

MINISTRY OF FINANCE

DESIGNATION OF AN ACTIVITY NOT FALLING WITHIN THE MEANING OF “RECEIVING FUNDS FROM THE PUBLIC” AND “BANKING BUSINESS” (SECURITIZATION SCHEMES)

Under paragraph (ab) of Section 1 of the Banking Institution Act, (Act No. 2 of 1998), as amended, on the recommendation of the Bank of Namibia, I designate the activity of Special Purpose Entities (SPEs) or issuing entity as set out in clause 2 of the notice, and which is performed in accordance with the conditions set out in clauses 2 to 21 of the Notice, as an activity that do not fall within the meaning of “receiving funds from the public” for the purpose of conducting banking business.

CALLE SCHLETTWEIN

MINISTER OF FINANCE

Windhoek, 31 August 2016

SCHEDULE

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PART 1

INTRODUCTORY PROVISIONS

1. Definitions

In this notice unless the context otherwise indicates -

“The Act” means the Banking Institution Act (Act No 2 of 1998), as amended, -

“Asset-backed commercial paper (ABCP) programme” means a programme in terms of which predominantly commercial paper with an original maturity of one year or more is issued to investors, which commercial paper is backed by assets or other exposures held in an insolvency remote special purpose institution, or such other programme as may be specified in writing by the Minister.

“Asset-backed security (ABS)” means a fixed-income or other security collateralized by any type of self-liquidating financial asset that allows the holder of the security to receive payments that depend primarily on cash flow from the asset.

“Associate” means an associate as defined in the Banking Institution Act, (Act No. 2 of 1998), as amended.

“Commercial paper” means-

- a) Any written acknowledgement of debt, irrespective of whether the maturity thereof is fixed or based on a notice period, and irrespective of whether the rate at which interest rate is payable in respect of the debt in question is fixed or floating rate; or
- b) Debenture or any interest-bearing written acknowledgement of debt issued for a fixed term in accordance with the Companies Act;
- c) Preference shares, but does not include bankers' acceptances.

“Companies Act” means the Companies Act, 2004 (Act No, 28 of 2004)

“Credit enhancement facility” means any facility or arrangement in terms of which the provider of such facility or obligor under the arrangement is obliged to absorb losses associated with-

- a) The assets transferred in terms of a traditional securitization scheme;
- b) The risk transferred in terms of synthetic securitization scheme; and
- c) Include both a first-loss credit-enhancement facility and a second-loss credit enhancement facility.

“Credit rating” means a rating assigned by an eligible institution to commercial paper issued in respect of a traditional or synthetic securitization scheme. It actually refers to an assessment of the credit worthiness of individual borrowers and corporations based upon their history of, but not limited to, borrowing and repayment, balance sheet, profitability, etc.

“Delayed payment on assets” means a delayed payment on assets that does not result directly from a default or potential default in respect of the underlying assets, but which results, inter alia, from administrative or technical difficulties experienced in respect of collection of payments in respect of the underlying assets.

“Disclosure document” means a prospectus, placing document, offering circular or any other document with similar import, published in order to provide certain information relating to a traditional or synthetic securitization scheme to prospective investors in the said securitization scheme.

“Eligible collateral” means the credit risk mitigation techniques that are recognized under the Determination on the Measurement of Capital for Credit, Market and Operational Risk (BID-5) or BID-5A, for the purpose of providing capital relief and, are specified in clause 16.8.1 of BID-5 or clause 3(a) of Annexure 6 to BID-5A.

“First loss credit-enhancement facility” means the credit enhancement facility that represents the first level of credit enhancement in a traditional or synthetic securitization scheme.

“Implicit support” the term refers to the wide range of mechanisms by which a bank provides non-contractual support to the holders of some securitization exposures, usually once there is deterioration in the credit quality of the underlying pool of exposures.

“Insolvency remote” In respect of special purpose entity, means that the assets of such a special purpose entity shall not be subject to any claim of any institution-

- a) Transferring assets in terms of a traditional securitization scheme; or
- b) Transferring risk in terms of a synthetic securitization scheme.

“Entity” means banking institution or any other institution within a banking group of which such a banking institution is a member or non-bank entity/institution, including associate companies, which engages in a securitisation transactions as originators or investors.

“Institution within the banking group” means the following institutions that may form part of the banking group:

- a) All banks in such group;

- b) All subsidiaries, joint ventures, or associates of such banks;
- c) The controlling company of such banks; and
- d) All other subsidiaries, joint ventures and associates of such bank controlling company.

“Liquidity facility” means a facility provided in respect of traditional or synthetic securitization scheme in order to cover deficiencies in cash flow within the said securitization scheme(s), resulting from, amongst other thing, the following:

- a) Time difference between the payment of interest and principal on assets transferred, or other payments due in terms of a traditional securitization scheme, and payment in respect of the senior commercial paper, or
- b) Time difference between the payment of interest and principal on assets that serve as collateral, purchased in terms of a synthetic securitization scheme, and payment in respect of the senior commercial paper; or
- c) Market disruption; or
- d) A combination of any of the matters specified above, and which facility does not constitute a credit-enhancement facility.

“Originator” means entity that acts as an originator or a person who (1) through an extension of credit or otherwise, creates an asset that collateralizes an asset-backed security; and (2) sells the asset directly or indirectly to an issuing entity or SPE.

“On-balance sheet retention” means a requirement where originator, sponsor or original lender are not permitted to receive protection against the credit risk of that proportion of the pool of exposures that fulfils the retention requirements, for both traditional and synthetic securitization scheme;

“Parties involved in a securitization scheme” means a special purpose institution, parties acting in primary roles and parties acting in secondary roles.

“Primary role” means participation by an institution in a traditional or synthetic securitization scheme as an originator, remote originator, sponsor or a re-packager.

“Remote originator” means an institution that directly or indirectly lends money to a special purpose institution in order for the special purpose to take transfer of the asset in terms of a traditional securitization scheme or transfer risks in terms of a synthetic securitization scheme.

“Repackager” means an institution that, whether at the commencement or during the life of the traditional or synthetic securitization scheme acquire and subsequently transfer the assets or the risk relating to assets.

“Secondary role” means the participation by an institution in a traditional or synthetic securitization scheme, as a provider of a credit-enhancement facility, a provider of liquidity facility, and underwriter, a purchaser of senior commercial paper, a servicing agent or a counterparty to a transaction included in the trading book of the bank.

“Second-loss credit-enhancement facility” means a credit enhancing facility that represents the second and further levels of credit enhancement in a traditional or synthetic securitization scheme; provided that-

- a) Such facility benefits from a substantial first-loss credit-enhancement facility, that is, when the first-loss credit-enhancement facility covers some multiple, as opposed to a fraction, of historical losses or expected losses estimated by way of simulation or other technique; and
- b) Such facility may be drawn only after the first-loss credit-enhancement facility has been exhausted.

When above conditions are not complied with the facility concerned shall for purpose of calculating a bank’s prescribed capital requirements be regarded as a first-loss credit enhancement facility in terms of this notice.

“Securitization” means the process by which relatively homogeneous loans, originally made by an entity, are pooled and sold to an SPE that issues marketable/tradable securities against the pooled assets.

“Servicing agent” means an institution that act as a servicing agent in relation to the collection of the amounts due in terms of traditional or synthetic securitization scheme (for a fee or charges).

“senior commercial paper” means commercial paper issued in terms of a traditional or synthetic securitization scheme, the purchase of which commercial paper does not constitute providing a first-loss or second-loss credit-enhancement facility.

“Short-term liquidity facility” means a liquidity facility provided in respect of a tradition or synthetic securitization scheme, for a period of less than one year.

“Special-Purpose Entity” means a company or trust, insolvency remote, incorporated, created or used solely for the purpose of implementation and operation of traditional or synthetic securitization scheme.

“Sponsor” in relation to-

- a) a traditional securitization scheme means an institution that facilitates, whether at the commencement or during the life of the traditional securitization scheme, in the capacity of arranger and/or structural, the indirect transfer of asset, that is, not from the institution’s own balance sheet, to a special purpose entity; and
- b) a synthetic securitization scheme means an institution that facilitates, whether at the commencement or during the life of the synthetic securitization scheme, in the capacity of arranger, and/or structural, the indirect transfer of risk, that is, not from the institution’s own balance sheet, to a special purpose institution.

“Synthetic securitization” is a structure with at least two different stratified risk positions or tranches (do not need to be in the legal form of a “security”) that reflect different degrees of credit risk where credit risk of an underlying pool of exposures is transferred, in whole or in part, through the use of funded (e.g. credit-linked notes) or unfunded (e.g. credit default swaps) credit

derivatives or guarantees that serve to hedge the credit risk of the portfolio. Accordingly, the investors' potential risk is dependent upon the performance of the underlying pool.

“Traditional securitization” is a structure where the cash flow from an underlying pool of exposures is used to service at least two different stratified risk positions or tranches (do not need to be in the legal form of a “security”) reflecting different degrees of credit risk. Payments to the investors depend upon the performance of the specified underlying exposures, as opposed to being derived from an obligation of the entity originating those exposures.

2. Designation of an activity

Under paragraph (ab) of the definition of **“receiving funds from the public”** in section 1 of the Banking Institutions Act, 1998 (Act No. 2 of 1998) as amended, the Minister on the recommendation of the Bank of Namibia, hereby designates the receiving of funds by a Special Purpose Entity or Issuing Entity from the general public against the issue of commercial paper by the aforementioned Special Purpose Entity or Issuing Entity, in respect of synthetic or traditional securitization schemes, as an activity that does not fall within the definition and meaning of **“receiving funds from the public for purpose of conducting banking business”**: provided that-

- a) When a banking institution within the banking group acts in a primary or secondary role, or both a primary and secondary role, in respect of synthetic or traditional securitization scheme, there shall be compliance by such institution within a banking group with the relevant conditions set out in paragraphs **4 to 21** of this notice.
- b) Non-bank entities acting in the capacity as primary or secondary role or both a primary and secondary role in respect of synthetic or traditional securitization scheme are not subjected to the requirements of paragraph **4, 5, 7, 8, 9, 10, 11, 12, 13, 14.1-3, 15, 16.3-4 and 6, 17, 18, 19, 20, 21 and 21** of this Notice. This is because non-bank financial institutions are not regulated by the Bank and are thus not subjected to the application of risk-weightings applicable to the assets of banks.
- c) Promoters of special purpose entities for the purpose of this Notice, except non-bank entities which are not engaging in banking activities, must apply in writing for the exemption in terms of this clause. The application must be accompanied by a set of information as may be specified by the Bank from time to time.
- d) No transaction other than transaction directly relating to synthetic or traditional securitization scheme shall be entered into by or on behalf of the special purpose entity.

3. Application and purpose

- 3.1 This notice applies to all entities and SPEs as designated under clause 2 above that are engaging in securitisation schemes in Namibia.

- 3.2 The purpose of this Notice is to provide a regulatory framework for the conduct of securitisation transactions subjected to this Notice, in NAMIBIA.

PART 2

OPERATIONAL CONDITIONS

4. Operational Conditions for Securitization Schemes

This Paragraph sets out the operational conditions for both traditional and synthetic securitisation schemes.

- 4.1 Neither the special purpose entity nor any of its creditors shall have the right of recourse against the entity acting in a primary role or any of its associated companies in respect of costs, expenses or losses incurred in connection with any of the assets or risks after the transfer thereof in terms of the traditional or synthetic securitization scheme.
- 4.2 Sub-clause (4.1) shall not apply when the special-purpose institution has a right of recourse against an institution acting in a primary role or any of its associated companies or in respect of losses incurred in connection with any of the assets or risk after the transfer thereof in terms of a traditional or synthetic securitization schemes, and such right of recourse emanates from warranties given by such an institution in respect of assets so transferred: Provided that-
- (a) the warranties do not relate to the future creditworthiness of the obligator in terms of assets or risk transferred; and
 - (b) the warranties do not relate to matters that do not fall within the control of the institution providing the warranties.
- 4.3 No commercial paper issued to investors by the special-purpose institution in respect of assets transferred shall constitute a direct or indirect obligation of the institution that transferred the assets or risk, that is, investors who invest in commercial paper issued by the special-purpose institution shall only have a claim in respect of the underlying pool of assets transferred.
- 4.4 When payments in respect of assets transferred in terms of a traditional securitization scheme are routed through the agency of an institution or any of its associated companies or acting in a primary role, neither the said institution nor any of its associated companies shall be under any obligation to remit funds to the special-purpose institution unless and until the payments are actually received from the obligator.

- 4.5 An asset or risk relating to an asset of an entity shall not be transferred to a special-purpose institution if the transfer will result in a breach of any of the terms of the relevant underlying transaction.
- 4.6 An entity acting in a primary role, may replace, at its own discretion, any asset or risk relating to any asset transferred in terms of a traditional securitization scheme, excluding a non-performing asset or risk relating to a non-performing asset, with an asset of equivalent credit quality.
- 4.7 An entity acting in a primary role, may repurchase assets or risk relating to an asset from a special-purpose institution only when such repurchase is conducted in compliance with the conditions specified below.
- a) The repurchase of assets or risk relating to an asset shall be conducted on market-related terms and conditions.
 - b) Such an entity shall not have any prior obligation to repurchase assets or risk from the special-purpose institution.
 - c) The repurchase of assets or risk from the special-purpose institution shall be subject to the entity's normal credit approval and review processes.
 - d) When the entity acting in a primary role is a bank, the total value of assets or risk associated with assets repurchased from a special-purpose institution in terms of this subparagraph, other than in the entity's normal course of trading in Government securities and qualifying items, and held on the books of the entity at any time, shall not exceed 10 percent of the maximum value of the pool of assets or risk associated with assets held by the special-purpose institution, that is, at least 90 percent of the risk associated with assets transferred to a special-purpose institution shall be transferred to third-parties: Provided that the Bank may in its sole discretion and subject to such conditions as it may determine allow an entity to repurchase assets in excess of limitation.
 - e) An entity may repurchase non-performing assets or risks relating to non-performing assets only if such a bank's or other institution's external auditors have certified that the assets or risks are being acquired at fair market value, which value shall reflect the non-performing status of the asset or risk relating to non-performing status of the asset.
 - f) To the extent that such a repurchase of assets amounts to such an entity providing a liquidity facility, the provisions in this Schedule relating to liquidity facilities shall apply in addition to the provisions of this subparagraph.
- 4.8 Once a securitization scheme has been perfected, the transfer by a bank acting in a primary role of further assets or risks in terms of that scheme shall be permissible only for

purposes of maintaining the capital value of the portfolio of assets of risks included in the scheme: Provided that-

- a) Such a transfer of further assets or risks shall not amount to the provision of a credit-enhancement facility; and
- b) The Bank may in its sole discretion and subject to such conditions as it may specify allow such a bank to transfer further assets or risks in excess of this limitation.

4.9 The securitization transaction shall not contain any clauses that –

- a) Require from the entity that transferred the assets or risks to alter systematically the quality of the underlying exposures such that the pool's weighted average quality is improved;
- b) After the credit transaction's inception, allow for increases in respect of a credit-enhancement facility provided by the entity that transferred the assets to the special-purpose institution;
- c) Increase the yield payable to parties involved in the securitization scheme other than the entity that transferred the assets or risks, such as investors and third-party providers of credit enhancements, in response to deterioration in the credit quality of the underlying pool.

4.10 The board of directors or body of trustees, as the case may be, of a special-purpose institution shall be independent of the entity acting in a primary role. Provided that such an entity acting in a primary role may –

- a) In the case of a company, appoint one director to its board of directors, which board of directors shall consist of not less than three members;
- b) In the case of a trust, appoint one trustee to its body of trustees, which body of trustees shall consist of not less than three members.

4.11 The name of a special-purpose institution shall not include the name of the bank acting in a primary role or imply any association with such a bank, since this usage is guided by the Banking Institutions Act of 1998, as amended.

4.12 When an entity acting in a primary role, in the opinion of the Bank, provides implicit support to a securitization scheme, that is, support beyond the predetermined contractual obligation-

- a) The implicit support shall be regarded as a first-loss credit enhancement facility;

- b) The bank, as a minimum-
 - i shall maintain capital and reserve funds against all exposures associated with a securitization scheme;
 - ii shall not recognize in the bank's capital and reserve funds any gain relating to the securitization transaction, such as an amount relating to expected future margin income;
 - iii shall disclose to the public sufficiently detailed information relating to the implicit support, including the related capital impact of providing implicit support to a securitization scheme.
- 4.13 When an entity acting in a primary role, transfers assets to a special-purpose institution in terms of a traditional securitization scheme, the entity shall receive the amount of consideration paid in respect of the assets so transferred no later than the date of the transfer of assets: Provided that the Bank may in its sole discretion and subject to such conditions as it may specify allow a bank to receive the amount of consideration in respect of the assets so transferred on a date later than the date of the transfer of the assets.

PART 3

RISK-WEIGHTINGS, OFF-BALANCE SHEET EXPOSURES, CLEAN-UP CALLS, IMPLICIT SUPPORT AND *OTHER PROVISIONS*

- 5. Risk-weightings and other operational requirements, Standardized Approach (SA)**
- 5.1 Banking institutions investing in securitisation must compute their respective risk-weighted amount of securitization exposures in accordance with the provisions of the Determinations on the Measurement and Calculation of Capital Charges for Credit, Market and Operational Risk (BID-5) or the Determination (BID-5A), whichever is applicable
 - 5.2 Banking institutions transferring risk must reflect the underlying assets on their balance sheets and, apply the prescribed risk-weights for capital adequacy purpose as though the underlying exposures had not synthetically securitized (if the risk mitigating techniques utilized do not offer capital relief benefit).
 - 5.4 If a banking institution **deduct** a securitization exposure from its total capital amount, the banking institutions must treat the deduction in accordance with the provisions of the Determinations on the Measurement and Calculation of Capital Charges for Credit, Market and Operational Risk (BID-5) or BID-5A, whichever is applicable.
 - 5.5 A bank that transfers assets to a special-purpose institution in terms of a traditional securitization scheme may be allowed to exclude from the calculation of its required capital and reserve funds the assets so sold when the transfer constitutes, amongst other things, a "true sale".

A "true sale" is likely to occur when there is no, inter alia, any obligation:

- a) to repurchase or exchange any of the assets or risks transferred;
- b) for any kinds of legal recourse through which any risk of loss from the assets sold or risks transferred could be retained or put back to the selling bank;
- c) to any party for the payment of principal or interest on the assets sold or risks transferred (other than those arising as services).

5.6 For synthetic securitization scheme, the use of credit risk mitigation techniques (i.e. collateral, guarantees and credit derivatives) for hedging the underlying exposures may be recognized for risk-based capital purpose only if all conditions specified in the applicable Determination on Capital Requirements, i.e. BID-5 or BID-5A, are fully complied with.

5.7 For the purpose of this notice, significant credit risk shall be deemed to have been transferred in any given transaction where the following is present:

- (a) Under traditional securitization exposures, an originating banking institution may exclude securitized exposures from the calculation of risk-weighted assets only if all the conditions specified in the applicable Determination on Capital Requirements, i.e. BID-5 or BID-5A, are fully complied with.
- (b) Banks meeting conditions referred to above in respect of both traditional securitization exposures, must still hold capital against any exposures that they retain.

6. Treatment of Off-balance sheet exposures

6.1 Banking institutions involving in securitization transaction by way of providing either eligible liquidity facilities including both controlled and non-controlled early amortization features or servicer cash advance facilities shall apply the applicable risk-weight as if the exposure is on-balance sheet exposure.

7. Treatment of clean-up calls provision.

7.1 A clean-up call is an option that permits the securitization exposures to be called before all of the underlying exposures or securitization exposures have been repaid. For the purpose of this notice, a clean-up call may take the form of a Paragraph that extinguishes the credit risk protection once the amount of the reference pool of underlying exposures has fallen below a level specified in the securitization documentation. For the originating entity to exercise the clean-up calls, the following requirements shall be adhered to:

- a) The exercise of clean-up call must not be mandatory, in form or substance, but rather must be at the discretion of the originating entity;
- b) The clean-up calls must not be structured to avoid allocating losses to credit enhancement or positions held by investors or otherwise structured to provide credit enhancements; and

- c) The outstanding principal amount of the reference portfolio of the underlying exposures (determined as of the inception of the securitization) must be 10% or less of the original portfolio value.

8. Treatment of Implicit Support

- 8.1 If a banking institution provides support to securitization in excess of the entities contractual obligation to provide credit support to the securitization, the following condition shall be complied with;
 - a) The entity must hold regulatory capital against all of the underlying exposure associated with the securitization as if the exposure had not been securitized and must deduct from tier 1 capital any after-tax gain-on-sale¹ resulting from the securitization; and
 - b) The banking institution must disclose publicly;
 - i That it has provided implicit support to the securitization; and
 - ii The regulatory capital impact of providing such implicit support.

9. Liquidity facilities

Normally, a liquidity facility enables a special-purpose entity to make timely payments of principal and interest amounts to investors, notwithstanding market disruptions or timing differences in the receipt of principal and interest amounts from the pool of assets that was securitized or obtained as collateral, and payment in respect of the senior commercial paper.

- 9.1 A liquidity facility-
 - a) shall not be associated with the credit risk of the underlying or reference asset;
 - b) shall have a specified maturity date;
 - c) shall be duly documented in a manner that clearly distinguishes the facility from any other facility provided by the bank or another institution within a banking group of which such a bank is a member in respect of the securitization scheme;
 - d) shall be transacted on market related terms and conditions, including matters relating to price and fee;
 - e) shall be subject to the bank's normal credit approval and review processes;

¹ Gain-on-sale refers to finance charges collections and other fee income received in respect of securitized exposures net of cost and expenses (future margin income in a securitization).

- f) may be reduced or terminated at the instance of the bank or such other institution within the banking group concerned should be a specified event relating to deterioration of asset quality occur;
 - g) shall contain a reasonable asset quality test to ensure that-
 - i the utilization of such a facility would not cover deteriorated or defaulted assets;
 - ii when the assets covered by the liquidity facility consist of assets that are externally rated, the facility shall be utilized only to fund assets that at the time of funding are rated investment grade, or better;
 - h) shall provide for termination of the facility when-
 - i there is no longer a sufficient level of performing assets of good quality to cover the amount of any new or existing utilization in terms of the liquidity facility;
 - ii the credit-enhancement facilities have been exhausted, that is, there is no longer a sufficient level of credit enhancement to cover the amount of any new or existing utilization in terms of liquidity facility;
 - iii Subject to reasonable qualifying conditions, the parties involved in a securitization scheme or a person acting on behalf of these parties shall have the unequivocal right to select an alternative party to provide a liquidity facility.
- 9.2 There shall be no recourse to an entity which entity provided a liquidity facility, beyond a fixed contractual obligation specified in the facility.
- 9.3 Subject to reasonable conditions, the parties involved in a securitization scheme or a person acting on behalf of these parties shall have the unequivocal right to select an alternative party to provide a liquidity facility.
- 9.4 The documentation relating to the facility shall clearly identify and limit the conditions for utilization and, in particular, shall state that the facility may not be utilized as a permanent revolving facility in order to provide credit enhancement or to cover losses sustained in respect of a securitization scheme.
- 9.5 The utilization of the liquidity facility shall be effected by the special-purpose institution and not directly by the investors.
- 9.6 Subject to the provisions of item 9.1(a) above, the debts resulting from the utilization of the liquidity facility shall not be subordinated to the interests of investors in the securitization scheme provided that the debts resulting from the utilization of the liquidity facility may be subordinated to the debts resulting from the utilization of other liquidity facilities whenever multiple liquidity facilities are provided to a securitization scheme.
- 9.7 Payment of any fee or other amounts due in respect of the liquidity facility shall not be further subordinated or subjected to deferral or waiver beyond what is explicitly provided for in the order of priority and payment entitlement provisions.
- 9.8 The salient features of the liquidity facility shall be disclosed in the disclosure document issued in respect of the securitisation scheme.

- 9.9 The disclosure document issued in respect of the traditional or synthetic securitization scheme shall contain a clear and unequivocal statement that-
- a) The obligations of the entity in respect of a liquidity facility do not significantly extend beyond the salient features disclosed in accordance with item 9.7 above;
 - b) The entity will not support the securitization scheme beyond the obligations stipulated in sub-item (a) above.

PART 4

CREDIT RISK RETENTION AND ELIGIBLE CRITERIA FOR RATING AGENCIES AND APPOINTMENT OF AUDITORS

10. Credit risk/reward retention requirements

- 10.1 Credit risk/reward retention refers to a situation where originating entity retains a portion of risk and net economic benefits associated with the asset securitized. The requirement is necessary to achieve alignment of the originating entity's interest with that of the investors, where originating entities also keep their own money at risk and do not have an incentive to securitize bad loans or lower their loan underwriting standard. The retention requirements is measured at the origination (when the exposures are being securitized for the first time) of securitization transaction, and shall be maintained throughout the life of the transaction (ongoing basis).
- 10.2 For the purpose of this notice, "**retention of credit risk/reward**" means that originating entities' interest of no less than 10 percent of the nominal value of the securitized exposures shall be maintained (on-balance sheet retention or any other form of credit risk retention). The application of hedging instruments and other credit risk mitigation techniques on the portion of retained exposures are not permitted under this notice for both traditional and synthetic securitization exposures (because such practice will defeat the purpose of credit risk retention requirement) this prohibition last so long as the securitization is outstanding.
- 10.3 The notice does not prescribe any particular form of credit risk retention that needs to be applied by individual originating entity, but any one of the several options as discussed in annex "**A**" of this notice may be chosen.

11. Eligibility Criteria for Credit Rating Agencies (CRAs)

- 11.1 Banking institutions that are utilizing the services of rating agencies are required in terms of this notice to only apply ratings assigned by rating agencies that are fully compliant with the eligibility criteria as outlined by the Basel Committee for Bank Supervisors.

- 11.2 Additionally, it is advised that where possible Credit rating agencies whose services are utilized by banking institution in Namibia must be registered with the European Security and Market Authority (ESMA). This is necessary because the ESMA assumes general competence in matters relating to the registration and on-going supervision of activities of registered credit rating agencies. (This additional requirement is based on the BCBS's recommendations reflected in the Report on securitization incentives dated July 2011).
- 11.3 Where the requirements outlined in 11.2 above are not complied with by the Credit rating agency whose services are being sought by banking institutions in Namibia, a written opinion of the home regulator on the reputation and credibility of such agency should be submitted to the Bank for consideration and approval, according to the Bank's internal procedures.

12. Appointment of an Independent Auditor

- 12.1 The board of directors or the trustee, as the case may be, of a special-purpose entity established for purposes of a traditional or synthetic securitization scheme shall appoint an independent auditor, who, in addition to his or her normal duties as independent auditor, shall be required-
- (a) to satisfy himself or herself that, on the basis of the information presented to him or her by the special-purpose entity, there shall be compliance with the relevant provisions of this Notice with regard to the conduct of the traditional or synthetic securitization scheme; and
 - (b) if such an auditor has so satisfied himself or herself, to furnish a statement to that effect, which statement shall be included in the disclosure document issued by the special-purpose institution with regard to the traditional or synthetic securitization scheme, in accordance with the provisions of clause 19 of this Notice.

PART 5

MANAGEMENT AND RESTRICTIONS

13. Management of securitization exposures

In fostering the establishment of sound and prudent management practices for trading in securitization, the Bank, requires entities and SPE to have in place appropriate systems and the necessary expertise to structure, execute, and monitor the securitization transactions.

- 13.1 The risk arising from securitization transactions in relation to which an entity is originator, investor or sponsor must be evaluated and addressed through the use of appropriate written policies and procedures, to ensure in particular that the economic substance of the transaction is fully reflected in the risk assessment and management decisions.
- 13.2 An entity that is party to the securitization transaction must fully understand the risks it has assumed or retained. In particular, it should do so in order that it can accurately determine in accordance with this notice the capital effect of the (retained portion) securitization.
- 13.3 The Bank expects an entity to continue to monitor any risks that it may be subject to when it has excluded the securitized exposures from its calculation of risk-weighted exposures amounts. The entity should consider the capital planning implications where risk may return and the impact that securitization has on the quality of the remaining exposures held by the originator.
- 13.4 There must be a clear delineation between securitized and non-securitized assets/loans (ring-fencing of securitized exposures by the originator for control purpose). Banking institutions are further required in terms of BID-18 to disclose the type of risks they are exposed to, their risk management objectives and policies including but not limited to the following disclosures:
- a) Summary of documented banks policies and procedures on securitization activities;
 - b) Total outstanding exposure securitized by the banking institution (for which the bank is obliged to collect payment on behalf of SPE);
 - c) Amount of non-performing loans and advances securitized (all classification categories as set out in BID-2);
 - d) Amount of losses recognized by the bank;
 - e) Aggregated amount of securitized exposures and risks retained by the bank;
 - f) Total amount of accounts settled before their original maturity date (early amortization)
 - g) Repurchased securitization exposures if any; and
 - h) Statutory capital amount held by the originating bank for retained exposures.

14. Restriction on utilizing funds sourced through securitization transactions for loans or investments purpose

14.1 Non-bank entities can engage in securitization transactions provided that the funds sourced through such transactions are utilized for infrastructural developmental and other purposes other than making loans or investments unless permitted by law.

15. Limits on the amount to be securitized:

15.1 **Diversified portfolio**, where the portfolio is composed of different types of loans the aggregated amount of that portfolio shall not exceed an amount equal to 5% of total loans and advances of the banking institution concerned at all time.

15.2 **Non diversified portfolio**, where the pool of loans is composed of one type of loans the aggregated amount of securitized exposures shall not exceed an amount equal to 10% of the total outstanding balance of that particular portfolio of the banking institution concerned at all time.

15.3 The minimum amount (value) that is permitted to be originated or securitized by non-bank or non-bank financial entities per programme/transaction shall not be less than an amount of N\$200 million.

15.4 Entities are required in terms of this Notice to ensure that, as a minimum requirement, the residential mortgage loan underlying the mortgage backed securities (MBS) must satisfy the following criteria:

- a) The borrower is an individual and legal entity;
- b) The debt is secured by the first legal charge on the property;
- c) The property secured by the charge is used as a borrower's residence or as a residence by a tenant of the borrower;
- d) The MBS should be fully secured at all times against residential mortgage loans which meet all the above conditions;
- e) The mortgage loans must not be in default at the time at which the risks inherent in exposures are being transferred to the issuer (special purpose entity); and
- f) The issuer of the MBS must be a Special Purpose Entity whose activities are exempted from the definition of "receiving funds from the public" and "banking business".

15.5 Limit on Investment in Securitised Assets by banking institutions:

The total amount of investment in securitised assets (Synthetic and Traditional) of a single entity must not exceed an amount equal to 30% of total qualifying capital of the investing banking institution (investor) at all time.

15.6 Originating entity must ensure that only good quality assets are securitised.

The potential risk of loss for the investors in commercial paper issued by the special-purpose entity primarily depends upon the performance of the underlying assets obtained by the special-purpose institution.

- a) To prevent the inclusion of non-performing loans in the pool of assets to be securitized, banking institutions are only permitted under this notice to securitize asset in the classification category of “**pass and special mention**” as determined in accordance with the requirements of the Determination on Asset Classification, Suspension of Interest and Provisioning (BID-2); and
- b) Non-bank entities must ensure that only performing assets (no arrears assets), by their respective classification standards. These assets should be confirmed by an independent auditor before being securitised which certification must be submitted to the SPE. This requirement is necessary to enable SPE to provide the same to the Bank should it be required to do so.

16 Servicing

- 16.1 A banking institution may undertake, notwithstanding the fact that such a banking institution is acting in a primary role, the role of servicing agent in respect of a traditional or synthetic securitization scheme provided that –
- a) A formal servicing agreement shall be in place, which agreement shall specify the services to be provided and the standard for the performance of the services;
 - b) Confirmation shall be included in the disclosure document that the servicing agent, in its capacity as servicing agent, is under no obligation to fund payments owed in respect of the securitization scheme, absorb losses incurred in respect of the assets or risk transferred to the special-purpose institution concerned, or otherwise recompense investors for losses incurred in respect of the said securitization scheme;
 - c) The servicing agent may withdraw, at its own discretion and subject to a reasonable period of notice, from its commitments as servicing agents;
 - d) Services and remuneration shall be provided in accordance with market related terms and conditions.
- 16.2 When payments due in terms of an underlying transaction are made through the agency of a banking institution that acted in a primary role, the banking institution shall not transfer any funds to the special-purpose institution in respect of such payments unless such payments have actually been received from the obligator in terms of the underlying transaction.
- 16.3 Payment of any fee or other amounts due in respect of the services of a banking institution acting as a servicing agent may not be further subordinated, or be subject to deferral or

waiver, beyond what is explicitly provided for in the order of priority set forth in the provisions of securitization scheme that regulate entitlement to payment.

PART 6

OWNERSHIP OF SPEs, DISCLOSURES AND REPORTING

17. Degree of Ownership or Control of SPEs

An entity acting in a primary role shall not –

- a) In the case of a special-purpose entity that is a company –
 - (i) Directly or indirectly acquire or hold any equity share capital in such a special-purpose entity of which the nominal value represents 20 percent or more of the nominal value of all the issued equity share capital in the special-purpose entity;
 - (ii) Have the right to determine the outcome of the voting at a general meeting of the special-purpose entity;
- b) In the case of a special-purpose entity that is a trust –
 - (i) Directly or indirectly or hold any beneficial interest in or be a beneficiary of such a special-purpose institution of which the value represents 20 percent or more of the interest (beneficial or otherwise) in the property forming the subject matter of the special-purpose institution;
 - (ii) Have the right to determine the outcome of the voting at a general meeting of the special-purpose institution.

18. Disclosures and reporting requirements

18.1 Originating entities shall ensure continued information transparency where the public, investors and other market participants are regularly updated through the SPE with the following information:

- a) Risk characteristic of the securitization position (where the banking institution operate in the capacity of an investor)
- b) Risk characteristic of the underlying exposures (originator)
- c) Statement/disclosures of originators about due diligence on the securitized exposures and collateral
- d) Methodologies underlying valuation of collateral and policies that ensures independence of valuer
- e) Material structural features of the securitization
- f) Performance information on exposures underlying securitization positions.
- g) Amount of the retained portion of the securitized asset.

- 18.2 Banking Institutions shall at the end of six-month period (i.e. end of June and December each year) submit to the Bank a statutory return in the format, frequency and submission date as may be specified by the Bank.
- 18.3 A disclosure document shall be issued by a special-purpose entity in respect of a traditional or synthetic securitization scheme, which document, as a minimum, shall clearly state, amongst other things-
- a) The name of the special-purpose entity;
 - b) The name of the auditor of the special-purpose entity;
 - c) The total amount of commercial paper to be issued by the special-purpose entity;
 - d) Whether or not the particular issue of commercial paper is listed;
 - e) A description of the assets transferred or the portfolio credit-derivative instrument used to transfer risk and the nature of such risk;
 - f) The cash flows arising from the assets transferred or purchased as collateral, or the premiums received, that will be utilized for the payments by the special-purpose entity in respect of the commercial paper issued;
 - g) Confirmation by the auditor of the special-purpose entity that the issue of commercial paper pursuant to a securitization scheme complies in all respects with the relevant provisions of this Schedule;
 - h) The details of any credit-enhancement facilities;
 - i) The details of any liquidity facilities;
 - j) That the institution acting in a primary role is not obliged to support any losses suffered by the special-purpose entity in respect of a traditional or synthetic securitization scheme;
 - k) That the board of directors or the trustees of the special-purpose entity are independent of the institution acting in a primary role and, whenever such an institution is a bank, of any other institution within a banking group of which such a bank is a member;
 - l) All other information that may reasonably be necessary to enable an investor to ascertain the nature of the financial and commercial risk of his or her investment.
- 18.4 The Bank may prescribe additional disclosure requirements in respect of a traditional or synthetic securitization scheme.

- 18.5 A disclosure document relating to the issue of commercial paper pursuant to a traditional or synthetic securitization scheme-
- a) Shall in the case of a special-purpose entity that is a company, be signed by two directors of such a company who are duly authorized to sign;
 - b) Shall in the case of a special-purpose entity that is a trust, be signed by two senior officials of such a trust who are duly authorized to sign.
- 18.6 Once a disclosure document has been signed by the persons indicated in 18.5 above, such signatories shall be deemed to have authorized the issue of such disclosure document.
- 18.7 Every signature to a disclosure document shall be dated, and the latest of such dates shall be deemed to be the date of the disclosure document.

**PART 7
CORRECTIVE MEASURES**

19. Remedial measures

Failure to adhere to the provisions of this notice will be dealt with in accordance with the provisions of section 71(2) of the Act.

**PART 8
EFFECTIVE DATE**

20. Effective date

This notice will become effective as from (specified date)

**PART 9
ENQUIRIES**

21. Enquires

Questions relating to this notice should be addressed to:

The Director
Banking Supervision Department
Bank of Namibia
P O Box 2882
71 Robert Mugabe Avenue, Windhoek, Namibia
Telephone number: +26461 283 5040
E-mail: romeo.nel@bon.com.na

ANNEX “A” FORMS OF CREDIT RISK

RETENTION

Credit risk retention refers to a situation where originating bank or sponsor retains a portion of risk and net economic benefits associated with the asset securitized. The requirement is a global market practice and became necessary to achieve the alignment of originating bank’s interest with that of the investors, where originating banks also keep their own money at risk and do not have an incentive to securitize bad loans or loosen their loan underwriting standard. The proponents of the credit risk retention concept proposed six principal options for (a) satisfying the risk retention requirements and (b) to accommodate a variety of structures utilized in the securitization dealings, these options are briefly discussed in the table below.

CREDIT RISK RETENTION OPTIONS (CRRO)

1. <u>VERTICAL SLICE OPTION</u>
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<p>Under this option, originating bank can satisfy the credit risk retention requirements by retaining at least 10% of each class of ABS interest² in the issuing entity issued as part of the securitization transaction. This minimum retention requirement applies, regardless of the nature of the class of ABS interest (e.g. senior or subordinated) and regardless of whether the class of ABS interest has a par value, was issued in certificated form or was sold to unaffiliated investors.</p>

<p>As noted above, the method for measuring the amount of each class of ABS interest is not specified. The treatment is such that regardless of the method of measurement, the amount retained by the originator utilizing the vertical slice option “should equal at least to ten percent (10%) of the par value (if any), fair value, and number of shares or units of each class.</p>
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² For the purpose of the Exemption Notice, the term “ABS-Interest” refers to any type of interest or obligation issued by an issuing entity, whether or not in certification form, payment on which are primarily dependent on the cash flows of the collateral owned or held by the issuing entity. Under the “vertical slice option”, the originator or other entity retain a specified pro rata piece of every class of interest issued in the transaction.

2. HORIZONTAL SLICE OPTION

Originator can satisfy the credit risk retention under this option by retaining an “eligible horizontal residual interest³” in an amount that is equal to at least ten percent (10%) of the par value of all ABS interest in the issuing entity issued as part of the securitization transaction. An eligible horizontal residual interest is an ABS interest that: -

- Is allocated all losses on the securitized assets (other than losses that are first absorbed through the release of funds from a premium capture cash reserve account, if such an account is required to be established as described below under “horizontal cash slice option) until the par value of such ABS interest is reduced to zero;
- Has the most subordinate claim to payment of both principal and interest by the issuing entity; and
- Until all the ABS interest in the issuing entity are paid in full, is not entitled to receive any payments of principal made on securitized assets; provided, however, an eligible horizontal residual interest may receive its current proportionate share of scheduled payments of principal received on securitized assets in accordance with the transaction documents.

³ Eligible Horizontal Interest is an ABS interest that; (1) hold the most subordinated claim to payment of both principal and interest and (2) bears the first loss in the event of insufficient funds to repay the ABS obligations.

3. HORIZONTAL CASH SLICE OPTION

The originator can satisfy the credit risk retention requirements by establish and fund, in cash, a horizontal cash reserve account in an amount equal to ten percent (10%) of the par value of all ABS interest in the issuing entities. The horizontal cash reserve account must meet all the following conditions: -

- The account is held by the trustee (or person performing similar functions) in the name and for the benefit of the issuing entity;
- Amount held in the account are invested only in GRN Treasury Bills, GRN stocks of instruments issued by Bank of Namibia
- Until all ABS interest in the issuing entity are paid in full or the issuing entity is dissolved: -
 - Amount in the account shall be released to satisfy payments on ABS interest in the issuing entity on any payment date on which the issuing entity has insufficient funds from any source to satisfy an amount due on any ABS interest: and
 - No other amount may be withdrawn or distributed from the account except that:
 - Amount in the account may be released to the originator or any other person due to the receipt by the issuing entity of scheduled payment of principal on the securitized assets, provided that such release of scheduled principal may not exceed the proportion of the current balance in the account to albas interest in the issuing entity; and
 - Interest earned on the account may be released once received by the account.

4. "L" SHAPED OPTION

Under this option the originator can satisfy the risk retention requirements by using a combination of the vertical slice option and the horizontal slice option (or horizontal cash reserve account in lieu of the horizontal slice option). Specifically, originator can satisfy the credit risk retention requirements if, at the closing of the securitization transaction, the originator:

- Retain not less than five (5%) of each class ABS interest in the issuing entity; and
- Retains an eligible horizontal residual interest in the issuing entity (or establishes and funds a horizontal cash reserve account) in an amount equal to at least five (5%) of the par value of all ABS interest other than the vertical portion of such ABS that the originator is required to retain as describe in the above bullet points above. This option combines the characteristics of both vertical slice option and horizontal cash slice option.

5. REPRESENTATIVE SAMPLE OPTION

The general requirements of this option is that, the originator can satisfy the retention by retaining ownership of a representative sample of the pool of assets that are designated for securitization and draws from such pool all of the securitized assets for the securitization transaction, provided that: -

- From the unpaid principal balance of the assets comprising the representative sample, the originator retains an amount equal to ten percent (10%) of the unpaid principal balance of all the securitized assets; and
- The “designated pool” with respect to any securitization transaction consists of the securitized assets comprising the representative sample and the originator must identify a designated pool of assets:
 - That consist of a minimum of 1000 separate assets;
 - From which the securitized assets and the assets comprising the representative sample are drawn; and
 - That contains no assets other than securitized assets or assets comprising the representative sample.

The representative sample option is not viable for Commercial Mortgage Bond Security (CMBS) transactions or securitization of large commercial loans.

6. REVOLVING ASSETS MASTER TRUST (SELLER’S INTEREST)

Securitization backed by revolving lines of credit, such as credit cards or dealer’s floor plan, often are structured using a revolving master trust, which allows the trust to issue more than one series of BAS backed by a single pool of the revolving assets. In these types of transactions, the originator or other entity (sponsor) typically holds an interest known as a “seller’s interest”.

This interest is normally pari-passu with the investor’s interest in the receivables backing the ABS interest of the issuing entity until the occurrence of early amortization events⁴. A seller’s interest is a direct, shared interest with all the investors in the performance of the underlying assets and thus, exposes the originator to the credit risk of the pool of receivables.

The general requirements of this option is that, the originator of the revolving assets master trust⁵ that is collateralized by loans or other extension of credit that arises under revolving accounts to meet its base risk retention requirement, by retaining a seller’s interest in an amount of not less than ten percent (10%) of the unpaid principal balance of all the assets held by the issuing entity.

⁴ Refers to those events whose occurrence will shorten the lifetime of the ABS, if there is any danger that the investor will not be fully paid.

⁵ The revolving master trust is defined as “an issuing entity that is (1) A master trust; and (2) established to issue on multiple issuance dates one or more series, classes, subclasses, or tranches of asset-backed securities all of which are collateralized by a common pool of securitized assets that will change in composition over time”

ALLOCATING OF RISK RETENSION, MULTIPLE ORIGINATORS

If a securitization transaction has multiple sponsors/originators, it is proposed that one of the originator or sponsor comply with the risk retention requirements. However, each sponsor/originator would remain responsible for ensuring that at least one of the sponsor or originator complies with the risk retention requirements.