30 Cannon Street, London EC4M 6XH, England
Phone: +44 (0)20 7246 6410, Fax: +44 (0)20 7246 6411
Email: iasb@iasb.org Website: http://www.iasb.org

International Accounting Standards Board

INFORMATION FOR OBSERVERS

ARG Meeting:	**November 2007, London**
Project:	**Consolidation – Example: Asset-backed Securitisation (Agenda Paper 2A)**

Introduction

1. This paper analyses an asset-backed securitisation example according to our proposed approach to consolidation.

Example: Asset-backed Securitisation

Fact pattern

Originator

2. The originator or transferor **(Originator)** is an entity that holds and has the rights to a portfolio of debt securities. The fair value of the securities is CU500 million. The originator sells the securities to a separate legal entity to isolate them from the rest of the business and to generate liquid assets (cash).

Transfer

3. Originator establishes a legal entity (**Entity**). Originator sells the portfolio of debt securities to Entity in exchange for cash of CU450 million and a subordinated interest in Entity of CU50 million. Entity has nominal equity that is held by a charitable trust with no voting rights. To fund the acquisition of the debt securities, Entity issues CU450 million of commercial paper to third party investors (**Investors**).

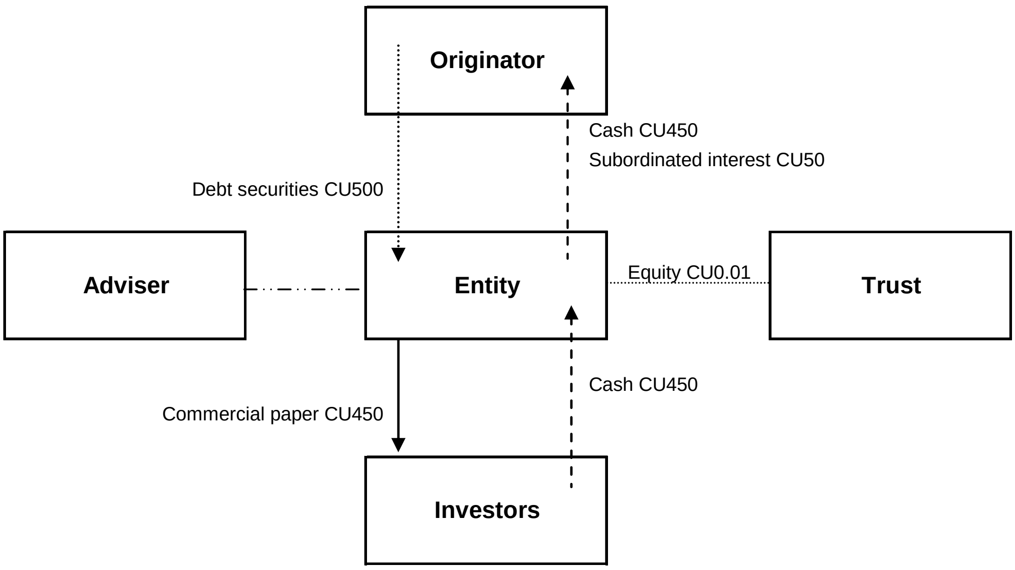
4. As a result, Entity has debt securities of CU500 million, commercial paper of CU450 million, subordinated debt of CU50 million and equity of CU0.01.

Entity

5. Entity is managed by a private advisory firm (**Adviser**) unrelated to Originator. Adviser receives a fixed fee plus a variable fee equal to five percent of the appreciation in the pool of transferred securities over CU500 million (the fees are at market rates).
6. The management of the debt securities owned by Entity has been contracted to Adviser. Within highly-specified parameters, Adviser is able to sell the securities of Entity based on its best judgement of the market [the specified parameters are such that Adviser is unable to control Entity]. Originator cannot terminate the contract with Adviser in the normal course of business (ie it does not have ‘kick-out’ rights)—the contract with Adviser can be terminated by a majority of Investors and Originator.
7. Originator’s subordinated interest in Entity entitles it to any residual returns of Entity after paying amounts owed to Investors and Adviser.
8. The limitations on the rights of Originator to manage the activities of Entity mean that it would be difficult to conclude that Originator controls Entity using a traditional assessment of control.

Analysis

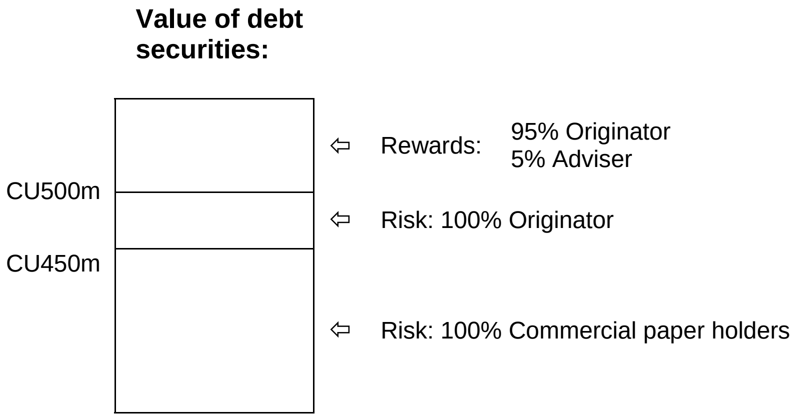
9. The flow of resources is summarised in the diagram that follows:



10. The table that follows summarises the rights and responsibilities (and the related risks and rewards) of each of the parties:

Party	Interest	Risks	Rewards
Originator	Subordinated interest in Entity.	First bears the risk if the market value of securities declines below CU500m; absorbs **all** losses between **CU450-500m**.	95% of the market value of debt securities above CU500m.
Advisor	Fixed and variable fee.	Minimal; senior fixed fee.	Fixed fee. Variable fee of 5% of the market value of debt securities if above CU500m.
Investors (CP holders)	Interest and principal payments on commercial paper.	Bear loss after Originator; absorb **all** losses if the value of the debt securities declines below **CU450m**. Risk is related to the class of CP.	Interest on CP (at market rates).

11. As a result of the transactions, any value changes in the debt securities are attributed to the parties as follows:



Proposed accounting treatment

[Paragraphs 12 to 19 have been omitted from the observer notes].