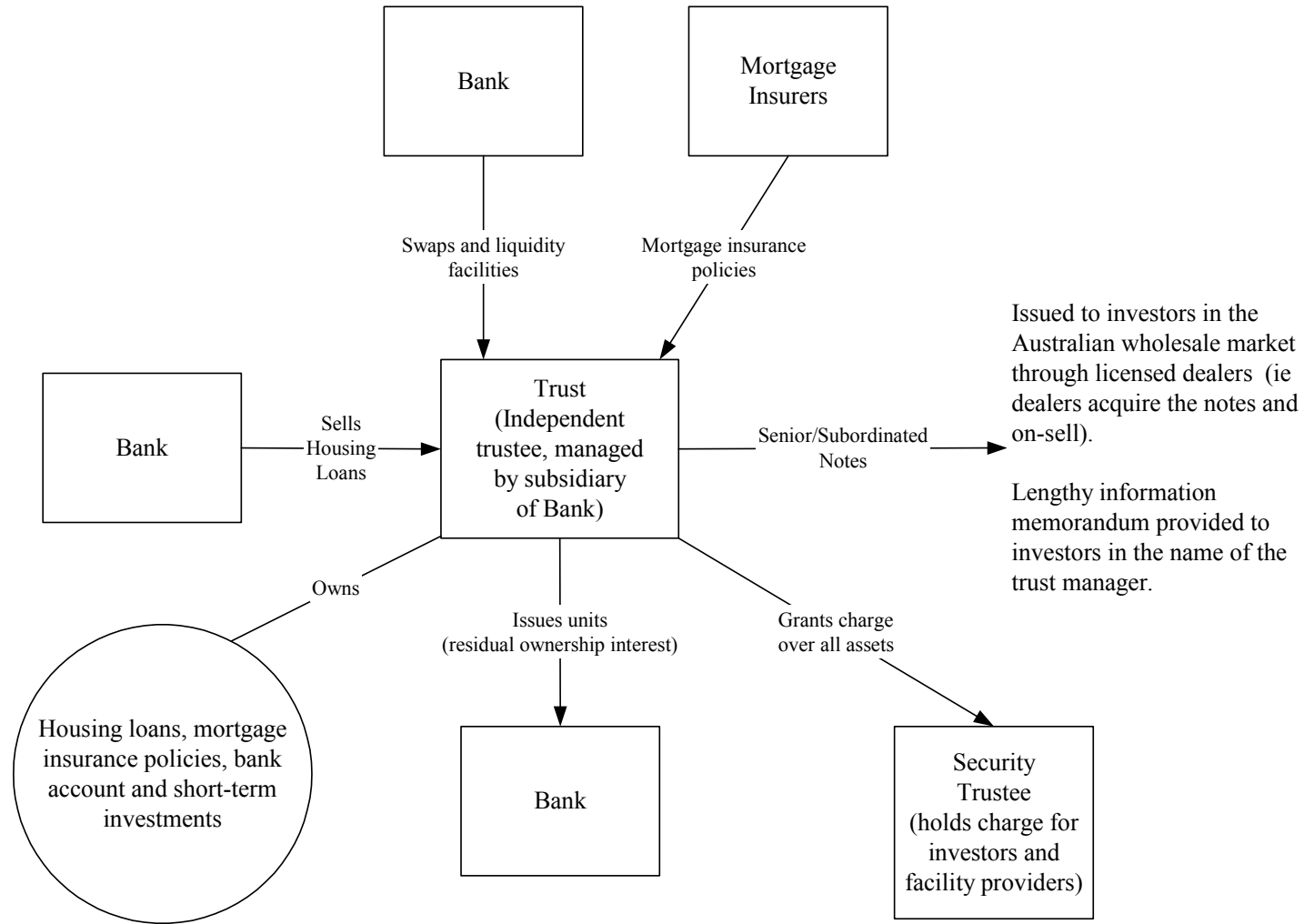
**"Wholesale Funding"** means raising funds from wholesale clients by way of issuing or entering into Wholesale Funding Instruments where those Wholesale Funding Instruments:

- (a) are acquired by a financial services licensee (to be retained by that financial services licensee or transferred to other wholesale clients); or
- (b) issued in accordance with section 911A(2)(b).

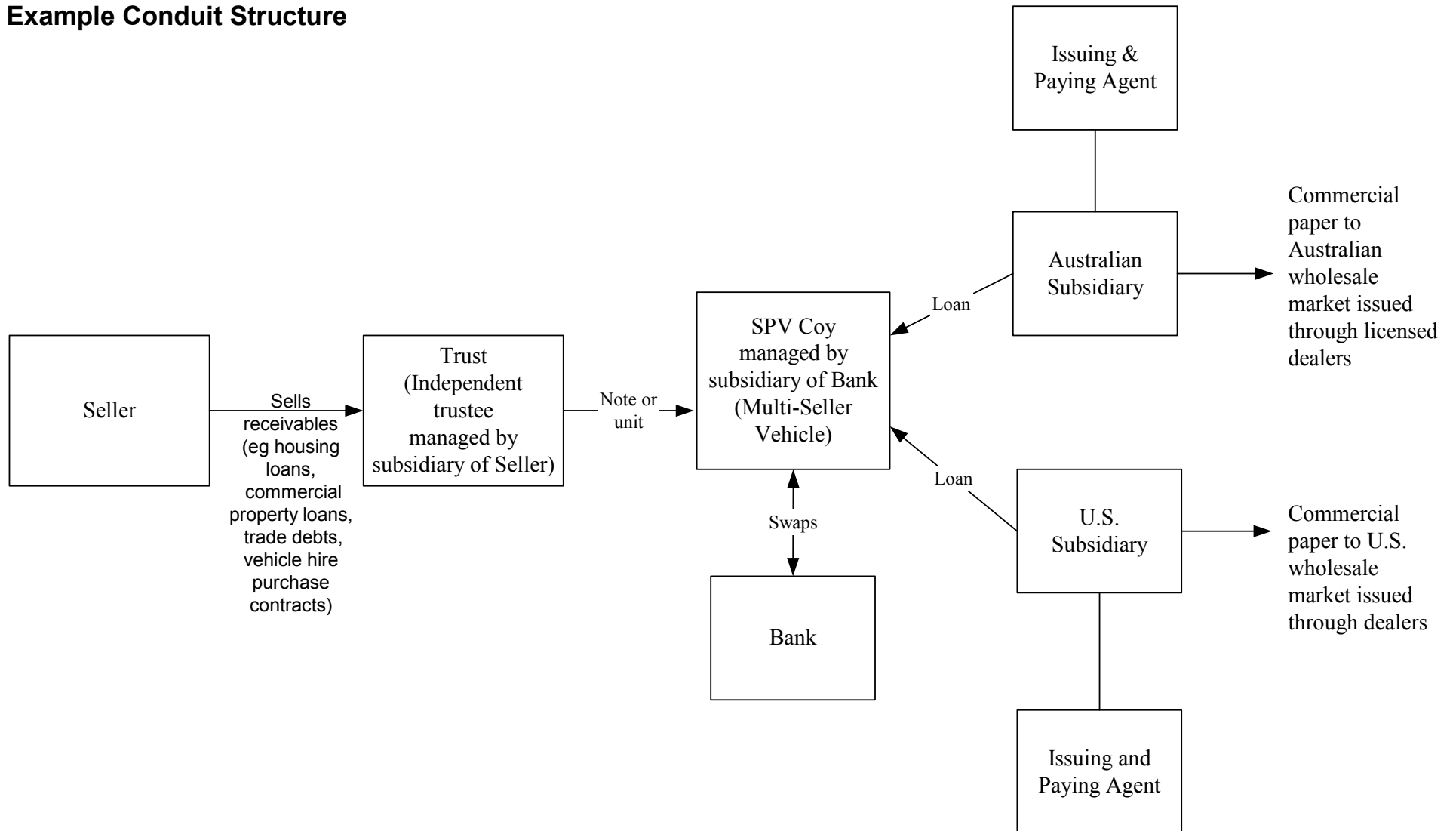
**"Wholesale Funding Instrument"** means:

- (a) a security;
- (b) any of the following in relation to a managed investment scheme:
  - (i) an interest in the scheme;
  - (ii) a legal or equitable right or interest in an interest covered by sub-paragraph (i); or
  - (iii) an option to acquire, by way of issue, an interest or right covered by sub-paragraphs (i) or (ii); or
- (c) a financial product mentioned in section 763A(1)(a).

## Example Bank Domestic RMBS



## Example Conduit Structure



**Example Synthetic**

