



**The Role played by Securitization in the Finance Market in Sri Lanka: A Way forward**

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*The Thesis/Dissertation/Research Report submitted to*

**GENERAL SIR JOHN KOTELAWALA DEFENCE UNIVERSITY**

**SRI LANKA**

*In partial fulfillment of the requirement for the award of the degree*

*Of*

**MASTER OF LAWS**

**10<sup>th</sup> August 2024**

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## **ABSTRACT**

Securitization is a modern financing concept used by financial institutions to enhance capital. The process involves several steps. A bank or other financial organization first selects the loans that should be taken off of its balance sheet and puts them into a portfolio. After that, a Special Purpose Vehicle (SPV) buys this portfolio and uses the proceeds from the sale to issue securitized bonds. Any asset generating cash flows can be securitized, including home mortgages, personal loans, auto loans, lease and hire purchase agreements, credit card payments, and utility bills. Home mortgage securitization is known as Mortgage-Backed Securitization (MBS), while securitization of other assets is called Asset-Backed Securitization (ABS). Securitization began in the USA with government-backed agencies pooling home mortgages. In the 1980s, other income-generating assets were included. Countries like Australia and the UK are also prominent in securitization.

In Sri Lanka, securitization primarily involves home mortgages and leasing contracts. However, many deals resemble loans more than true securitization, with underlying assets used as collateral and originators guaranteeing repayment. In genuine securitization, the SPV holds the credit risk, not the originator. Investors bear any losses once assets are sold, and the originator is not obliged to repurchase defaulted credits. The Finance Leasing Act No. 56 of 2000 permits Finance Leasing Companies in Sri Lanka to participate in securitization on a regular basis. This Act's Section 24 permits lessors to assign or transfer their rights, subject to lessee authorization, which is frequently spelled out in lease agreements. Since the Finance Leasing Act's Section 24(1) requires the Central Bank to approve securitization schemes, Sri Lankan securitization lacks actual structural integrity. Regarding the approval of quasi-structural securitizations, there remains uncertainty.

Apart from the Finance Leasing Act, Sri Lanka has no specific securitization regulation. The Securities and Exchange Commission attempted to introduce securitization legislation, but it remains inactive. The absence of a dedicated securitization law in Sri Lanka leads to industry issues and potential unauthorized activities. This research focus on due to structural and regulatory problems, the Sri Lankan securitization market is hindered in its ability to grow and be transparent, which affects investor confidence and market stability. Objective of this research is analyze the current regulatory framework governing securitization in Sri Lanka, evaluate the structural integrity of securitization practices in comparison to international standards and identify challenges and opportunities for developing a robust securitization market in Sri Lanka.

This research uses a quantitative methodology, and it thoroughly reviews the literature on securitization that has already been written, with an emphasis on regulatory frameworks, industry practices, and the difficulties faced by emerging markets. It also analyzes academic papers, industry reports, and legal documents to provide a theoretical framework for the study. Finally, it looks at the regulations that currently govern securitization in Sri Lanka, identifying specific laws, regulations, and guidelines that are relevant to the market and comparing them with international best practices and standards to find any gaps or weaknesses. In order to strengthen Sri Lanka's securitization industry, this research recommends legislative and regulatory actions as well as the creation of a specific securitization law. Some of the main recommendations include creating a comprehensive legal and regulatory framework, raising the bar for transparency and disclosure, ensuring asset quality and due diligence, implementing risk retention clauses, fortifying investor protection measures, developing market infrastructure, and resolving inconsistent tax and accounting treatment. It also suggests amending the current mortgage, property registration, and debt recovery regulations.

**Key Words:** Securitization, Underlying Assets, Investor, Originator, Special Purpose Vehicle (SPV)