



## RESPONSE TO: NOTICE OF PROPOSED RULEMAKING

Risk Based Capital Guidelines; Capital Adequacy Guidelines; Capital Maintenance; Regulatory Capital; Impact of Modifications to Generally Accepted Accounting Principles; Consolidation of Asset Backed Commercial Paper Programs; and Other Related Issues

**October 2009**

**Board of Governors of the Federal Reserve System  
Federal Deposit Insurance Corporation  
Office of the Comptroller of the Currency  
Office of Thrift Supervision**

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## Executive Summary

**The proposed rules, if put in place without modification, will have significant consequences to the Customer Conduit market which will have a ripple effect to the financing of corporations and ultimately consumers that have relied on this market for the past 26 years. Approximately \$371.8 B<sup>1</sup> is currently funded through customer centered multi-seller ABCP conduits (“Customer Conduits”).**

- Increasing regulatory capital by up to 10 times will significantly limit the availability of credit and/or increase pricing significantly for mid-corporate and large corporate customers who in turn in many cases provide financing to small and mid sized corporations and end consumers through credit cards, auto loans and leases, etc.
- U.S. banks will be at a very significant disadvantage to non-U.S. banks who calculate capital under the risk based Basel II rules and result in much lower capital requirements for this product versus the proposed rules. U.S. regulated banks will be unable to fully adjust pricing to compensate for this increased capital.

### Capital Should Equal Risk

- Customer Conduits have had a long proven track record of very low losses. In the more than 26 year history in this market, with nearly a trillion dollars financed, there have only been 25 basis points<sup>2</sup> of total cumulative losses. Regulatory capital held against these exposures has been well in excess of what has been needed, averaging more than 7 times coverage in the past three economically strained years.
- While we understand the U.S. Agencies’ desire to add capital to the banking system, it is imperative that this capital be appropriate for the risks inherent in the products so as not to create disincentives for safe, sound banking practices.

### This Should Not Be A One Size Fits All Rule

- Customer Conduits have been lumped in with other products with very different characteristics and different performance in the stressed economic environment.
- Customer Conduits can be clearly defined to avoid the expansion of the product into more risky exposures.

<sup>1</sup> Source: Moody’s, May 2009

<sup>2</sup> ASF Global Survey 9/09. Cumulative losses divided by cumulative originations.

## Executive Summary *(continued)*

**While additional regulatory capital is warranted for more risky banking products, it would seem completely inappropriate to impose 100% risk weighting against Customer Conduits given the extremely strong credit performance.**

**The ASF requests that the U.S. Agencies continue to provide an exemption for Customer Conduits consolidated on the balance sheet of the sponsoring bank which will allow for the continued use of current risk-based capital treatment on exposures until full implementation of Basel II - IAA.**

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## Definition of Customer Conduits

**ASF suggests a definition for Customer Conduits which would be allowed to continue under the current exclusion from consolidated assets and/or use the IAA to include all programs where:**

- All investments are individually negotiated by the Customer Conduit sponsor in order to provide financing to a customer of the sponsor.
- Explicit contractual liquidity facilities provided to the program in aggregate cover at least 100% of the outstanding ABCP.
- There is no requirement to sell investments funded in the Customer Conduit due to a decline in the market value of the investment.

### **Customer Conduits Are Not**

- CDOs
- Securities Arbitrage Vehicles
- SIVs/SIV Lites

See Appendix for detailed information on these structures. The structural features that these program types have do not meet the definition of Customer Conduits as detailed above.

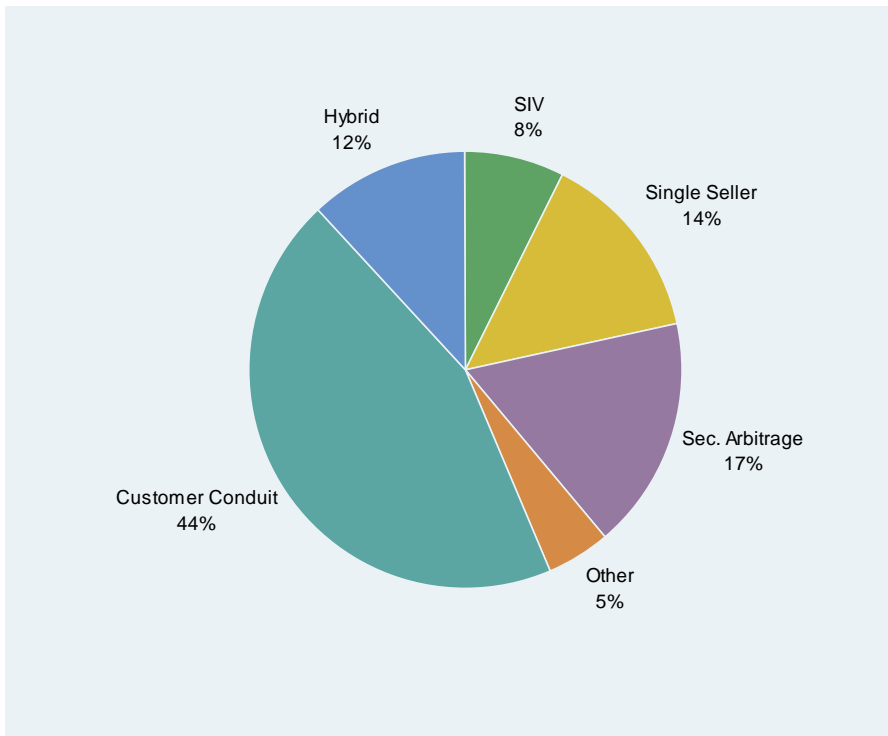
## Distinct Features of Customer Conduits

### **Customer Conduits and the transactions they fund have unique structural components that have resulted in unparalleled performance.**

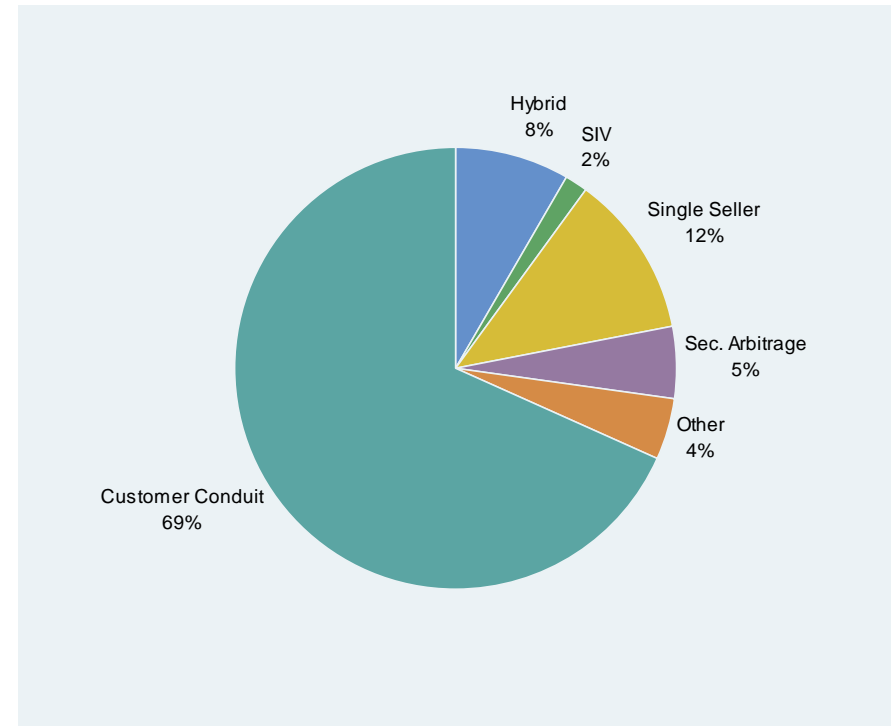
- The Customer Conduit business has full contractual liquidity supporting the ABCP issued.
- Regulatory capital held against support facilities has been more than sufficient to cover realized losses.
- Customer Conduit transactions allow for the active management of transactions in downside scenarios to strengthen structures.
- Tighter triggers on Customer Conduit transactions combined with the real threat of penalty pricing result in sellers being very willing to strengthen structures to avoid higher pricing.
- Dynamic credit enhancement structures for some transactions adjust the amount of credit enhancement within the transaction on an ongoing basis based on the actual performance of the transaction.
- The majority of transactions have 364 day tenor of liquidity which allows for a reassessment of transactions.

## In Addition to Customer Conduits, the ABCP Market is Comprised of the Following Conduit Types

Global ABCP Outstandings by Program Type  
4Q 2006



Global ABCP Outstandings by Program Type  
2Q 2009



Source: Moody's Global Market Update, June 18, 2009  
Note: ABS CDOs are in the "Other" Category.

- The importance of bank sponsored Customer Conduits for the financing of consumer and commercial assets has increased over the past 3 years as many non-bank sponsored vehicles have exited the market.
- Conduits without 100% liquidity support have wound down or are in the process of winding down.



## Customer Conduits Finance Traditional Asset Classes

- While there has been a substantial contraction in the overall ABCP market (total ABCP has reduced from a peak of \$1.0 trillion in August 2007 to 579.7 billion as of May 2009), Customer Conduits remain a key source of financing in the market.
- The table below evidences the significant contraction in the financing of various traditional asset classes that are funded in the overall ABCP market and specifically in Customer Conduits.

Asset Type Diversification (\$ Billions)	Total ABCP Market Peak August 2007	Customer Conduits		
		Total Customer Conduit Peak August 2007	May 2009 Customer Conduit O/S	Percent Change
Auto Loans and Leases	102.8	84.5	75.7	(10)%
Commercial Loans and Leases	86.2	68.4	55.6	(19)%
Trade Receivables	91.2	77.4	55.1	(29)%
Credit Cards	83.9	69	44.1	(36)%
Student Loans	44.5	36.6	36.4	(1)%
Other	53.8	44.2	26.3	(40)%
Mortgage Loans/HELOC's	49.1	40.3	21.2	(47)%
Equipment Leases and Loans	20.7	17.0	20.0	18%
Floorplan Financed	12.2	10.0	11.2	12%
CBO&CLO	29.2	23.3	9.6	(59)%
Consumer Loans	22.7	18.7	9.0	(52)%
Government Guaranteed Loans	8.3	6.8	7.5	10%
Securities	397.9	NA	NA	NA
<b>Total</b>	<b>1,002.60</b>	<b>496.4</b>	<b>371.8</b>	<b>(25)%</b>

Source: Moody's ABCP Query and the Federal Reserve website. Data for Customer Conduits includes multi-seller and hybrid vehicles but excludes any portion of such vehicles used to fund securities.

## Customer Conduits Fund Customers Across A Broad Range of Industries

(\$ Billions) Industry	May 2009 Customer Conduit O/S
Consumer Finance	91.0
Automotive Finance	84.1
Commercial Finance	64.5
Other	29.0
Mortgage Finance	26.4
Equipment Financing	16.9
Oil, Gas, and Energy	7.1
Aerospace and Defense	7.0
Electronics	5.1
Banking	4.8
Finance	4.6
Mining and Metals	4.6
Manufacturing	4.5
Telecommunications	4.4
Automobile	4.4
Utilities	3.9
Chemicals, Plastics, and Rubber	3.3
Leisure and Entertainment	3.1
Farming and Agriculture	3.1
Total	371.8

Source: Moody's ABCP Query and the Federal Reserve as of May 2009

- **We would anticipate significant additional contraction and/or significantly higher financing costs to the corporations who access this market if assets within U.S. Customer Conduits attract 100% RWA.**

# Description of Risk Positions in a Multi-Seller ABCP Structure

## Transaction Liquidity

- Typically provided by the sponsor of the conduit.
- There is a separate liquidity facility for each transaction sized at least equal to 100% of the ABCP used to fund the transaction.
- Most liquidity facilities are structured to have a maturity of 364 days from issuance.
- Typically structured as an asset purchase agreement although may also be structured as a loan agreement.
- Only at risk for the transaction to which it is specifically assigned.
- Has attracted risk based capital beginning in 2004.

## Programwide Credit Enhancement

- Typically provided by the sponsor of the conduit.
- At risk for all of the assets in the conduit.
- Subordinate to CP, Programwide Liquidity, and typically transaction specific liquidity.
- Has attracted minimum 100% RWA since it was first created.

## Programwide Liquidity

- Typically provided by the sponsor of the conduit.
- At risk for all of the assets in the conduit.
- Typically used to repay CP during a temporary market disruption.
- Duplicative to the transaction specific liquidity. Netted for purposes of calculating regulatory capital.

## Customer Conduits Have Explicit Contractual Support

### **Customer Conduits have at least 100% explicit contractual support in the form of liquidity**

- In addition, Customer Conduits have contractual programwide credit enhancement facilities.
- These support facilities have risk based capital pursuant to the current general risk-based capital rules.
- Even during the most stressed times in our market, support provided to Customer Conduits was contractual and explicit.

## How Have Customer Conduits Performed?

- Customer Conduit transactions are structured using well developed and tested criteria to an investment grade standard.
- The conduit sponsors' direct relationships with the sellers of receivables, the short-term maturity of the liquidity facilities and the tighter triggers on Customer Conduit transactions relative to their term market equivalents have provided an ability to strengthen structures as performance issues develop.
- This ability has significantly improved the performance of transactions funded in Customer Conduits during the recent market crisis.
- As transactions have come up for renewal of the liquidity facility or have hit performance triggers within the structure of the transactions, structures have been tightened and improved to better protect the conduit (and all relevant risk position takers). For example,
  - Material additional credit enhancement was often provided by sellers of the receivables to transactions.
  - “Stronger” forms of credit enhancement have been substituted for “weaker” forms (e.g., over-collateralization instead of excess spread).
  - Trigger levels have been further tightened.
  - Certain transactions were liquidated.
- In addition, the significant diversification of underlying assets funded within Customer Conduits resulted in overall risk reduction.

**The outstanding performance over the past 3 years was based on the tools and structures already in place.**

## Summary Comparison of Structures

	Customer Conduit	Cashflow ABS CDO	SIV	SIV-lite	Securities Arbitrage
<b>Assets Funded: Individually Negotiated Customer Transactions/Publicly Traded Securities</b>	<b>Individually Negotiated Customer Transactions</b>	Publicly Traded Securities	Publicly Traded Securities	Publicly Traded Securities	Publicly Traded Securities
<b>Primary Business Purpose</b>	<b>Customer Financing</b>	Arbitrage	Arbitrage	Arbitrage	Arbitrage
<b>Ability to Strengthen Structure in Underlying Transactions</b>	<b>Yes</b>	No	No	No	No
<b>Market Value Triggers Forcing Liquidation</b>	<b>No</b>	No	Yes	Yes	No
<b>Full Committed Liquidity</b>	<b>Yes</b>	Yes	No	No	Yes
<b>Seniority of Underlying Transactions</b>	<b>Typically senior</b>	High Grade and Mezzanine ABS	Typically senior ABS and mezzanine bank paper	Typically senior RMBS	Typically senior ABS
<b>Diversified Underlying Asset Base</b>	<b>Yes</b>	No – almost entirely mortgage	Typically yes - also significant (approx. 20% concentration in mezzanine bank paper)	No – almost entirely mortgage	To a lesser degree than multi-seller ABCP (large concentrations in RMBS, CMBS and CDOs)
<b>Pricing Basis</b>	<b>Pass Through Actual Cost of Funds</b>	LIBOR index based	LIBOR index based	LIBOR index based	LIBOR index based
<b>Business Model</b>	<b>Ongoing Business</b>	Wind down	Wind down	Wind down	Wind down
<b>Performance During Recent Market Crisis</b>	<b>Strong</b>	Poor due to asset performance	Poor performance due to RMBS, CDO and monoline issues as well as MTM triggers forcing liquidations and liquidity issues	Poor due to asset performance, MTM triggers forcing liquidations and liquidity issues	Significant deterioration in the underlying securities resulted in increased risk to sponsoring banks

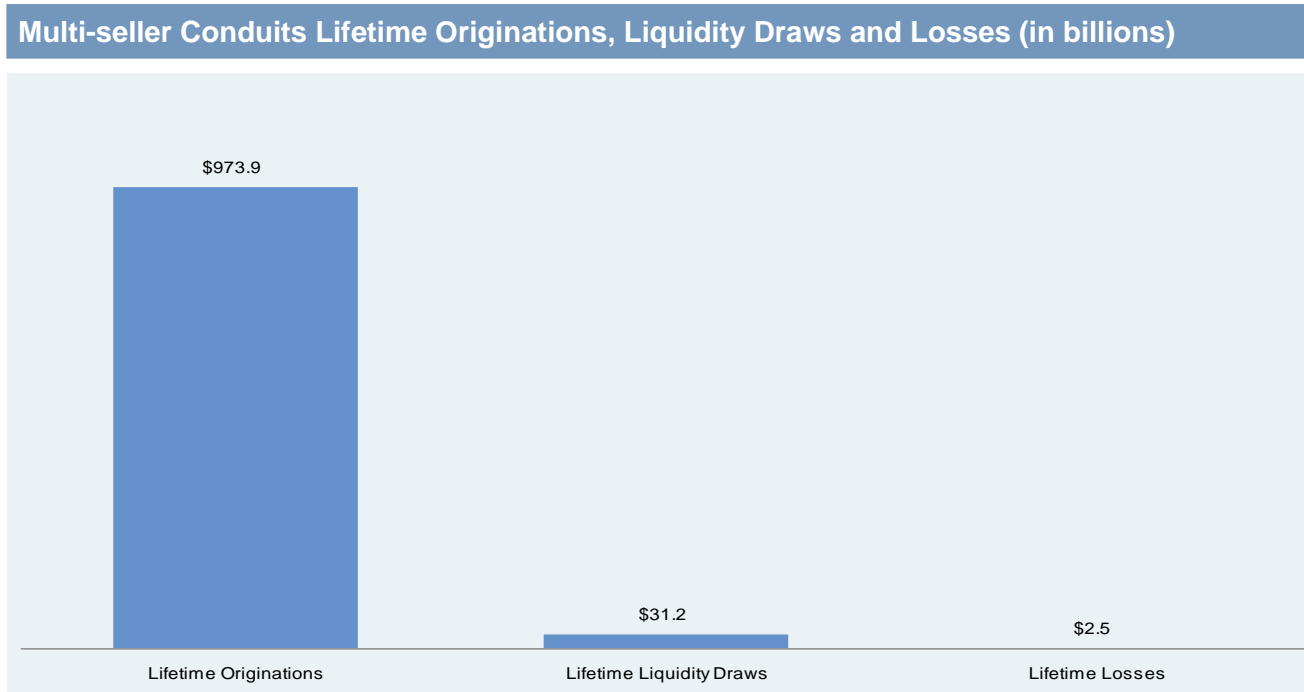
Note: Hybrid conduits (referenced on page 7) are typically a combination of customer conduit and securities arbitrage conduits.

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# Multi-Seller Conduit Performance Information

CUSTOMER CONDUITS ARE A VERY LOW RISK PRODUCT



Source: ASF Industry Survey, 09/09. Data collected from a survey of 10 U.S. and international ABCP conduit sponsors.

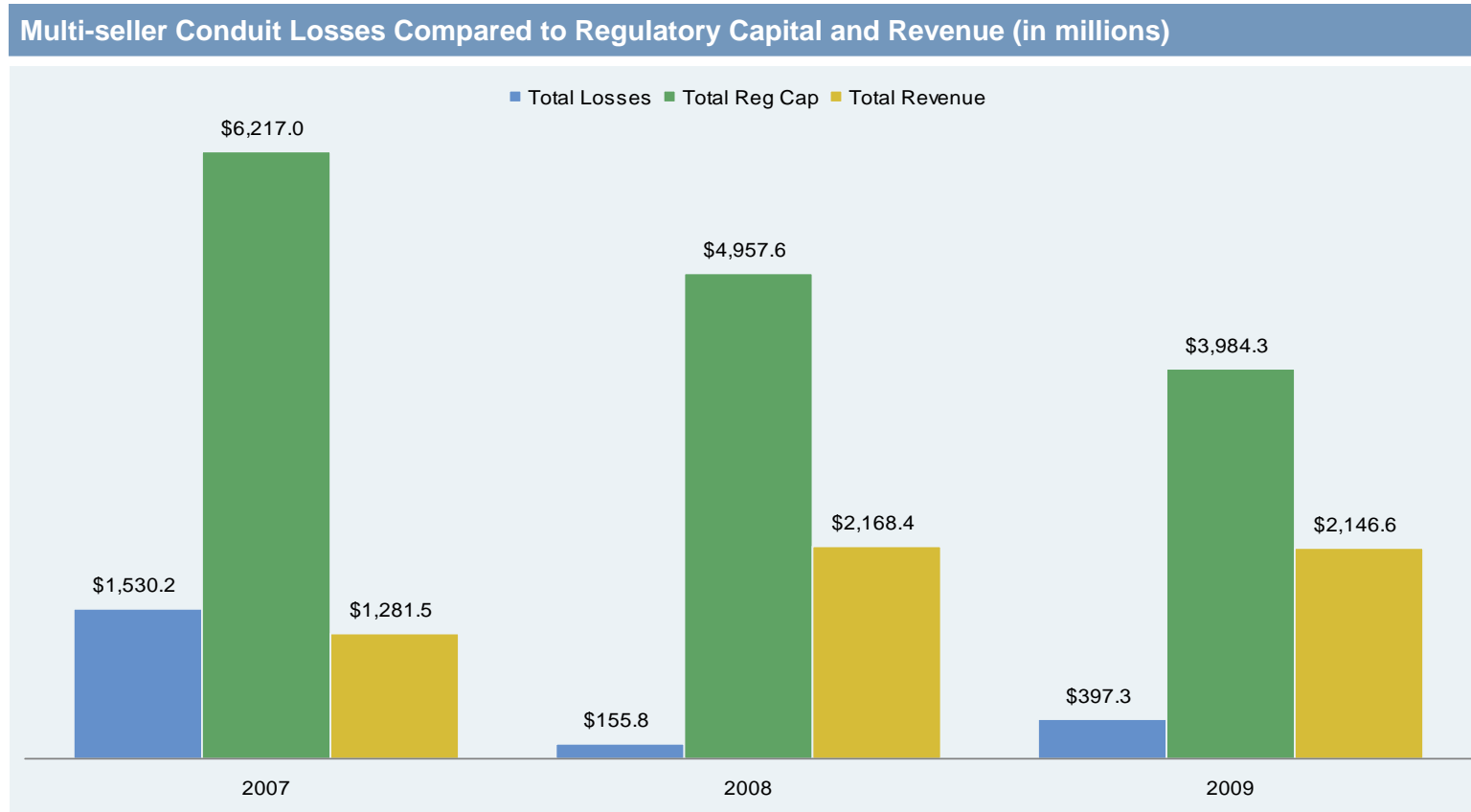
- Lifetime Losses can be further classified as Core (Customer related) and Total Losses (including CDOs and Securities Arbitrage) as follows<sup>1</sup>:
  - Core Losses 8 bps
  - Total Losses (including Non-Core) 25 bps
- In the over 26 year history of this market, multi-seller ABCP conduits, occasionally funded non-core assets, such as CDOs and publicly traded securities. The definition of Customer Conduit proposed here would preclude such inclusions in the future.

<sup>1</sup> Calculated as a percent of lifetime originations.



# Multi-Seller Conduit Loss Experience

CUSTOMER CONDUITS ARE A VERY LOW RISK PRODUCT



Source: ASF Industry Survey, 09/09. Data collected from a survey of 10 U.S. and international ABCP conduit sponsors.

- Regulatory capital held is well in excess of what is needed for this business.
- In the past three years (a stressed economic environment), regulatory capital has averaged more than 7 times the amount of losses for the Customer Conduit business on a global scale.
- Cumulative net losses prior to 2007 were less than \$400MM industry-wide.
- In addition, current year's revenue in most years more than completely offsets losses and even in the most stressed period nearly equaled the loss amounts.

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## Expected Impact on Corporate Lending

### **Proposed Rule may result in Banks reducing capacity for this product and/or increasing prices.**

- Most banks (if not all) are more focused on capital allocation measurements given requirements to increase capital. Return on risk based capital is a key metric.
- Faced with higher risk based capital combined with an inability to price for this increased capital, banks may reduce the amount of Customer Conduit financing they do.
- This will result in reduced capacity for borrowing for large and mid-corporate customers.
- Many of these customers finance small and mid sized corporations as well as consumer assets such as credit cards, auto loans and leases (see chart on page 7 for spectrum of assets financed).
- In addition, the increase in risk based capital could result in significantly higher costs associated with such funding for customers who still have access.
- Non-U.S. banks likely will not be able to fully absorb the gap in funding due in part to new leverage ratio issues facing the European banks.

### **Proposed Rule creates negative incentive for risk taking**

- The proposal creates disincentives from a risk perspective. Banks will be incented to take on riskier assets for more yield. If “risk based” capital is the same for a “AAA” conduit position and a loan to a “BB” company, but the loan attracts higher pricing, the bias will be to the BB loan (contrary to Basel II).

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# Competitive Inequity

U.S. Regulated Banks			Non U.S. Regulated Banks
Current RWA <sup>1</sup>	Proposed RWA (1/1/2010)	Basel II RWA <sup>2</sup> (+3 years)	Basel II RWA (Current)
10%	100%	7-20%	7-20%

<sup>1</sup> For some assets, RWA may be higher.

<sup>2</sup> RWA dependent on rating of the transaction (7-20% reflective of typical assets funded in Customer Conduits AAA to A risk).

**Non-U.S. Regulated Banks have already adopted Basel II and would have a significant regulatory competitive advantage.**

- Under Basel II, there is no difference between on and off balance sheet conduits and under the IAA, banks would hold much less capital than U.S. regulated banks would be required to hold for the same risk.
- Global competition would make it impossible for U.S. regulated banks to price for this increase in risk based capital.

## ABCP Conduit Administrators (O/S Greater than \$2.5 billion)

2 <sup>nd</sup> Quarter 2009 Average CP O/S (in \$ billions) <sup>1</sup>			
Administrator	Avg CP O/S	Administrator	Avg CP O/S
Citibank, N.A.	66,852	HBOS Treasury Services plc	7,498
Royal Bank of Scotland PLC	60,104	Credit Suisse	7,175
Bank of America, N.A.	43,801	Bank of Montreal (London Branch)	6,489
The Liberty Hampshire Company, LLC	32,811	AIG Financial Products Corp.	6,366
JPMorgan Chase Bank	32,256	Royal Bank of Canada, Canada	6,056
Bank of Tokyo-Mitsubishi UFJ	31,332	Sumitomo Mitsui Banking Corp.	5,915
Deutsche Bank AG	31,135	BMO Capital Markets	5,359
HSBC Bank PLC (London)	26,310	HSBC Bank PLC (U.S.)	5,140
Rabobank Nederland	22,218	Canadian Imperial Bank of Commerce	5,084
State Street Global Markets LLC	20,387	SG Hambros Bank & Trust (Channel Islands) Limited	4,732
Hudson Castle Group Inc.	19,687	Bank of Nova Scotia	4,601
Barclays Bank PLC	18,357	Dresdner Bank AG	4,454
Royal Bank of Canada, New York Branch	17,088	Bayerische Landesbank	4,273
Calyon	16,911	PNC Bank, N.A.	4,133
QSR Management Limited	16,906	ING Bank N.V.	3,873
Lloyds TSB Bank PLC	15,441	Ixis Financial Products	3,667
Société Générale	14,950	Société Générale Australia Limited	3,453
BNP Paribas	14,093	Lord Securities Corporation	3,311
Fortis Bank S.A./N.V.	12,964	General Electric Capital Corp.	3,188
The Bank of New York Mellon/BMO Capital Markets	12,240	Bank of New York Mellon <sup>2</sup>	3,035
WestLB AG	11,317	Bayerische Hypo-und Vereinsbank AG	2,927
Bank of Montreal / BMO Nesbitt Burns Inc.	10,350	Norddeutsche Landesbank Girozentrale	2,856
TD Securities Inc.	10,063	Sun Trust Equitable Securities	2,761
Ford Motor Credit Company	9,230	Banca Intesa S.p.A.	2,687
Wachovia Bank, N.A.	9,036	MBIA Asset Management UK Limited	2,500

Source: Moody's 3<sup>rd</sup> Quarter 2009 Program Index (reports 2<sup>nd</sup> quarter data)

<sup>1</sup> Note that U.S. regulated banks (the only banks affected by the NPR) are highlighted.

<sup>2</sup> Bank of New York acts as a third party administrator for conduits sponsors and does not necessarily provide liquidity to the entities, therefore they would not be consolidating nor subject to these rules.

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# Conclusion

## **Customer Conduits are a Key Financing Source for the Economy**

- Customer Conduits are an important financing component for the overall economy currently providing over \$371.8 billion of financing.
- At its current and originally adopted Basel II risk based capital levels, this provides banks a cost efficient, much needed financing for consumer and commercial assets.

## **Customer Conduits Has Proven Strong Performance in an Extremely Stressed Economic Environment**

- Performance of Customer Conduits has remained strong despite the severe economic downturn experienced over the past several years – Cumulative Losses on Core Business of 8 bps and Total Business (including Non Core) of 25 bps.
- Keys to this strong performance experience have been:
  - The ability to strengthen structures as problems occur – a feature unique to Customer Conduit facilities.
  - The absence of any triggers forcing the sale of transactions due to a change in the market value of the assets.
- Capital Associated with Customer Conduits Risk Positions is appropriate under the current rules and Basel II rules.

## **Risks in Customer Conduits are Clearly Differentiated from Other Structured Programs Which Do Not Have These Risk Mitigating Characteristics**

- These significantly different structures led to the materially worse performance relative to Customer Conduits during the recent market stresses.

**Therefore, ASF believes that while additional regulatory capital is warranted for more risky banking products, it would seem completely inappropriate to impose 100% risk weighting against Customer Conduits given the extremely strong credit performance. Capital associated with Customer Conduits is appropriate as currently calculated and under Basel II rules.**



## Conclusion *(continued)*

“The agencies initially implemented these provisions in the general risk-based capital rules in 2004 in response to changes in GAAP that required consolidation of certain ABCP conduits by sponsors. The provisions were driven largely by the agencies’ belief at the time that banking organizations sponsoring ABCP conduits generally faced limited risk exposures to ABCP programs, because these exposures generally were confined to the credit enhancements and liquidity facility arrangements banking organizations provided to these programs.

Additionally, the agencies believed previously that operational controls and structural provisions, as well as overcollateralization or other credit enhancements provided by the companies that sell assets into ABCP programs, could further mitigate the risk to which sponsoring banking organizations were exposed.”<sup>1</sup>

**The basic performance assumptions with respect to Customer Conduits continue to be valid.**

<sup>1</sup> Federal Register, Vol. 74, p 47143 (September 15, 2009): Risk Based Capital Guidelines; Capital Adequacy Guidelines; Capital Maintenance; Impact of Modifications to Generally Accepted Accounting Principles; Consolidation of Asset-Backed Commercial Paper Programs; and Other Related Issues.

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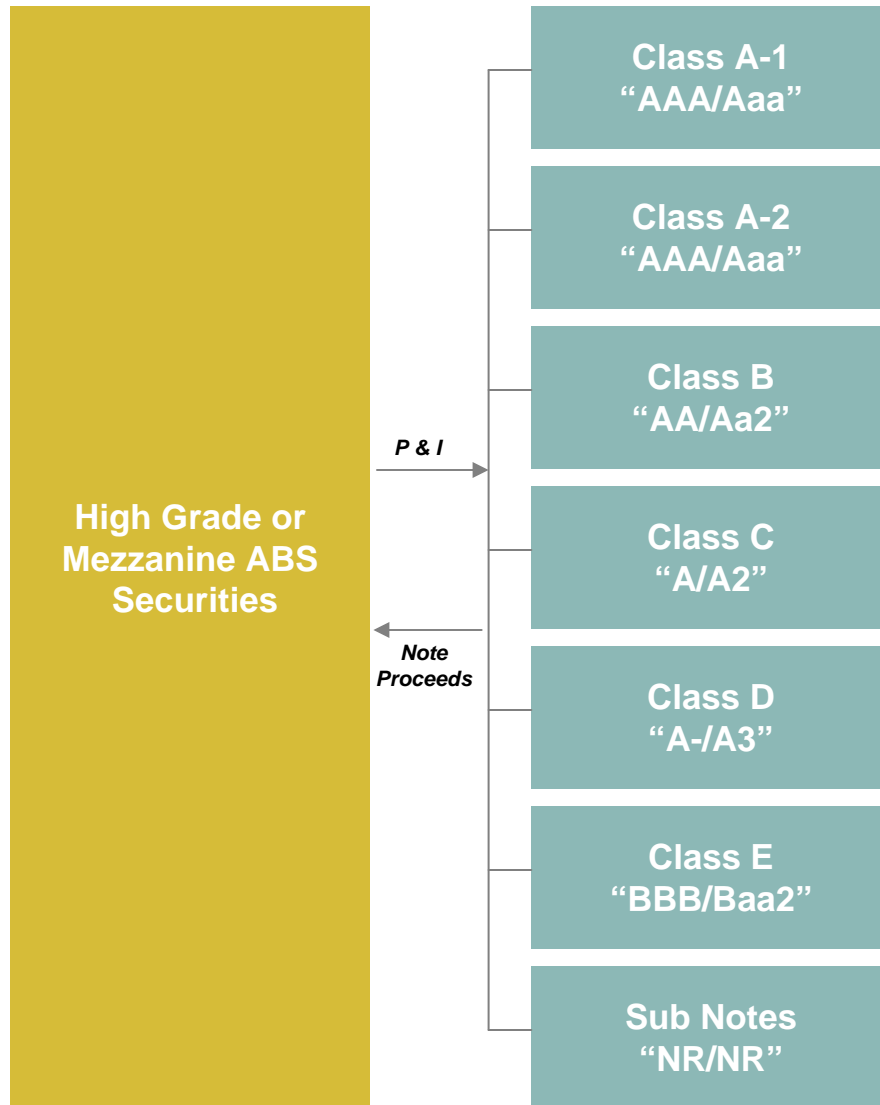
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## History of the ABCP Business

- Asset-backed Commercial Paper has been an important funding source for bank clients since its inception 26 years ago.
- The overall ABCP market began with the financing of trade receivables through the issuance of ABCP fully guaranteed by the sponsoring bank
- These vehicles were initially established as a balance sheet neutral way to offer financing to clients of the sponsoring bank on an unfunded basis with attractive regulatory capital treatment
- The market evolved to finance a variety of asset classes in addition to trade receivables including auto loans, credit card receivables and equipment leases
- Beginning in 1989, SIVs were introduced as an efficient method of securities arbitrage. These structures did not include full contractual liquidity support and instead had tests tied to the ongoing market value of the underlying securities
- Beginning in 1992, the liquidity behind the traditional multi-seller ABCP evolved to a partially supported<sup>1</sup> structure allowing for what is now 10% RWA for eligible liquidity exposure with a tenor of 364 days
- The market continued to develop and grow and, beginning in 2005, ABCP was used to fund a much broader array of asset classes most notably:
  - Senior and super senior CDO tranches
  - Repo facilities, and
  - Mortgage extendable commercial paper facilities through structures that relied on the ability to quickly liquidate what had been liquid instruments to repay maturing liabilities
- As the investor universe became uncomfortable with the risks associated with these newer structures and the more established SIV structures due to their market value risk, the forced liquidation of a large number of securities resulted in investor losses which were unprecedented for this industry

<sup>1</sup> In a fully supported program, the liquidity facility is obligated to fund regardless of the performance of the underlying assets. In a partially supported program, the liquidity facility does not fund “defaulted” assets

# Cashflow ABS CDO Structure and Risks

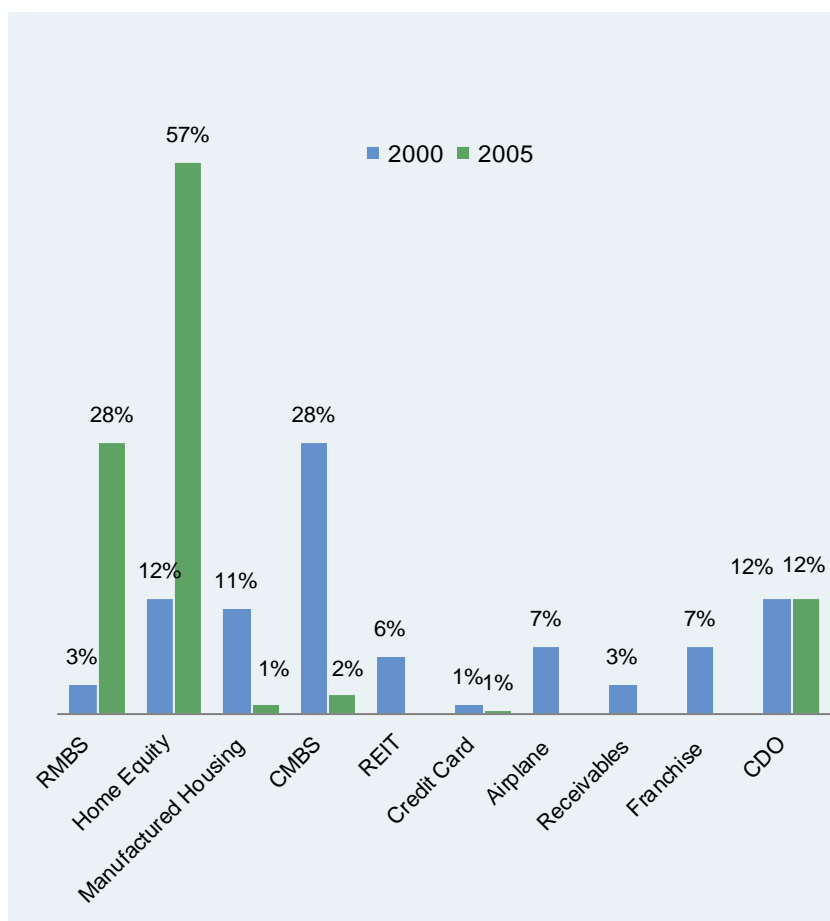


## Assets

- Publicly traded, high grade and mezzanine tranches of ABS.
- Heavily weighted towards mortgage related assets.
- Increasingly over time, these ABS tranches were backed by subprime mortgages.
- As the assets in the CDO are public securities, the portfolio manager of the CDO has no control over the underlying structures of the securities and would be unable to restructure or improve upon a problem situation in the underlying transactions funded in the CDO.
- There is no ability to improve upon the risk position in the CDO other than limited trading which may allow a portfolio manager to sell out of a higher risk security (at a loss) and buy a less risky security.

# ABS CDOs: Asset Mix - 2000 versus 2005

Top Sector Concentrations in SF CDOs



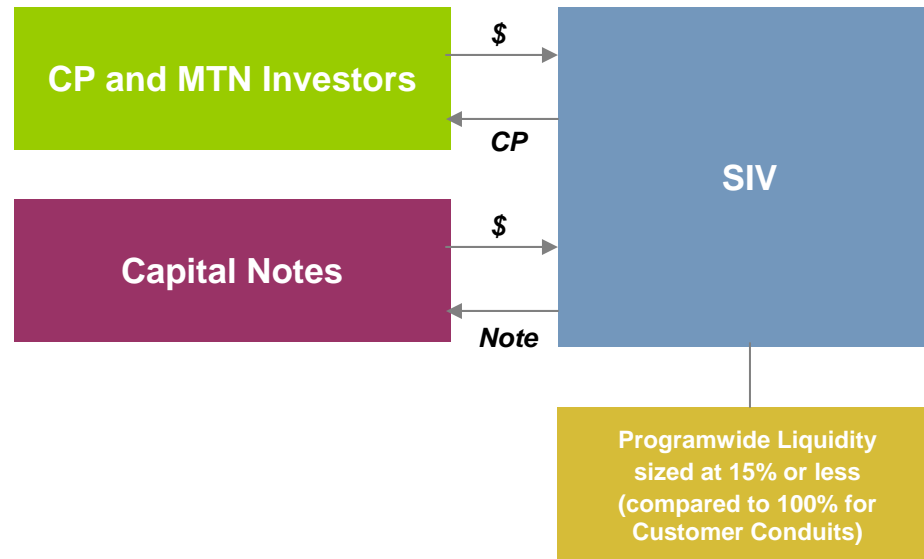
Source: "Credit Risk in Structured Finance CDOs", 2006, JPMorgan

- Diversity in the asset classes comprising CDOs decreased drastically from 2000 to 2005.
- During the same time period, the concentration of mortgage related assets in SF CDOs increased significantly.
- By 2005, the asset mix for ABS CDOs had moved to 88% mortgage related product and 12% CDO product (the majority of which was also backed by mortgage collateral).
- This trend towards mortgage collateral with concentrations in subprime and Alt-A collateral continued well into 2007.

## How have ABS CDOs performed throughout this market crisis? What went wrong?

- Cashflow ABS CDOs experienced significant problems due to their over concentration to mortgage (much of it subprime) collateral.
- As the assets within the mezzanine ABS CDOs were primarily comprised of thin, mezzanine tranches in RMBS, rising defaults in the underlying obligors on these mortgages had a dramatic impact on the cashflows (or lack thereof) on these tranches.
- As the defaults on the mortgages continued to rise, the collateral backing these ABS CDOs became worthless.
- Unlike with multi-seller ABCP facilities, these portfolio managers were largely “stuck” as they were unable to restructure the underlying transactions and improve their risk positions.
- The only potential method available to them to resolve the declining value of their assets would have been to sell the collateral and reinvest. This quickly became problematic as the market value of these RMBS tranches was deeply distressed as well.
- In addition, many of these ABS CDOs were structured in synthetic form. These involved the use of a counterparty to take on the risk in the underlying tranches of the RMBS.
- Problems with some of these counterparties further added to the problems in some of these transactions.

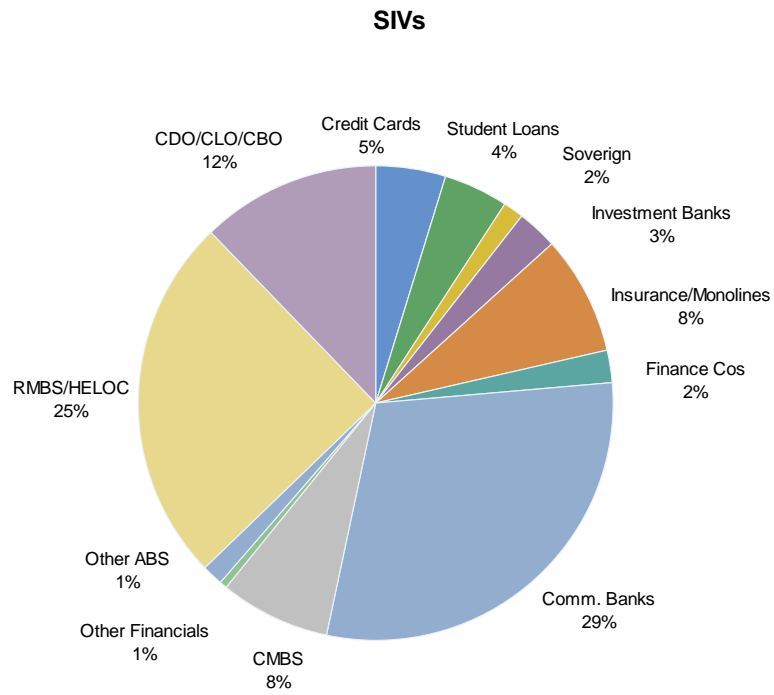
## SIV Structure and Risks



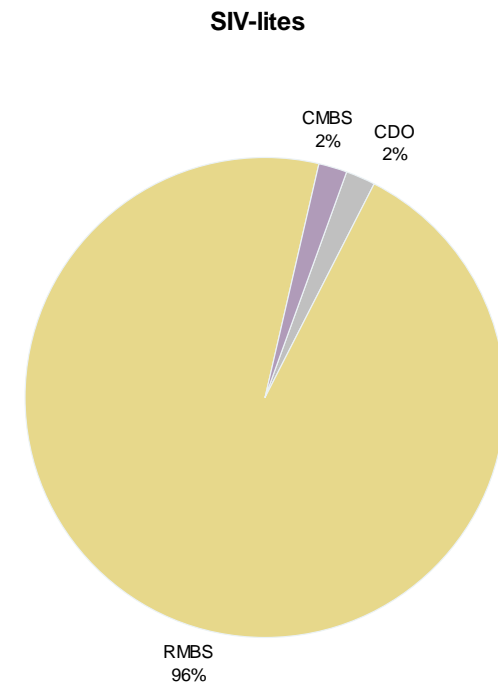
### Assets

- Pre-2004, SIV portfolios were mainly diversified portfolios of consumer and commercial securities.
- Post-2004, SIV portfolios became concentrated in securities backed by mortgages.
- The securities held in the SIV are publicly traded, typically senior tranches of ABS and mezzanine bank debt. The portfolio manager of the SIV has no control over the underlying structures of the securities and no ability to improve upon the structure or performance of the underlying securities if performance was not as expected.

# SIVs: Asset Mix



Source: Moody's, January 2008



Source: Moody's, July 2007



## How have SIVs performed throughout this market crisis? What went wrong?

- SIV and SIV-lite structures were built (unlike Customer Conduits) with reliance on the market value of the underlying collateral.
- These structures included an ongoing net asset value (“NAV”) test that when failed, required the portfolio manager to take actions to resolve the failure – this translated into the forced sale of the underlying collateral.
- As previously indicated, by 2007, much of the underlying collateral backing (in particular the SIV-lite structures) was mortgage related collateral where performance and the mark to market were severely negatively impacted during this time.
- The negative impact on the SIV collateral was to a certain extent circular as the forced sales of what ended up being significant portfolios of assets further distressed the mark to market on the remaining book of assets thereby forcing further liquidations.
- In addition, large scale downgrades in the securities held by the SIV resulted in a freezing of the market for ABCP issued by SIVs. The failure to re-issue the liabilities (ABCP and MTNs) required the portfolio managers to take action to raise proceeds from the structure to pay off the maturing liabilities.
- Any available liquidity (that unlike Customer Conduits was not sized to 100% of the liabilities) in the structure was drawn to repay liabilities.
- When the liquidity facilities were fully utilized and there was still a need for more proceeds to pay off maturing liabilities, a forced liquidation of the assets into a distressed market resulted in further losses.

# Securities Arbitrage ABCP Conduit Structure and Asset Description

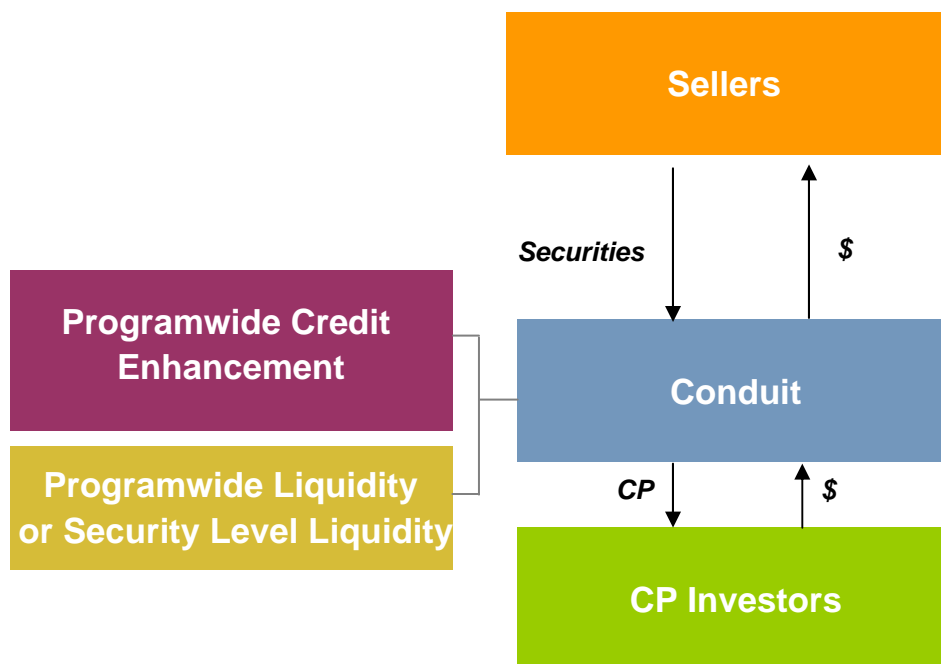
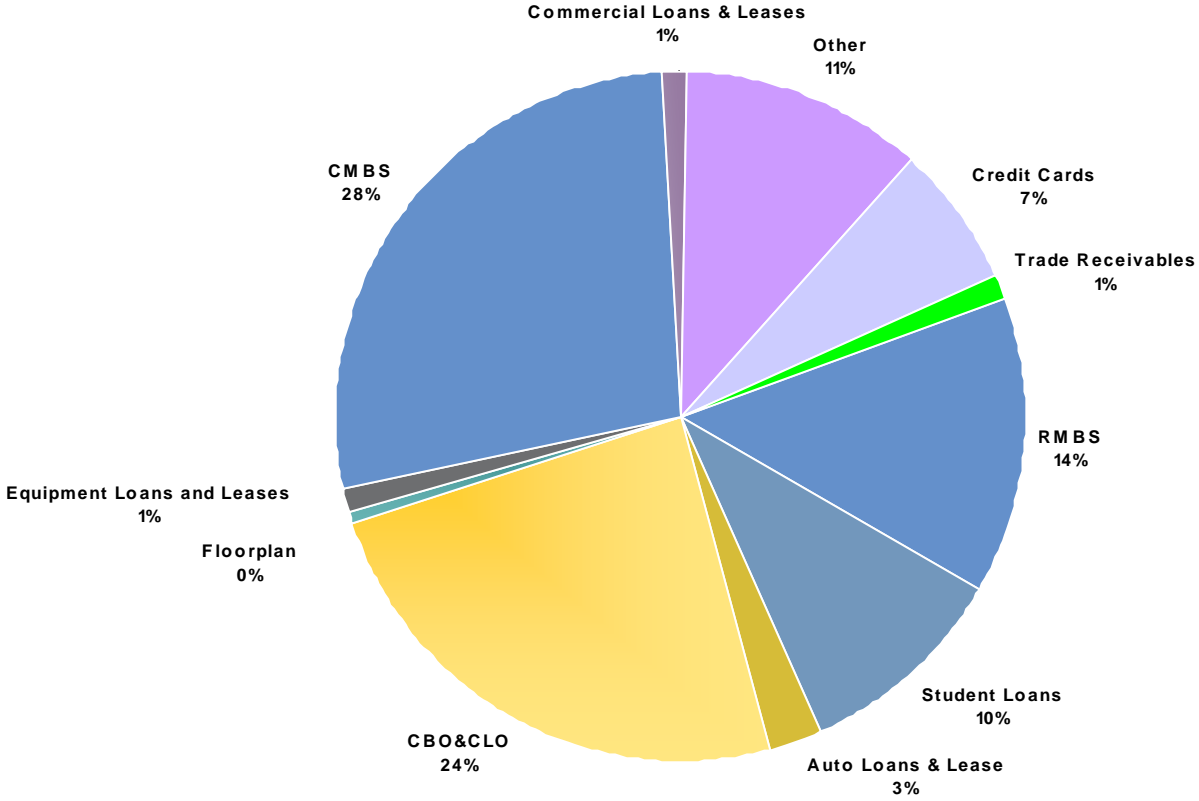


Diagram illustrates structural features commonly found in securities arbitrage ABCP conduits. Individual conduits will have slight differences in structure; however the general principles will remain (no market value triggers, purchase of senior, rated securities, etc.).

## Assets Funded

- Portfolio of senior, publicly traded securities.
- Major asset classes funded include CMBS, RMBS and CDOs.
- There is 100% liquidity support for the ABCP issued.
- Liquidity now unconditional industry-wide.
- There are no market value triggers requiring sale of conduit funded securities.

# Asset Mix: U.S. Securities Program



Source: Moody's, "ABCP 2008 Year in Review and 2009 Outlook", February 2009

