745 Seventh Avenue
New York, NY 10019
United States

July 21, 2011

U.S. Department of the Treasury
Office of the Comptroller of the Currency
250 E Street, SW., Mail Stop 2-3
Washington, DC 20219
Docket Number OCC-2011-0002

U.S. Securities and Exchange Commission
100 F Street, NE.
Washington, DC 20549-1090
Attn.: Elizabeth M. Murphy, Secretary
File Number S7-14-11

Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue, NW.
Washington, DC 20551
Attn.: Jennifer J. Johnson, Secretary
Docket No. R-1411

U.S. Federal Housing Finance Agency
Fourth Floor
1700 G Street, NW.
Washington, DC 20552
Attn.: Alfred M. Pollard, General Counsel
RIN 2590-AA43

Federal Deposit Insurance Corporation
550 17th Street, NW.
Washington, DC 20429
Attn.: Comments, Richard E. Feldman, Executive Secretary
RIN 3064-AD74

U.S. Department of Housing and Urban Development
Regulations Division
Office of General Counsel
451 7th Street, SW., Room 10276
Washington, DC 20410-0500
Docket # FR-5504-P-01

Re: Credit Risk Retention; Proposed Rule

We are writing to provide our thoughts and concerns regarding the recently promulgated risk retention rules and their potential impact on the U.S. structured finance and housing markets. We appreciate the continued efforts of the regulators in jointly constructing workable regulations that benefit markets and follow the legislative intent of Congress. We understand the motivations behind the risk retention rules in particular, namely to encourage prudent mortgage lending and sound securitization structures; however, we urge careful consideration and impact study of the proposed rules to ensure these aims are achieved without overly restricting credit in the housing market.

Moreover, we believe risk retention has limited use as a complementary tool in overall securitization reform, and is not a primary solution. It is an indirect means of encouraging strong lending standards; underlying issues, such as asymmetry of information (among investors, securitizers and originators) and resulting suboptimal screening activity at loan origination are best addressed directly. If the intent of risk retention is to properly align securitizers' interests with those of investors, stronger

repurchase mechanisms, servicing standards and better information offer a more direct path to that end goal.

As a basic premise, securitization can provide meaningful and efficient financing to housing markets and the broader economy. We have advanced beyond the post-crisis qualitative questioning of the process. The Federal Reserve's TALF program successfully rejuvenated certain sectors of the securitization markets. Treasury has expressed continued support for the securitization markets and we note the abridged conclusions of the Financial Stability Oversight Council's Study on the Macroeconomic Effects of Risk Retention Requirements:

i) securitization is an important source to the economy of credit formation, but has certain risks;
ii) risk retention can address *some* of these inherent risks; and
iii) to the extent it can incent better lending, it *may* help mitigate some of the pro-cyclical effects of securitization on the economy.

This seems to be a clear acknowledgement that risk retention, while a useful part of a broader regulatory toolkit, is limited in its utility. Having examined the proposed rules from our position as a sponsor of ABS transactions, we are concerned that rulemaking without proper study of the impact on markets could cause negative unintended consequences. We believe the rules as currently proposed embed in the regulatory framework excessive cost and complexity that could impede the revitalization of healthy securitization and housing markets, and potentially unduly restrict credit availability for a majority of consumers, contravening stated policy goals of both Congress and the White House. The supply of credit to borrowers of varying, documented income levels is essential to encourage home purchases on a national level. Borrowers at low and moderate income levels that save meaningful down payments, possess good credit histories and earn steady income may be priced out of home ownership by the proposed rules.

The Congressional mandate set forth in the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (the "Act") was intended to address transparency, conflicts of interest and require credit retention by securitizers. In reviewing the proposed rules, it is critical to remember that risk retention is one of many reforms and cannot by itself constitute, and should not compromise, securitization reform's goal. With that background, we would like to provide our views on the following aspects of the risk retention rules:

I. Synthetic Transactions
II. Retention Form
III. Retention Allocation
IV. QRM Definition
V. Resecuritizations
VI. Premium Capture Cash Reserve Account

I. Synthetic Transactions

The exclusion of synthetic transactions from the risk retention rules described in Footnote 32 of the proposing release is very concerning. It states, "Because the term "asset-backed security" for purposes of section 15G includes only those securities that are collateralized by self-liquidating financial assets, "synthetic" securitizations are not within the scope of the proposed rules". This exclusion will push certain otherwise standard securitization activity from the cash markets to the synthetic markets in the form of ABS credit default swaps and total return swaps. The purpose of Section 941 of the Act will be contravened if securitization vehicles can be synthetically exposed to underlying assets without regard to how those assets are underwritten. Moreover, large sponsors (primarily commercial banks) could effectively hedge or sell off all of their risk through a synthetic transaction, while smaller sponsors would only have the option of all-cash securitizations that are bound by the risk retention rules, making them more costly and executed with greater risk to sponsors.

II. Retention Form

The Act gives regulators full authority to independently determine the form of risk retention. The proposed forms of risk retention pose significant issues for securitizers. For example, if a sponsor retains risk through a horizontal slice of the capital stack, capital will be trapped until cash flows fully pay off the bond. Additionally, the capital charges incurred on that retention over the life of the bond will be held captive. This will restrict future lending to new borrowers. These capital implications inherent in horizontal risk retention create a disincentive for sponsors to use this option.

The representative sample option therefore looks like a more attractive alternative, but is a viable alternative only for large commercial lenders. If these entities retain a representative sample of loans on balance sheet, it will allow them to gain an even larger share of the market than they already enjoy. In the residential mortgage loan industry, four banks control approximately 70% of the private origination market. Due to their greater capital capacity and because they can originate excess assets that are not securitized, certain banks will gain an advantage over sponsors that cannot employ the representative sample option.

This could result in most non-QRMs, including loans to the least creditworthy borrowers, sitting on the books of a few large commercial banks, exacerbating the "too big to fail" risk and potentially crowding out other types of players (e.g. investment banks, other financial institutions) from the market. Such an outcome would not further the regulators' goal of reducing systemic risk while preserving access to credit as it would limit the distribution of risk to and capital access from hedge funds and other institutional clients, an important feature of such intermediary participation. Moreover, although assets

will swell, the balance sheets of these banks are still not large enough to absorb the loan levels necessary to revive and sustain the housing markets.

III. Retention Allocation

The limited ability to allocate risk retention to non-sponsor participants (other than originators) in a securitization under the proposed rules should also be re-examined. The concepts driving the provisions allowing allocation of risk retention to CMBS B-piece buyers to satisfy retention requirements should be extended to RMBS. Although third party buyers in the RMBS market historically have not conducted due diligence on assets and purchased first loss pieces in the same manner and to the same extent as they have in the CMBS market, allowing for this option would create a valuable tool capable of directly addressing incentive misalignment.

This option would also provide an additional check on prudent loan origination while ensuring a robust private label securitization market and offering risk to those best placed to bear it. Third parties investors can conduct due diligence on assets and negotiate appropriate pricing for risk to be held in their investment portfolios. Many sponsor institutions are not investors, but rather serve as market intermediaries that are constricted by the Volcker Rule-related limitations on proprietary investments. In conjunction with this policy shift and revised risk management policies, the capacity of many sponsors to be exposed to macroeconomic or other shocks is very limited. Also, because hedging of retained risk is restricted, broker-dealers will be limited in the amount of risk they can hold, forcing them to steer away from valuable intermediary activity as sponsors of securitizations.

We recognize that any proposed or final CMBS standards cannot simply be grafted onto other asset classes, however, and welcome the opportunity to discuss alternatives and provide feedback on proposed models. For example, because RMBS investors may not be expected to perform extensive diligence on each residential mortgage loan in a transaction that is collateralized by hundreds or thousands of assets, they could be expected or required to conduct diligence on a specified amount of any pool. This specified amount could be set at a statistically significant level for any transaction. However, we propose that the determination of any such levels be done with extensive market consultation and feedback.

IV. QRM Definition

The current proposed definition is unnecessarily narrow and we advocate a more moderate position guided by the intent of Congress. We do not believe that qualified residential mortgages ("QRMs") were intended by Congress to be default-proof. This observation is supported by the language of the Act, which states that regulators should take into consideration "underwriting and product features that historical loan performance

data indicate result in a *lower* risk of default" and requires that the standard be no broader than the definition for a qualified mortgage in Section 129C of the Truth in Lending Act, as amended by Section 1412 of the Act. This provides guidance for a significantly broader definition for QRMs than exists in the proposed rules and one that allows room for lower costs of credit to homebuyers. Such a definition would make credit more accessible to creditworthy borrowers and can co-exist with a robust non-QRM market.

Based on data as of April 2011 from the LoanPerformance loan-level database of non-agency mortgages (i.e., mortgages used to collateralize private label RMBS transactions), approximately 7% of the original balance of fully documented, owner occupied, non-agency first lien purchase loans with original combined LTVs of 80% originated in 2004 to borrowers in the U.S. excluding California, Florida, Arizona and Nevada with FICO scores between 680 and 720 have become 60+ days delinquent. For borrowers with the same characteristics but original combined LTVs of 85%, 90% and 95%, the cumulative delinquency/default rate as of April 2011 was 8%, 11% and 14.5%, respectively. Other comment letters have also noted evidence to support an adjustment to the proposed rules' high down payment and low LTV standards for QRMs.

In a comment letter to the proposed rules, Hon. Barney Frank and other members of Congress noted, "we are very concerned that the high 20% down payment requirement in the draft rule inappropriately excludes too many otherwise qualified homebuyers . . . there is evidence that a 20% [down payment] requirement does not result in sufficiently lower risk to justify the significantly enhanced hurdle to buying a home that this represents." While we believe that loans to borrowers with poor credit and lack of ability to repay loans should fall outside of the QRM definition, the QRM definition is too narrow as drafted and will raise the cost of borrowing for non-QRM mortgages to many homebuyers and make borrowing impossible for certain low income but creditworthy borrowers. We believe that the credit risk of a borrower should guide the interest rate charged, but the proposed rules would create additional upfront costs for borrowers that could put continued downward pressure on housing prices.

Title XIV of the Act directly imposes conditions on mortgage origination that impact issues risk retention cannot itself solve. While the provisions of Title XIV do not provide all necessary controls for sound lending, they target the residential mortgage loan origination practices of lenders. These rules should be considered when crafting the risk retention rules, in concert with the disclosure, representations and warranties, due diligence, conflicts of interest and other regulations flowing from the Act. Therefore, we believe that a marginally broader exemption for QRMs could be a very valuable tool for encouraging sound lending and a safer process.

As formulated, the QRM definition has very limited use and again gives a strong advantage to balance sheet banks because they have the ability to extend and more competitively bid on non-QRM loans and hold them on their books without tapping the capital markets to fund the loans through securitization. This hurts the ability of other

financial institutions to lend and constrains credit provision to borrowers. Where borrowers fall just outside of a single criterion while satisfying others, sponsors would be burdened by risk retention that may negatively impact the lending decision.

At present, GSE deal execution comprises over 90% of the mortgage origination market. With conforming mortgage limits still high and continued uncertainty in securitization regulation, the private label markets remain dormant. The White House and Congress have sent a clear message that the GSEs will be wound down and private capital is needed to fill the void that will be created. For that private capital to form, it must be able to do so in a stable and efficient manner.

The GSEs currently use representations and warranties as the primary method of enforcing strong underwriting standards with sellers. When crafted properly and held by the appropriate counterparty, a repurchase or replacement obligation is akin to 100% risk retention. If a loan fits within the QRM definition, it should carry with it repurchase obligations and will be protected by the many remaining reforms in regulations mandated by the Act. The representation and warranty, disclosure and conflicts of interest protections will not fall away by virtue of QRM status. Therefore, the QRM definition should be expanded to encompass mortgages made to borrowers with a meaningful down payment, good credit history and steady income sufficient to service their debt.

The regulations will have a more immediate impact on residential mortgage loan markets because they become effective one year after publication in the Federal Register, while the regulations for all other ABS become effective one year after the residential mortgage loan regulations. Legislators clearly intended that the mortgage markets be afforded strong protections on an accelerated schedule, likely due to a combination of a greater need to repair and revive this segment by introducing certainty to originators, sponsors and investors. Legislators also gave regulators the authority to create exemptions – these should be fully utilized to the extent they encourage prudent lending.

Many alternatives could be explored to make the QRM definition more aligned with the purpose of securitization reform and Congressional and White House intent. For example, seasoned loans made some time before securitization should be exempt from risk retention because the seasoning period will alleviate concerns around poor underwriting. Also, the DTI levers can be adjusted upward to allow loans to those with otherwise acceptable characteristics. The rules could employ a simple matrix that allows a less rigid box in which QRMs fit. In any event, we believe that Congress intended the QRM universe to be significantly broader than proposed and request that the regulators jointly reconsider the definition and revise the proposed parameters.

V. Resecuritizations

Resecuritizations serve a valuable role because investors can resolve inefficiencies in the markets by restructuring their investments in ABS. Through resecuritization, institutional investors are able to manage risks in securities that are assigned lower than expected ratings as a result of downgrades from their initial ratings level. The higher return classes of the resecuritization transaction can be sold to hedge funds and other investors with a greater appetite for risk and much lower restrictions in the capital they must hold against assets. Unlike CDOs, the assets of these transactions are not dynamic, or actively managed. The tranching of securities allows investors to participate in transactions with an appropriate amount of credit enhancement for senior classes of securities through the subordination of payment entitlements owing to junior classes of securities, despite the structure of the underlying securities.

More importantly, risk retention's goal is not achieved on legacy assets (ABS issued prior to the effectiveness of the final rules) or at the resecuritization transaction level. Legacy assets' underwriting standards at origination cannot be changed retroactively. Retention by the sponsor of a resecuritization will not impact the underwriting process for the origination of the securities that underlie the resecuritization. The draft rules construct a regime where risk is held at the asset level and the trust level, effectively *doubling* risk retention. Moreover, because the exemption provided in the proposed rules is too narrow, sponsors will likely be unable to execute resecuritizations of legacy ABS.

In addition to an exemption for securities that satisfy risk retention criteria that are issued after the effectiveness of the final rules, we submit that currently outstanding RMBS should be eligible for the exemption because the underwriting standards and incentives of market intermediaries cannot be altered. Any benefit otherwise achieved by risk retention would not materialize in this context. Finally, the exemption should allow for multiple classes of securities within a transaction through tranching for the reasons described above.

VI. Premium Capture Cash Reserve Account

While we believe the proposed risk retention rules will negatively and unnecessarily impact the cost of borrowing, the proposed premium capture cash reserve account will have altogether deleterious effects on otherwise efficient lending practices. It is worth noting that Congress did not in the Act mandate promulgation of rules for this account and we believe that this additive mechanism compromises the framework set by legislators. If the intent of requiring the premium capture cash reserve account was to take away funds that a sponsor could use to partially offset the cost to fund the retention piece, we do not believe it is appropriate.

If a sponsor can partially fund a retained slice through the monetization of excess spread by a sale of premium bonds, it would not thereby become indifferent to the quality of assets originated. In other words, the goal of risk retention – encouraging prudent lending and sound securitization structures – will have been attained regardless of how sponsors decide to fund their full 5% risk retention requirement. It is critical to recognize that certain financial institutions are required to incur capital charges for retained bonds. These capital charges increase if such retained bonds are downgraded. Also, as in any private business activity, sponsors expect to cover costs and receive some level of profit in order to undertake the process of organizing and initiating securitizations.

Further, the addition of a premium capture cash reserve account to the baseline hold amount is likely to compromise sale accounting treatment. Ownership by the sponsor of greater than 5% of the transaction as a result of the reserve account may trigger consolidation of the entire securitization trust on the balance sheet of the sponsor. The risk of consolidation will simply prohibit sponsors from engaging in the organization and initiation of securitizations. Whatever the intent of introducing the premium capture cash reserve account, the result is a strong disincentive for securitizers to sponsor securitization transactions.

In practice, this provision penalizes all participants by creating additional risk retention above the 5% level and deferring compensation in an uneconomical manner for a valuable business activity, rendering many securitizations impractical. Premium capture serves to replenish costs of completing securitization transactions and allow sponsoring firms to profit, which in turn encourages securitizers to sponsor future transactions. We believe securitization can continue to support sustainable credit formation if sponsors are properly motivated to source funding for borrowers in a manner that follows sound underwriting standards and accurately balances the likelihood of default and interest charged for lending.

Excess spread constitutes efficiency achieved in the process, allowing lenders to extend financing to borrowers on more attractive terms versus balance sheet lending. It represents the savings inherent in the process and lowers the cost of borrowing to consumers. Eliminating the monetization of excess spread will destroy a primary benefit of the process which could constrain the flow of private capital critical to mortgage lending and therefore result in lower levels of credit provision.

Conclusion

Through securitization, risk is sold to investors at an appropriate price, providing an important source of capital and supporting liquid markets for debt. For the process to work efficiently underwriting standards must be met and investors must receive the information required to evaluate the risk premium they will earn. During the credit crisis, underwriting standards loosened. Scrutiny of available information deteriorated and

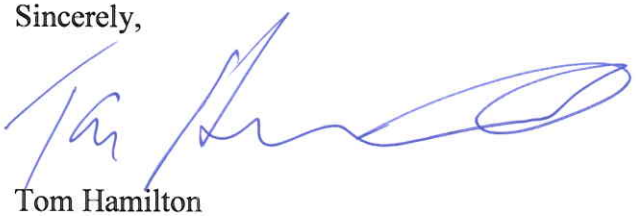
unforeseen events upended previously held assumptions. As large amounts of risk were held by sponsoring institutions prior to the crisis, it is unclear that rules mandating that additional risk be held by those institutions would better align incentives of the participants in the securitization process.

Increased credit provision is one of the key Congressional and White House priorities and is central to a continued economic recovery. At the same time, however, banks are required to de-risk, hold more capital against assets and under regulatory regimes such as that imposed by risk retention rules, to hold more assets. Holding assets with punitive risk weighting significantly reduces the ability of banks to lend, with potential knock-on impacts on the housing market and the broader economy. In order to allow the housing market to heal through the revitalization of securitization markets, careful implementation of risk retention must be achieved, complete with appropriate exemptions and exceptions.

The impending transition away from reliance on the GSEs for housing finance means that the final risk retention rules cannot jeopardize the overall legislative framework set by Congress to address investor protections in the securitization markets. The final risk retention rules should aim to both reduce the origination of risky, poorly underwritten loans and encourage credit extension to qualified borrowers. However, we believe strongly that holistic reform to securitization is the most effective means to remedy its past shortcomings and that other complementary reform to the securitization industry will drastically alter the overall process, making it significantly safer.

We appreciate the opportunity to provide input on this important process. Please feel free to contact me at (212) 412-1708 or tom.hamilton@barcap.com with any questions or follow up related to the content of this letter. Thank you for your consideration of our comments.

Sincerely,



Tom Hamilton
Managing Director, Head of Securitized Products Trading
Barclays Capital Inc.