

New LEGISLATION

SEC's Proposed Rule To Stop Banks From Profiting At Investors' Expense

(Sarah N. Lynch) - Underwriters or sponsors of asset-backed securities would be banned for one year from taking positions to profit from investors' losses under a plan released by U.S. securities regulators on Monday.

The proposal by the Securities and Exchange Commission would get at the very heart of issues raised by U.S. Senate investigators in a report earlier this year that accused Goldman Sachs of positioning itself to profit from clients' losses on complex securities that it packaged and sold.

The proposal would also prohibit the kinds of conflicts that were seen in the SEC's civil case against Goldman in 2010 by banning third parties from helping assemble an asset-backed pool that would let those parties profit from investors' losses.

In the Goldman case, the SEC accused the bank of creating and marketing a CDO known as ABACUS 2007-AC1 without telling investors that hedge fund Paulson & Co helped choose the underlying securities and was betting against them. Goldman later settled the case for \$550 million.

The SEC's proposal, expected to be put out for public comment later on Monday, would implement a provision in the Dodd-Frank Wall Street overhaul law that sought to prevent big banks from betting against financial products that they package and sell to investors.

The one-year ban from taking an opposite market position from investors would not apply in certain key cases, such as when a firm is hedging its risk or acting as a market-maker.

It would prohibit underwriters, placement agents, initial purchasers, sponsors, or any of their affiliates or subsidiaries of an asset-backed security from shorting the assets in the pool and creating a material conflict for investors. The shorting ban would be in effect for one year after the first closing of the sale.

The securities industry will likely pay very close attention to how the SEC's proposal fleshes out the details of the exemptions. If the SEC is too restrictive in the kinds of permitted activities, some industry executives have warned it could impede the recovery of the securitization market.

(Reporting by Sarah N. Lynch; editing by John Wallace)