SECURITIZATION IS ILLEGAL.

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Abstract

Under US laws, securitization is illegal, primarily because its fraudulent and causes specific violations of RICO, usury, and antitrust laws. Securitization of many types of assets (loans, credit cards, auto receivables, intellectual property, etc.) has become more prevalent, particularly for financially distressed companies and companies with low or mid-tier credit ratings. This article focuses on securitization as it pertains to asset-backed securities and mortgage-backed securities, and analyzes critical legal and corporate governance issues.

Keywords:

Securitization; antitrust; RICO; constitutional law; capital markets; complexity; fraud.

Introduction

Under US laws, securitization is illegal. Indeed many authors have illustrated the deficiencies in securitization.1 This article focuses on securitization as it pertains to asset-backed securities and mortgage-backed securities [2,3]**.** The existing literature on legal and corporate governance issues pertaining to securitization is extensive, but has several gaps that have not been addressed at all or sufficiently:

* Whether securitization is legal.
* Whether securitization causes usury.
* The standards for usurious loans/forbearance.
* The specific components of cost-of-capital, for purposes of assessing usury violations.
* Antitrust liability in securitization transactions.

* Federal/state RICO liability in securitization transactions.
* The constitutionality of securitization transactions.
* The validity of contracts used in effecting securitization transactions.
* Whether securitization usurps the purposes of the US bankruptcy code.

(On “True-sale” and “assignment” distinctions, **see**: *Major's Furniture Mart, Inc. v. Castle Credit Corporation, Inc.*, 602 F.2d 538 (3rd Cir. 1979); *In re Major Funding Corporation*, 82 B.R. 443 (Bankr. S.D. Tex. 1987); *Fox v. Peck Iron and Metal Company, Inc.*, 25 B.R. 674 (Bankr. S.D. Cal. 1982); *Carter v. Four Seasons Funding Corporation*, 97 S.W.3d. 387 (Ark. 2003); *A.B. Lewis Co. v. Nat'l Investment Co. of Houston*, 421 S.W.2d 723 (Tex. Civ. App. - 14th Dist. 1967); *Resolution Trust Corp. v. Aetna Casualty and Surety Co. of Illinois*, 25 F.3d 570, 578 (7th Cir. 1994); *In re Royal Crown Bottlers of North Alabama, Inc.*, 23 B.R. 28 (Bankr. N.D. Ala. 1982) (addressing 'reasonably equivalent value' in transfer by parent to subsidiary); *Butner v. United States*, 440 U.S. 48 (U.S. 1979); *In re Schick*, 246 B.R. 41, 44 (Bankr. S.D.N.Y. 2000); (state law determines the extent of the debtor's interest; bankruptcy law determines whether that interest is "property of the estate")).

This article seeks to fill these significant gaps in the literature. Although the following analysis is supported with US case law, the principles derived are applicable to securitization transactions in common-law countries and civil-law countries. In analyzing the legality of securitization, the following criteria are relevant:

* Origins and history of securitization – legislative history, evolution of securitization processes, and current practices. Carlson (1998), Janger (2002) and Lupica (2000)[4] traces the history of securitization to direct and specific efforts/collaborations to avoid the impact of US bankruptcy laws. Klee & Butler (2002) and other authors have traced the history of securitization to attempts to handle the problem of non-performing debt. * Types of contracts used in securitization. The key criteria for enforceability:

* Purposes, wording and scope of applicable laws – state contract laws, state trusts laws, US bankruptcy code, and state/federal securities laws. The legislative intent of the US Congress in drafting and revising the US Bankruptcy Code.
* How the applicable laws are applied in securitization processes – by market participants, regulators and lawyers that represent investors.

* The people, markets, and entities/organizations affected by securitization.
* The usefulness of existing (if any), possible and proposed (if any) deterrence measures designed to reduce fraud/crime/misconduct.
* Transaction costs.
* The results and consequences of application of relevant laws.

A. Securitization Violates State Usury Laws.

Securitization violates usury laws, because the resulting effective interest rate typically exceeds legally allowable rates (set by state usury laws)[5]**.** There is substantial disagreement (conflicts in case-law holdings) among various US court jurisdictions, and also within some judicial jurisdictions, about some issues and these conflicts have not been resolved by the US Supreme Court[6]. On these issues, even the cases for which the US Supreme Court denied certiorari, vary substantially in their holdings. The issues are as follows:

1. What constitutes usury.
2. What costs should be included when calculating the effective cost-of-funds.
3. What types of forbearance qualify for applicability of usury laws.
4. Conditions for pre-emption of state usury laws.

Where the securitization is deemed an assignment of collateral, the effective cost of funds for the securitization transaction is not the advertised interest cost (investor's coupon rate) of the ABS securities but the sum of the following:

* The greater of the sponsor's/originator's annual cost-of-equity (in percentages) or the percentage annual cash yield from the collateral (in a situation where the SPV's corporate documents expressly state that the Excess Spread should be paid to the sponsor, the Excess Spread should be subtracted from the resulting percentage). The Excess Spread is defined as the Gross Cash Yield From The Collateral, minus the interest paid to investors, minus the Servicing Expense (paid to the servicer), minus Charge-offs (impaired collateral).

* **The Amortized Value Difference**. The difference between the Market Value of the collateral, and the amount raised from the ABS offering (before bankers' fees), which is then amortized over the

average life of the ABS bonds (at a discount rate equal to the US Treasury Bond ate of same maturity) and then expressed as percentage of the market value of the collateral. This difference can range from 10-30% of the Market Value of the collateral, and is highest where there is a senior/junior structure, and the junior/first-loss piece serves only as credit enhancement.

* **Amortized Total Periodic Transaction Cost**. The *Pre-offering Transaction Costs* are amortized over the average life of the ABS, a rate equal to the interest rate on an equivalent-term US treasury bond. The *Periodic Transaction Costs* are then added to the Amortized Pre-Offering Transaction Costs to obtain *Total Periodic Transaction Cost* which is expressed as a percentage of the value of the pledged collateral. The *Pre-offering Transaction Costs* include external costs (underwriters' commissions/fees, filing fees, administrative costs (escrow, transfer agent, etc.), marketing costs, accountant's fees, legal fees, etc.) and internal costs incurred solely because of the securitization transaction (costs incurred internally by the sponsor/originator - direct administrative costs, printing, etc.). The *Periodic Transaction Costs* include administrative costs, servicing fees, charge-off expenses and escrow costs.

* **Foregone Capital Appreciation.** The foregone average annual appreciation/depreciation of the value of the collateral minus the interest rate on demand deposits, with the difference expressed as a percentage of the Market Value of the collateral. The sum of these four elements is typically greater than state-law usury benchmark rates. Where the securitization is deemed a 'true-sale', there is an implicit financing cost which is typically usurious, because it is equal to the sum of the following:

* **Base Cost of Capital.** The greater of the sponsor's/originator's annual weighted average-cost-of-capital, or the annual percentage yield from the collateral.

* **The Amortized Total Periodic Transaction Cost**. The *Pre-Securitization Transaction Costs* paid by the sponsor/originator and directly attributable to the offering is amortized over the life of the ABS, at a rate equal to the interest rate on an equivalent term US treasury bond, and the result (the *Amortized Pre- Securitization Costs*) is added to the *Periodic Transaction Costs* for only one period to obtain the *Total Periodic Transaction Cost*, which is then expressed as a percentage of the market value of the collateral is the *Amortized Total Periodic Transaction Cost*. The *Pre-Securitization Transaction Costs* include external costs (underwriters' commissions/fees, filing fees, administrative costs (escrow, transfer agent, etc.), marketing costs, accountant's fees, legal fees, etc.) and internal costs incurred

solely because of the securitization transaction (costs incurred internally by the sponsor/originator - direct administrative costs, printing, etc.). The *Periodic Transaction Costs* include servicing fees, administrative fees, and charge-off expenses.

* **The Value Difference**. The difference between the Market Value of the collateral, and the amount raised from the ABS offering (before bankers' fees), is amortized over the average life of the ABS bonds and the result is then expressed as percentage of the Market Value of the collateral. This difference can range from 10-30%, and is highest where the senior/junior structure is used and the junior piece serves only as credit enhancement.

* **Amortized Unrealized Losses.** Any unrealized loss in the carrying amount of the collateral, is amortized over the estimated average life of the ABS, and the result for one period is expressed as a percentage of the book value of the collateral. Most ABS collateral are recorded in financial statements at the lower of- cost-or-market.

* **Foregone Capital Appreciation**. The foregone appreciation/depreciation of the value of the collateral minus the interest rate on demand deposits, with the difference expressed as a percentage of the market value of the collateral. The sum of these five elements is typically greater that the state-law usury benchmark interest rates.

B. All "True-Sale", "Disguised Loan" And "Assignment" Securitizations Are Essentially Tax-Evasion Schemes.

In the US, the applicable tax evasion statute is the US Internal Revenue Code Section 7201**7** which reads as follows: "Any person who willfully attempts in any manner to evade or defeat any tax imposed by this title or the payment thereof shall, in addition to other penalties provided by law, be guilty of a felony and, upon conviction thereof, shall be fined not more than $100,000 ($500,000 in the case of a corporation), or imprisoned not more than 5 years, or both, together with the costs of prosecution..." Under this statute and related case law, prosecutors must prove three elements beyond a reasonable doubt:

1) The "actus reus" (the guilty conduct) — which consists of an affirmative act (and not merely an omission or failure to act) that constitutes evasion or an attempt to evade either: a) the assessment of a

tax or b) the payment of a tax.
2) The “mens rea’ or "mental" element of willfulness — the specific intent to violate an actually known legal duty.
3) The “attendant circumstance” of the existence of a tax deficiency — an unpaid tax liability. In the case of ‘true sale’ transactions, the tax evasion[8] occurs because:

a) the sponsor determines the price at which the collateral is transferred to the SPV, and hence, can arbitrarily lower/increase the price to avoid capital gains taxes – its assumed that the sponsor is a profit maximizing entity and will always act to minimize its tax liability and to avoid any tax assessment;
b) the sponsor typically retains a ‘residual’ interest in the SPV in the form of IOs, POs and “junior piece”, which are typically taxed differently and at different tax-basis compared to the original collateral - hence the sponsor can lower the price of the collateral upon transfer to the SPV, and convert what would have been capital gains, into non-taxable basis (for tax purposes) in the SPV “residual;”
c) there is typically the requisite “intent” by the sponsor – evidenced by the arrangement of the transaction and the transfer of assets to the SPV;
d) before securitization, collateral is typically reported in the sponsors’ financial statements at book value (lower-of-cost-or-market - under both US and international accounting standards, loans and accounts receivables are typically not re-valued to market-value unless there has been some major impairment in value) which does not reflect true Market Values. and results in effective tax evasion upon transfer of the collateral to the SPV because any unrealized gain is not taxed;
e) the Actus Reus is manifested by the execution of the securitization transaction and transfer of assets to the SPV;
f) the Mens Rea or specific intent is manifested by the elaborate arrangements implicit in securitization transactions, the method of determination of the price of the collateral to be transferred to the SPV, the objectives of securitization, and the sponsor’s transfer of assets to the SPV;
g) the unpaid tax liability consists of foregone tax on the capital gains from the collateral (transaction is structured to avoid recognition of capital gains), and tax on any income from the collateral which is ‘converted’ into basis or other non-taxable forms;
h) income (from the collateral) that would have been taxable in the sponsor’s financial statements, is converted into non-taxable basis in the form of the SPV’s interest-only (IO) and principal-only (PO) securities - part of the Interest-Spread (the difference between the SPV’s income and what it pays as interest and operating costs) is paid out to PO-holders and this transforms interest into return of-capital or just capital repayment, with no tax consequences.

In the case of 'disguised loan' or 'assignment' securitization transactions, the tax evasion occurs because:

a) the sponsor determines the price at which the collateral is transferred to the SPV, and hence can lower/increase the price of the collateral to avoid capital gains taxes;
b) the sponsor typically retains a 'residual' interest in the SPV which is typically taxed differently and at different tax-basis compared to the original collateral - hence the sponsor can lower the price upon transfer to the SPV, and covert what would have been capital gains, into non-taxable basis for tax purposes;
c) the transfer of collateral to the SPV and the creation of interest-only and principal-only securities essentially converts what would have been taxable capital gains into non-taxable basis;
d) any gain in the value of the collateral is not recognized for tax purposes, because there has not been any 'sale';
e) where the ABS is partly amortizing, any capital gains are converted into interest payments;
f) the Actus Reus is manifested by the execution of the securitization transaction and transfer of assets to the SPV;
g) the Mens Rea or specific intent is manifested by the elaborate arrangements implicit in securitization transactions, the objectives of securitization and the sponsor's transfer of assets to the SPV;
h) the unpaid tax liability consists of tax on the capital gains from the transfer of the collateral (the transaction is structured to avoid recognition of a sale, whereas the transfer to the SPV is effectively a sale), and tax on any income from the collateral which is 'converted' into basis or other non-taxable forms (IOs and POs) , by securitization.

C. In All "True-Sale", "Disguised Loan" And "Assignment" Securitizations, The Conflict Of Interest Inherent In The Sponsor Also Serving As The Servicer, Constitutes Fraud And Conversion.

In most securitization transactions, the sponsor eventually serves as the servicer of the SPV asset pool. As servicer, the sponsor:

a) determines when there has been impairment of collateral, and

b) selects collateral for replacement;
c) monitors collateral performance. To prove fraud, prosecutors must prove several elements beyond a reasonable doubt:

1) **The "actus reus" (the guilty conduct)** — which consists of an affirmative act (and not merely an omission or failure to act) of misrepresentation of materials facts. In securitizations, the sponsor typically makes material misrepresentations: a) the sponsor/servicer selects the assets to be transferred to the SPV, and the terms of the Offering Prospectus typically misrepresents the level of objectivity and fairness of the servicer/sponsor; b) the sponsor/servicer selects collateral for substitution where there are problems – the past and present disclosure statements and ABS offering documents materially misrepresent the sponsor/servicers objectivity/fairness.

2) **The "mens rea' or "mental" element of willfulness** — the specific intent to misrepresent the sponsor/servicer's acts, truthfulness and objectivity/fairness is manifsted by the dual role of sponsor/servicer which constitutes a conflict-of-interest. Mens Rea is also clearly inferable from the facts and circumstances - the sponsor/servicer clearly has significant economic, psychological and legal incentives to maximize its profits by:

a) delaying substitution of collateral for as long as possible,
b) delaying recognition of collateral impairment, and
c) substituting impaired collateral with sub-standard collateral; all of which make the sponsor very un-suitable for the role of servicer.

3) **The reliance element**. ABS investors rely heavily on the structure/arrangements, contracts and disclosure statements in securitizations, which are relatively complex. These form the primary source of knowledge and valuation terms for the investor.

4) **The victim(s) suffers loss as a result of the misrepresentations** (direct or proximate causation). Investors suffer losses because of the sponsor's/servicer's misrepresentations of its obligations, fairness, objectivity and fiduciary duties –

a) investors' estimates of the values of ABS are inaccurate and too high due to the servicer's/sponsor's misrepresentations,

b) investors incur unnecessary trading costs to re-balance their portfolios as the ABS becomes riskier,
c) investors and the sponsor/servicer incurs additional monitoring costs whenever there is any report of impairment of collateral or substitution. Furthermore, in the ABS sales process, the underwriter makes certain representations concerning the effectiveness and predictability of the collection process. Under certain conditions, investors relying on such representations may have a securities fraud claim if the servicer fails to perform, such as in bankruptcy.

C. In All "True-Sale", "Disguised Loan" And "Assignment" Securitizations Where The SPV Is A Trust, The Declaration of Trust Is Void Because Its For An Illegal Purpose.

The declaration of trust relating to the SPV is void because the intent and purpose of the SPV is illegal and unconstitutional as described in this article and in Nwogugu (2006).

D. Off-Balance-Sheet Treatment Of ABS (Both True-Sale And Assignment Transactions) Constitutes Fraud.

Under present accounting rules in the US and most countries, if certain criteria were met, the debt raised by the SPV in securitization can be treated as off-balance sheet debt — but this requires compliance with three criteria:

(I) The SPV should be truly independent from the sponsor and of the directors, fiduciary administrative duties notwithstanding.
(ii) The sponsor's transfer of the assets to the SPV should be a "true sale" and the sponsor should not have any ongoing economic interest in the assets.
(iii) The form and substance should transparently be identical, and the structure should not appear to be illusory or deceptive.

However, this off-balance-sheet treatment criteria has been recently reformed by changes in accounting standards. The UK-based International Accounting Standards Board and the US FASB are moving towards stricter reporting standards:

* FIN 46 (FASB): Effective in 2003, FIN 46 applies only to companies subject to regulation by FASB. Its goal is to substantially tighten the criteria necessary to obtain off-balance-sheet treatment for SPVs,

and its main thrust is capital adequacy. FIN 46 also imposes an obligation on originators to consolidate the accounts of an SPV (denying off-balance-sheet treatment) unless the total equity at risk is regarded as sufficient to enable the SPV to finance its own activities.

* IAS 32, IAS 39, and IFRS 7: International Accounting Standards (IAS) 32 covers the disclosure and presentation of financial instruments, but from 2007 onwards the disclosure aspects will be replaced by the introduction of International Financial Reporting Standard (IFRS) 7. IAS 39 deals with the recognition and measurement of financial instruments, and has been challenged in two aspects: introducing the concept of "fair value" accounting for financial instruments and whether SPVs should be consolidated back into the balance sheet of the originator. Like Fin 46, IAS 32 is likely to result in consolidation of most SPVs on-balance-sheet of the sponsors.

* Basel II: The proposals are aimed at the global banking industry and call for a more scientific measurement of risk and of capital requirements for banks in order to support that risk. Since the general expectation has been that, in overall terms, the proposals could require the banking industry to maintain a higher rather than lower capital base, the proposals have met resistance by many banks. The Basel Committee's rules/codes are not binding because the committee is not a regulator.

The off-balance sheet treatment of ABS debt in securitizations, constitutes fraud because:

1) **The "mens rea' or "mental" element of willfulness** — the specific intent to misrepresent the true "Trust" nature of the SPV debt is manifested by the elaborate arrangements and structure of the securitization transaction.

2) **The "actus reus" (the guilty conduct).** This consists of the affirmative act of misrepresentation of materials facts by not consolidating the SPV on the sponsor's Balance Sheet. In Securitization, consolidation of the SPV in the Sponsor's financial statements is warranted because the sponsor:

a) typically retains a residual economic interest in the SPV;
b) functions as servicer of the SPV asset pool – which grants the sponsor significant control over the assets and the SPV's operations,
c) determines recognition of impairment of collateral, and selects and provides assets for 'substitution' of collateral,

d) typically misrepresents the level of objectivity and fairness of the servicer/sponsor in disclosure statements. Taken together, these factors and the aforementioned new/proposed accounting standards constitute sufficient Actus Reus.

3) **The reliance element**. The sponsor's current and prospective shareholders and other investors rely heavily on the structure/arrangements of securitizations, associated disclosure statements and assurances of off-balance sheet treatment of SPV debt in securitizations, which are relatively complex. These form the primary source of knowledge and valuation terms for the investor.

4) **The victim suffers loss as a result of the misrepresentation** (direct or proximate causation). Investors suffer loss because of the sponsor/servicer' misrepresentations of its obligations –
a) investors' estimates of the values of the sponsor's equity are inaccurate and too high due to the servicer's/sponsor's misrepresentations of the SPV debt,
b) investors incur unnecessary trading costs to re-balance their portfolios as the sponsor is deemed more risky,
c) the investor and the sponsor/servicer incurs additional monitoring costs whenerver there is any report of impairment of collateral or substitution.

E. All "True-Sale", "Disguised Loan" And "Assignment" Securitizations Involve Fraudulent Conveyances.

Any transfer/conveyance of a debtor's assets that is deemed to be made for the purposes of hindering, delaying or defrauding actual or potential creditors may be determined to be a fraudulent conveyance. [9] In the US, three sets of laws cover potential fraudulent conveyances:

a) Section 548 of the US Bankruptcy Code (the Code); or
b) Most states have adopted the Uniform Fraudulent Transfer Act (UFTA)[10] or the older Uniform Fraudulent Conveyance Act (UFCA); or
c) Fraudulent Transfers claims can also be made under a theory of constructive fraud, in which circumstantial evidence may warrant a finding that fraudulent transfers were made with the primary purpose of shielding assets from current or future creditors. Although each state has its own laws regarding the appropriate elements of proof of constructive fraud, Section 548(a)(2) of the US Bankruptcy Code permits an inference of constructive fraud if the following factors exist:

1) the debtor received less than reasonably equivalent value for the property transferred; and
2) the debtor either: was insolvent or became insolvent as a result of the transfer, retained unreasonably small capital after the transfer, or made the transfer with the intent or belief that it would incur debts beyond its ability to pay. The following are various theories of fraudulent conveyance within the context of securitization.

E1. Sponsor/Originator Receives Insufficient Value For Assets Transferred.

All 'true sale" and 'assignment' securitizations involve fraudulent conveyances (as defined in the US Bankruptcy Code and the Uniform Fraudulent Transfer Act) because the originator typically receives insufficient value for assets that it transfers to the SPV[11,12]**:**

i) horizon mismatch – in the case of receivables and fixed income assets, since the originator/sponsor sells these assets before their maturities, their effective yields and values are much lower than their stated yields, and hence, the originator receives less than normal value for assets transferred.

ii) the Originator always incurs substantial cash and non-cash transaction costs in such transfers, which reduces the net-value it receives from the transfer to the SPV – these costs include legal fees, accounting fees, underwriting fees, monitoring costs, administrative costs, regulatory compliance costs, capital-budgeting costs (the decision to securitize has inherent negotiation costs, conflict costs and resource allocation costs), etc.;

iii) in these asset transfers, the Originator loses all the future appreciation of the transferred assets – the transfers are done at book values or stated adjusted costs – the asset valuation for the transfers don't consider future increases in asset value, and hence are an implicit undervaluation.

iv) where the assets transferred have residual values (as in computer leases and equipment leases), the originator often cannot accurately calculate such residual values accurately and does not incorporate them in asset valuation, and loses such residual value, and hence, receives less than normal value for the assets transferred; **v**) in some securitizations, the Originator's transfer of assets to the SPV is backed by recourse (to the originator's assets) and such recourse has economic value that reduces the net-value that the Originator receives from the transfer – Higgin & Mason (2004), Pantaleo et al (1996) and Plank (1991)[13] describe the basis for the value of such recourse.

vi) Where the Originator/sponsor is financially distressed, securitization is often the chosen form of financing, and under fraudulent conveyance laws, securitizations are illegal because,

1) securitizations increase the bankruptcy risk of the Originator/sponsor,

2) the distressed company's assets are typically valued at higher interest rates (which yield lower asset values) and hence, the originator loses value in the transfers.

vii) the originator's/sponsor's net-cash proceeds from the securitization transaction is often significantly less than either the pre-transaction carrying value of the collateral, or the net realizable value of the collateral (liquidation value in a supervised open auction) – primarily because of transaction costs, over-collateralization, etc..

E2. "Intent To Hinder, Delay Or Defraud Creditors"– Implicit Pre-Petition Waiver Of Right To File For Bankruptcy.

All 'true-sale", "Disguised Loan" and "Assignment" securitizations involve fraudulent conveyances (as defined in the US Bankruptcy Code and the Uniform Fraudulent Transfer Act) because as described in this article, such securitizations are the equivalent of illegal pre-petition waivers of the right to file bankruptcy, and the waiver of the bankruptcy stay – all of which are sufficient evidence of "intent to hinder, delay, or defraud any creditor of the debtor", which is the major element of fraudulent conveyance under the UFTA and the US Bankruptcy Code.

E3. "Intent To Hinder, Delay Or Defraud Creditors" – Originator's Transfer Of Assets To SPV.

All 'true-sale", "Disguised Loan" and "Assignment" securitizations are fraudulent conveyances (as defined in the US Bankruptcy Code and the Uniform Fraudulent Transfer Act) because the originator's/sponsor's mere act of transferring assets to an SPV reduces the values of any of its un-secured creditor's claims – ie. trade creditors, holders of unsecured loans, holders of certain preferred stock, etc.[14] Without such transfers, un-secured creditors would have had access to such assets. This is sufficient evidence of "intent to hinder, delay or defraud" existing creditors.

E4. "Intent To Hinder, Delay Or Defraud" Creditors – Originator's Transfer Of Assets To SPV

Is Not Done In Arms-Length Transactions.

The originator's transfer of assets to the SPV via a "true sale" or "assignment" is typically not done in arms-length transactions. Most originators have substantial influence/control over the valuation of collateral, the selection of the appraiser/valuers, the choice of appraised collateral, the corporate form and life of the SPV, and the selection of the officers/trustees of the SPV. Hence, the originator can manipulate the values of collateral for accounting and economic purposes. The originator typically creates, funds and staffs the SPV – hires the SPV's officers and directors and determines the SPV's corporate governance policies. The combination of such excessive control, and the originator's transfer of assets to the SPV is prima facie evidence of 'intent to hinder, delay or defraud' the originator's existing and future creditors.

E5. Securitization Increases The Originator's Bankruptcy Risk Securitization can increase the bankruptcy risk of an originator [15], where:

a) the cash proceeds from the securitization transaction are significantly less than either the carrying value of the collateral, or the net realizable value of the collateral (liquidation value in a supervised auction); or
b) management reinvests the cash proceeds of securitization in projects that yield returns that are less than what the collateral would have yielded or less than the company's cost of debt.

Securitization via assignments or 'disguised loans' increases the risk of the originator/sponsor, and also increases its post-transaction cost of capital primarily because:
a) the amount raised is less than the assets pledged,
b) the pledge of assets to the SPV reduces the originator's borrowing capacity and financial flexibility,
c) the pledge of assets to the SPV reduces the originator's ability to repay other debt. Hence, the originator/sponsor loses value in the transfer of assets to the SPV.

F. Securitization Usurps US Bankruptcy Laws And Hence, Is Illegal.

Securitization undermines US federal bankruptcy policy, because its used (in lieu of secured financing) as a means of avoiding certain bankruptcy-law restrictions,[16] the origins of securitization in the US can be traced directly to efforts by banks and financial institutions to avoid bankruptcy law restrictions.

An analysis of the legislative intent of the US Congress with regard to the US Bankruptcy Code confirms that securitization contravenes most policies of the US Bankruptcy Code[17] These policies include:

a) recognition of financial distress,
b) stay of bankruptcy proceedings,
c) determination of claims and priorities of security interests;
d) fair division of value;
e) the continuance or liquidation decision,
f) efficient reorganization. In most cases, Insolvency often occurs before management decides to file for bankruptcy. Many firms that are either financially distressed and or technically insolvent continue to operate as if they are normal companies, and enter into securitization transactions – often securitization enables them to reduce the effect of actual and or perceived low credit ratings.

Securitization is often a major strategic choice for financially distressed companies.[18] Under the US Internal Revenue Tax Code, securitization qualifies as a reorganization. The underlying issues are as follows.

F1. Implicit Waiver Of Right To File For Bankruptcy And Or Stay.

Securitization involves an implicit (and often express) waiver of the debtor's/Originator's/sponsor's right to file for voluntary bankruptcy. This is achieved by using a bankruptcy-remote SPV and segregating the assets that otherwise would have been part of the bankruptcy estate.[19,20] Securitization involves an implicit (and sometime express) waiver of the creditor/ABS-investor's right to file for involuntary bankruptcy[21, 22] US courts have repeatedly held that such waivers are void as against public policy. In the absence of securitization, this same investors/creditors would have been a creditor/lender to the sponsor/originator. This implicit waiver is achieved by using an SPV and segregating the assets that otherwise would have been part of the bankruptcy estate; and by various forms of credit enhancement.

Without the automatic stay of the bankruptcy code, the debtor/sponsor would not need to transfer assets to an SPV – Carlson (1998) traces the history of securitization to direct and specific efforts/collaborations to avoid the impact of US bankruptcy laws.[23] Furthermore, there is a distinct difference of opinions among US courts about the enforceability of pre-petition waivers (of rights to file for voluntary or involuntary bankruptcy) which has not been resolved by the US Supreme Court [24] – however, the standard securitization processes differ substantially from the conditions in cases where the courts held that pre-petition waivers (or rights to file for bankruptcy) were un-enforceable.

F2. The US Bankruptcy Code Expressly Invalidates Certain Pre-filing Transfers Sections of the US bankruptcy code that expressly invalidate certain types of pre-filing transfers, payments and transactions (that occur within a specific time period before the filing of bankruptcy). Most securitizations fall under the classes of voidable pre-flinging transfers. Hence under these foregoing circumstances/conditions, bankruptcy laws and associated principles are implicated and apply where the firm has not filed for bankruptcy. Therefore, any pre-bankruptcy filing transactions that invalidate or contravene the principles of bankruptcy codes are illegal. The bankruptcy-remoteness characteristic of securitizations prevents the efficient functioning of bankruptcy law.

G. New Theories Of The Effects Of Securitization On Bankruptcy Efficiency

The following are new theories that explain how securitization contravenes the principles of US bankruptcy laws.

G1. The *Illegal Wealth-Transfer Theory –*
Securitization can result in fraudulent conveyance and illegal wealth transfer where the transaction effectively renders the originator/issuer company technically insolvent; or fraudulently transfers value to the SPV (in the form of low collateral values) and then to the ABS/MBS bond holders (in the form of low bond prices, and or high interest rates). [25] Courts have held that stripping a company of the ability to pay judgment claims is a 'predicate act' that is actionable under federal RICO statutes[26]**.** Securitization can also result in illegal wealth transfers to the intermediary bank where it retains a residual interest in the Trust/SPV (residual securities) or is over-compensated (excessive cash fees, trustee positions, underwriter is granted a percentage of securities offered, etc.).

G2*. The Priority-Changing Theory –*
To the extent that bankruptcy laws are designed to facilitate rehabilitation of troubled companies, and increase efficient allocation of debtor assets to creditors, securitization enables the debtor to defeat the Absolute-Priority principle; and to effectively re-arrange priorities of claims, particularly where the

debtor/originator does not have any secured claims (but has only un-secured claims). This is achieved by securitizing un-encumbered assets and using credit enhancement to provide higher-quality securities (the equivalent of higher priority) to other creditors.

G3. The Facilitation Of Inefficient-Continuance Theory –

Securitization enables the debtor/originator to change the progression of financial distress, by supplying cash that typically lasts for short periods of time, and often at a high effective cost of funds. This implicates the principles of 'inefficient continuance' (where an otherwise non-viable company that should be liquidated, sold/merged or substantially reorganized, continues to operate solely as a result of short-term solutions and or bankruptcy court orders), and hence, the sections of the Sarbanes-Oxley Act ("SOX") - which require certification of solvency of the company and adequacy of internal controls, and also carry criminal penalties for non-compliance.[27] The question of whether 'inefficient continuance' has occurred is a matter of law that should be decided by judges. Thus, all else remaining constant, where the necessary elements occur, (a securitization and 'inefficient continuance' and management's certification of solvency and adequate internal controls), management and the company become criminally liable.

G4. *The Information-Content Effect Theory –*

Securitization changes and distorts the perceived financial position of the originator/sponsor, because various forms of credit enhancement (senior/junior pieces, loan insurance, etc.) are used to achieve a high credit rating for the SPV – which may be misconstrued by stock-market investors as evidence of good prospects for the originator-company. To the extent that all securities offerings have relevant information content and associated signaling, then securitization by financially distressed companies effectively conveys the wrong signals to capital markets and hence, changes the expectations of creditors and shareholders (and in the case of bankruptcy, makes it more difficult to efficiently form consensus on a plan of reorganization once the bankruptcy petition is filed). In this realm, investor and creditor expectations are critical and have utility value and typically form the basis for investment/disinvestment and for negotiations about restructuring or plan of reorganization. Courts have held that persons that create false impressions about the financial condition of a company are potentially liable under federal RICO statutes. [28]

G5. *Avoidance Theory –*

To the extent that securitization defers or eliminates a potential creditor's rights to file for involuntary bankruptcy, then securitization can be deemed to be fraudulent, and gives rise to criminal causes of action such as deceit, conversion, etc. The creditor's right to file for a debtor's involuntary bankruptcy is a valid property right that arises from state property law, state contract law, state constitutional laws, and federal bankruptcy laws.[29] Deprivation of, or interference with this property right is a violation of the US constitution. Securitization can defer or eliminate this property right, and hence violate the US constitution where the transaction:

a) effectively rearranges priority of claims; or
b) reduces the debtor-company's borrowing capacity (value of unencumbered/ un-pledged collateral) to the detriment of secured and or un-secured creditors; or
c) uses the proceeds of the transaction to pay-off some (but not all) members of a potential class of creditors that can file an involuntary bankruptcy petition.

H. ***Securitization Constitutes A Violation Of Federal RICO Statutes***

In 'true-sale', 'disguised loan' or 'assignment' securitizations, there are fraudulent transactions which serve as 'predicate acts' under federal RICO statutes[30]. The specific RICO sections implicated are:

* Section 1341 (mail fraud)
* Section 1343 (wire fraud)
* Section 1344 (financial institution fraud)
* Section 1957 (engaging in monetary transactions in property derived from specified unlawful activity).
* Section 1952 (racketeering).

The prices of the collateral are determined in negotiations between the sponsor/issuer and the intermediary bank and on occasion, the SPV's trustees. This presents opportunities for "predicate acts" (ie. fraud, conversion, etc.) because:

1. The collateral could be under-valued or over-valued. There are no state or federal laws that require independent valuation of collateral or appointment of independent/certified trustees in securitization transactions. The parties involved are often business acquaintances. The originator/sponsor controls the entire process.

2. The trustees can be, and are influenced by the sponsor/originator and or intermediary investment-bank.

3. The required disclosure of collateral is sometimes insufficient –

a) does not include historical performance of collateral pools,
b) does not include criteria for selection of collateral and for substitution of collateral,
c) criteria for replacement of impaired collateral is sometimes not reasonable.

4. Mail and wire are used extensively in communications with investors and participants in the transaction.

5. There is compulsion because the intermediary/investment bank has very substantial incentives to under-price the securities, and to inflate/deflate the value of the collateral in order to consummate the transaction and earn fees.

The entire securitization process constitutes violations of federal RICO[31] statutes because:

1. There is the requisite criminal or civil "enterprise" – consisting of the sponsor/issuer, the trustees and the intermediary bank. These three parties work closely together to effect the securitization transaction.

2. There are "predicate acts"[32] of:

a) Mail fraud - using the mails for sending out materials among themselves and to investors.
b) Wire fraud – using wires to engage in fraud by communicating with investors.
c) Conversion – where there isn't proper title to collateral.
d) Deceit- mis-representation of issues and facts pertaining to the securitization transaction.
e) Securities fraud – disclosure issues.
f) Loss of profit opportunity.
g) Making false statements and or misleading representations about the value of the collateral.
h) Stripping the originator/issuer of the ability to pay debt claims or judgment claims in bankruptcy

court – this may apply where the sponsor is financially distressed and the cash proceeds of the transaction are significantly less than the value of the collateral.

3. There is typically the requisite 'intent' by members of the enterprise – evident in knowledge (actual and inferable), acts, omissions, purpose (actual and inferable) and results. Intent can be reasonably inferred from:

a) existence of a sponsor that seeks to raise capital – and obviously cannot raise such capital on better terms using other means,

b) existence of an investment bank that has very strong incentives to consummate the transaction on any agreeable (but not necessarily reasonable) terms.

I. Securitization Constitutes Violations Of US Antitrust Laws

The various processes in securitization constitute violations of the US Antitrust statutes.[33, 34, 35] These violations are described as follows.

I-1. Market Concentration: The US ABS and MBS markets are dominated by relatively few large entities such as FNMA, Freddie Mac, the top-five investment banks (all of which have conduit programs), the top-five credit card issuers (MBNA, AMEX, Citigroup, etc.), etc.. Hence the top-five ABS/MBS issuers control more than 50% of the US ABS/MBS market. This constitutes illegal market concentration under US Antitrust laws.

I-2. Market Integration: The ABS and MBS markets are essentially national and international (geographically-diverse entities/individuals participate in each transaction). Each ABS transaction/offering typically involves a 'road show' which consist of presentations to investors in various cities – the cost of the road show is often paid by the underwriter(s) before its fees are paid by the sponsor. In addition, there are printing, mailing, traveling and administrative costs that increase with the greater geographical dispersion of investors. This has two main effects:

a) it reduces competitive pressure on dominant investment banks and groups of investment banks (to the detriment of smaller investment banks); and

b) it raises market-entry barriers by making it more expensive to conduct ‘road-shows’ for new offerings. Hence, the market integration created by the industry practices of securities underwriters is anti-competitive and violates the Sherman Act, and the FTC Antitrust statutes.

I-3. Syndicate Collusion: the syndicates (of investment banks) used in distributing ABS/MBS essentially collude to determine:
a) the price at which each ABS tranche is sold,
b) which investors can purchase different tranches.

Collusion occurs because:

a) In the typical ABS offering, the price determination process is not transparent or democratic because the lead underwriters typically negotiate the offering price with the originator/sponsor and the prospective investors (but some underwriters use auctions). The lead underwriters purchase most of the new-issue ABS, and the balance is typically sold to ‘junior’ syndicate members (who presumably can arrange to buy more ABS from the lead underwriters than allocated to them). In essence, the true price-demand characteristics and negotiability of junior underwriting-syndicate members are very much hidden simply because of the structure of the underwriting/bidding process. Hence, the existing syndicate-based ABS distribution system for new issue ABS distorts the true demand for ABS, reduces competition, and facilitates and results in collusion, and constitutes violations of the Sherman Act and the FTC Antitrust statutes.
b) Similarly, the ABS allocation process is not transparent. The lead underwriter and junior underwriters allocate new-issue ABS to investors based on subjectively determined “suitability” and “in-house criteria”. There are no established or generally accepted major guidelines for such ‘in-house’ criteria and associated allocation. The lead and junior underwriters can typically collude to determine that only certain investors deemed appropriate are allocated ABS. Hence, the antitrust violation (collusion) occurs solely by the underwriters’ discretionary choice of investors to whom ABS are allocated – this is more evident where the investor pool consists of mostly institutional investors, and thus, final offering prices are more sensitive to choice of investors, and prices can change significantly simply by changes in allocation to investors. In such circumstances, the collusion is reasonably inferable, so long as there are no statutory or generally accepted allocation criteria that have been approved by the NASD or other trade associations.

I-4. Price Formation: The price of ABS securities is often linked to the price/yields of US treasury bonds – the credit risk of ABS/MBS is priced relative to risk of US Treasury bonds. This system distorts the true demand/supply balance for ABS/MBS, and erroneously incorporates the demand/supply relationships of the US Treasury Bond market, into the ABS/MBS markets. The key question then, is whether there are conditions under which the US Treasury Bond market is completely de-coupled from the ABS market, or phrased differently, whether there is sufficient justification for actual or perceived de-coupling of the US Treasury Bond market and the US ABS market. These conditions are as follows:

1. The credit fundamentals of the US treasury market differ substantially from those of the ABS market. The treasury market is much more sensitive to US Federal Reserve actions, currency fluctuations, consumer spending, federal/state fiscal policies, etc.). The ABS market tends to be more sensitive to industry-specific and sometimes company-specific risks/factors.

2. The use of various credit enhancement techniques/products further exacerbates the differences in the credit trends/quality in the US treasury and ABS markets. In ABS transactions, most forms of credit enhancement creates a floor, but does not limit or affect other industry-exposure or company-exposure. In the US treasury market, investors are subject to more variety of risks.

3. The investor objectives in the US treasury bond markets differ from those of investors in ABS markets. Hence, investors are very likely to view these two markets and the underlying risks differently, and should value the securities differently.

I-5. Vertical Foreclosure: In the ABS/MBS markets some investment banks and commercial banks are active in almost all phases of the securitization process – origination (through their in-house conduits), due diligence, disclosure and pricing, new issue securities offerings, and secondary-market trading. Similarly, non-bank entities can use their own asset portfolios (origination of credit card receivables or mortgage receivables), shelf-registration procedures and or Regulation-D/Rule 144A procedures (pricing and new-issue offerings) and in-house trading desks (secondary-market trading) to participate in almost all aspects of securitization processes. Hence, these companies have almost no incentive to, and are not required to make their infrastructure and relationships available to competitors. Such vertical foreclosure constitutes violation of antitrust laws.

I-6. Tying[36]:

a) the sponsor is sometimes formally or informally required to purchase other financial services (loans, letters of credit, custody services, etc.) from the investment bank, in order to effect the securitization transaction,

b) the investors are sometimes required to simultaneously purchase two or more tranches of an ABS offering, or to promise to buy the same or similar ABS/MBS securities in order to be allocated ABS in new offerings;

c) the sponsor and or investment may formally or informally require investors to purchase minimum dollar volume of ABS in specific offerings in order to get 'allocations' in future offerings. These acts constitute tying which is anti-competitive.

I-7. Price-Fixing[37] – The *Locus-shifting Theory* is introduced here. Locus-shifting occurs when a potential and obvious party to a price-fixing scheme is effectively replaced (in pricing negotiations) by a third party that has the resources and willingness to dramatically alter the pricing of goods/services in either the transaction, or a series of transactions or in the sector/industry as a whole. Normally, price-fixing would occur between two sponsors or two intermediary banks. Since the intermediary-investment bank is central to ABS offerings, and associated pricing and negotiations, the price fixing should be deemed to occur between the sponsor/originator and the investment bank (or between two sponsors). Since each active investment bank typically underwrites many offerings simultaneously, and essentially controls the pricing of each new-issue ABS, the investment banks are the locus of said price fixing and are potentially liable for the associated antitrust violations. Further evidence of price fixing maybe obtained by analyzing:

a) the yield differentials of various ABS offerings in various asset classes (ie. autos, home equity, mortgages, etc.) by different sponsors within a specific block of time, **b)** the price differentials of various ABS offerings in various asset classes (autos, home equity, credit cards, mortgages, etc.) with the same rating, within a specific block of time.

I-8. Exclusive Contracts [38]

Exclusive contracts facilitate and enhance anti-competitive behavior by contractually restricting conduct by and trade among participants in the market. In the US ABS/MBS markets, existing illegal exclusive contracts include:

a) contracts that prevent the intermediary investment bank from providing financial services to other prospective securitization sponsor-companies in the same industry/sector,
b) contracts (by the sponsor, underwriter(s) or third parties) that prevent or limit the formation of a syndicate of securities dealers;
c) contracts that prevent the sponsor from selling securities through other underwriters, other than an appointed intermediary investment bank. These types of contracts constitute direct violations of US antitrust statutes.

I-9. Price Discrimination[39]

There are several classes of ABS:

1) Securities that involve pure “pass-through” of cash flows, and hence rights to payment of cash from the SPV pool, but no ownership interest in the pool to:

a) IO – interest only securities;
b) PO – principal only securities; and c) traditional ABS that pay both interest and principal.

2) Securities that confer ownership interests in the underlying pool to:

a) IO – interest only securities;
b) PO – principal only securities; and c) traditional ABS that pay both interest and principal.

3) Debt-type securities that involve a security interest in the underlying collateral:

a) IO – interest only securities;
b) PO – principal only securities; and **c**) traditional ABS that pay both interest and principal.

In many instances, the SPV offers many tranches in each of the above-mentioned classes of ABS. The tranches within each class typically vary by term, interest rate, duration, and bond-rating/risk-rating. Hence, in any situation where the tranches don’t have any priority as to security interests or rights-to-payment of cash flows from the pool, such stratified offerings within each class (IO, or PO or ordinary;

or pass-through, collateral-type or equity-interest) constitutes price discrimination because the underlying asset and risk is essentially the same, although different securities are being offered in the same transaction (or series of transactions), at different prices to investors, based on the same underlying pool of assets. The distinguishing and critical element is that there is no contractually agreed-upon priority of claims as to security interests or right-to-payment of cash from the poll of assets.

I-10. Predatory Pricing[40]

This occurs when investment banks under-price ABS offerings in order to obtain more investors, and to build name recognition for a particular issuer (that does or intends to come to the ABS market regularly). Evidence of predatory pricing may be inferred or established by:

a) Comparing the offering prices of various new-issue ABS bonds sold by one sponsor/originator, in the same asset class (auto loans, home equity, credit cards, etc.), but at different times of the year, to offering prices of similar ABS bonds sold by other regular ABS sponsors/originators in the same time periods.
b) Running regressions to identify any statistically significant relationship between:

> 1) the difference in the yield of company XYZ's ABS bond and the yields of other similar ABS bonds, and
> 2) various independent variables such as yield, price, asset type, bond rating, duration, industry, amount of offering, frequency of ABS offerings, types of investors, etc.

c) Comparing the offering prices of various new-issue ABS bonds underwritten by one investment bank (in the same asset class, but at different times of the year) to offering prices of similar ABS bonds underwritten by other investment banks in the same time periods.

I-11. Rigging Of Allocations

Most ABS offerings are done via allocations of securities by investment banks to their brokerage customers.

1. Most sponsors issue ABS/MBS through bids by investment banks. Most bids for ABS securities are won by a few investment banking firms. This may suggest that customers have been "allocated" among investment banks. This is also an indication of collusion.

2. On occasion, the primary underwriters subcontract work (re-sell securities) to secondary underwriters.

J. *Securitization Involves Void Contracts*

The process of securitization involves several contracts that are either signed simultaneously or are all signed within a short time frame. Many of these contracts are void and illegal for the following reasons:

a) Lack Of Consideration[41] – there is no consideration in many of the contracts used in effecting securitizations. Many of these contracts are unilateral executory promises and contain illusory promises. There are three main issues:
I) Unilateral Executory Promise[42]– A unilateral executory promise is not consideration. The following are some unilateral executory contracts in securitizations:

> * The promise made by the SPV to payout periodic interest, whether contingent or non-contingent on whether the collateral pays cash interest.
> * Collateral-substitution Agreement contains a promise in which the sponsor agrees to substitute impaired collateral.
> * Assignment Agreement - Assignment of future collateral (not yet existing) may be deemed a unilateral executory promise by the assignor.
> * Transfer Agreement. The sponsor agrees to transfer the collateral to the SPV, and the SPV in return pays cash to the sponsor.

ii) *Illusory Promises*[43] – An illusory promise is not a valid consideration for a contract. The following are some illusory promises inherent in securitization transactions:

> * The Subscription/purchase Agreement. The SPV's promises to acquire the collateral with the cash raised from investors are essentially illusory promises. These promises are embedded in

the offering Prospectus, but are typically not included other corporate documents. In most cases, the offering prospectuses don't state the exact steps in the SPV's promised purchase of the collateral.

Purchase/Subscription Agreement. The SPV's investors purchase beneficial interests in the SPV or the SPV's debt. These beneficial interest evidence:

a) right to payments from the SPV, or
b) an ownership interest in the underlying collateral, or
c) a 'participation' in the underlying collateral. However, at the time of executing this agreement, the only consideration that the SPV can grant to investors in exchange for the purchase amount, consist of promises to purchase the collateral in the future, and to make payments from the SPV's assets. Hence, an existing asset is being exchanged for a future asset that does not exist as of the date of the purchase/subscription agreement.

* Furthermore, all securitization offerings are done pursuant to 'Subscription Agreements' and Investor Questionnaires – the two documents have to be signed by the prospective investor. None of the agreements signed by the investor as part of his/her purchase of the SPV's ABS expressly incorporates the promises embodied in the Offering Prospectus. What typically exists is an implied agreement to subject the investor to the SPV's articles of incorporation, Trust Indenture, and or Trustees'/board of directors' (or Board of Trustee's) decisions.

* The SPV's promise to pay interest/dividends on ABS IOs, Preferreds and POs are essentially illusory promises because the underlying collateral may not produce any cash flows, in which case there wont be any interest or dividend payments. iii) *No Bargain* – some courts have held that there is no consideration (and hence, the contract is void) where one party was not allowed to bargain for the alleged agreement.[44] In some securitizations, the process of setting offering prices for new ABS issues does not afford all parties the opportunity to negotiate terms of the offering, especially individual investors, because the price of the ABS is typically determined primarily by the sponsor and the lead-underwriters. Furthermore, in securitizations, the originator sets the terms of the SPV (trust documents, articles of incorporation, Bylaws, etc.).

2. *No mutuality*[45] in the securitization context, for there to be mutuality:

a) each party must have firm control of the subject matters of the contract and the underlying assets (consideration), and

b) there should be a direct contractual relationship between the parties. At time of the Subscription Agreement, the SPV typically does not own or have rights to the collateral, and hence, there is not mutuality. Furthermore, the concept of 'piercing the SPV veil' is introduced here (and is similar to piercing the corporate veil) and applies since the following conditions exist:

* The economics of the transaction is an asset transfer from the sponsor/originator to the SPV investors, in exchange for a loan to the sponsor. However, there is no direct contractual relationship
* The sponsor typically controls the SPV before the ABS offering and determines (or substantially influences) the SPV's post-offering operating characteristics. Since prospective ABS investors don't have firm pre-offering control of the SPV and cannot influence its post-offering policies, there is no mutuality between the SPV and the ABS investors; and securitization is void.
* The sponsor influences the appointment of the SPV's trustees or board of directors.

Thus, under contract law, the use of the SPV in securitization effectively eliminates any mutuality between the two main contracting parties - the sponsor and the investors. Secondly, there is no mutuality between the SPV and the investors: a) the SPV corporate documents (trust indentures or bylaws or articles of incorporation) typically limits the rights of each ABS investors and the group of ABS investors. Thirdly, there is no mutuality between the SPV and the sponsor/originality because both entities are essentially the same, and are controlled by the sponsor before and after the securitization.

3. *Illegal subject matter And Contravention Of Public Policy* **46** – as explained in preceding sections of this article, securitization constitutes violations of antitrust statues and federal RICO statutes, and hence, the contracts used to effect securitizations are void and illegal.

Conclusion

Under US laws, Securitization is clearly illegal. This requires the enactment of special federal securitization statutes; and changes in law enforcement patterns and practices.