FEDERAL DEPOSIT INSURANCE CORPORATION, Washington, DC 20429

SHEILA C. BAIR
CHAIRMAN

July 28, 2010

Honorable Barney Frank
Chairman
Committee on Financial Services
House of Representatives
Washington, D.C. 20515

Dear Mr. Chairman:

I am writing in response to your request for my views on recent legislative proposals concerning covered bonds.

The FDIC has long supported a vibrant, sustainable covered bond market. Before the crisis, the FDIC worked closely with Washington Mutual and Bank of America when they launched the first U.S. covered bond programs in 2006. As a result, Bank of America was able to issue covered bonds at a lower cost than many European issuers. In 2008, the FDIC issued a Statement of Policy that set standards the industry agreed created a framework for an active U.S. covered bond market. The FDIC worked closely with Treasury in its development of supporting 'best practices' for covered bonds. Unfortunately, the market collapse of 2008 prevented initiation of any new covered bond programs. Even during that crisis, however, the FDIC was able to sell Washington Mutual's covered bond program intact to JPMorgan in a failed bank resolution transaction – demonstrating the effectiveness of the process outlined in our Statement of Policy.

As you know, covered bonds are general obligation bonds of the issuer, normally an insured bank or thrift, with payment secured by a pledge of a pool of loans. This inherently involves significant over-collateralization beyond the face amount of the bonds. When a bank fails, the FDIC must have flexibility – as it does under current law for any other secured claim – to recapture this over-collateralization. To prevent moral hazard and to protect the Deposit Insurance Fund (DIF), we have suggested that the FDIC must continue to have the flexibility to perform under the covered bond program, sell it to another bank, turn over the collateral to the investors, or terminate the covered bond agreements, pay the face amount of the bonds, plus accrued interest due, and recapture this over-collateralization.

Unfortunately, proposals we have seen would require the FDIC to hand over the excess collateral to covered bond investors without effective compensation. No other secured creditor has such rights under banking law, the Bankruptcy Code, or long-

standing American law, which has always limited any secured claim to the value owed – here defined by the face amount of the bonds. Adoption of these proposals will increase the costs to the DIF by taking away the value of the over-collateralization and turning it over to the investors.

Again, thank you for soliciting our views on this matter of great importance to the FDIC. We stand ready to work with you and your staff on legislation that will support a healthy, vibrant covered bond market in a way that promotes market discipline among covered bond investors and protects the Deposit Insurance Fund.

Sincerely,

Sheila C. Bair

FEDERAL DEPOSIT INSURANCE CORPORATION, Washington, DC 20429

SHEILA C. BAIR
CHAIRMAN

September 3, 2010

Honorable Jeffrey Merkley
United States Senate
Washington, D.C. 20510

Dear Senator Merkley:

Thank you for sharing your views with me relative to the proprietary trading and conflicts of interest sections of the Dodd-Frank Wall Street Reform and Consumer Protection Act. I have placed them in the public docket and we will consider them carefully as we move forward with our rulemaking process.

We appreciate your interest and comments regarding this important issue. If you have further questions or comments, please do not hesitate to contact me at (b)(2) (b)(2) or Paul Nash, Deputy for External Affairs, at (b)(2)

Sincerely,

Sheila

Sheila C. Bair

FEDERAL DEPOSIT INSURANCE CORPORATION, Washington, DC 20429

SHEILA C. BAIR
CHAIRMAN

September 3, 2010

Honorable Carl Levin
United States Senate
Washington, D.C. 20510

Dear Senator Levin:

Thank you for sharing your views with me relative to the proprietary trading and conflicts of interest sections of the Dodd-Frank Wall Street Reform and Consumer Protection Act. I have placed them in the public docket and we will consider them carefully as we move forward with our rulemaking process.

We appreciate your interest and comments regarding this important issue. If you have further questions or comments, please do not hesitate to contact me at (b)(2) (b)(2) or Paul Nash, Deputy for External Affairs, at (b)(2)

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