HOUSING POLICY COUNCIL
THE FINANCIAL SERVICES ROUNDTABLE

1001 PENNSYLVANIA AVENUE, N.W.
SUITE 500 SOUTH
WASHINGTON, D.C. 20004
Tel. 202.289.4322
Fax 202.628.2569

June 30, 2010

Robert Feldman
Executive Secretary
Attn: Comments
Federal Deposit Insurance Corporation
550 17th St. N.W.
Washington, D.C. 20429

Re: RIN-3064 – AD53

Dear Secretary Feldman

The Financial Services Roundtable and its Housing Policy Council ("the Roundtable") welcome the opportunity to comment on the Notice of Proposed Rulemaking regarding the treatment by the Federal Deposit Insurance Corporation ("FDIC" or "Corporation"), as receiver of an insured depository institution, of financial assets transferred by the institution in connection with a securitization or participation ("the Proposed Rule"). This notice follows the Advanced Notice of Proposed Rulemaking on the same subject to which the Roundtable earlier responded.

In our response to the Advance Notice of Proposed Rulemaking, we raised a number of policy issues among our comments and believe they remain important and worthy of consideration by the Corporation. We welcome the consideration that the Corporation has given to our comments and would like to have those comments, which at this point have not changed the Proposed Rule, to be incorporated by reference and to be reviewed again by the Corporation.

We believe that the Corporation would benefit from further consideration of the policies inherent in the Proposed Rule in light of the current changing environment in Congress and sister agencies. There is no need to rush to a final regulation; delaying adoption of a final regulation until the environment becomes more fixed and certain will not cause undue stress to the Deposit Insurance Fund, and such a delay will lead to a better rule. The regulatory reform legislation, including its risk retention provisions, will likely be signed into law prior to or shortly after the closing of the comment period on the Proposed Rule, and the SEC will have its final rules in a reasonable period of time following that.

We would also like to emphasize that the transition period for institutions to incorporate the regulations that the Corporation might adopt will be in addition to a very large number of transition periods related to intensely complicated regulations that will follow from the regulatory reform bill. The Proposed Rule will be yet another imperative for retooling systems at

insured depository institutions, but will be only one of dozens that will be imposed upon the institutions during the next few years.

We urge that the FDIC take that environment into account and provide a transition period of two years or, at a minimum, concurrent with the transition period provided by the new legislation's transition period for implementing regulations related to its risk retention period. Integrating new and complicated rules into systems takes considerable time and the efforts of many individuals who will also be called upon at the same time to integrate the additional regulations to be promulgated.

I. Harmonize the Proposed Rule with new legislation and the rules of other agencies.

We believe that consistency among the government agencies on rules as significant as risk retention in securitizations is crucial. While the Corporation, the SEC and other agencies, including the soon to be created Consumer Financial Protection Bureau, have been (or will be) given individual charters and the responsibility to operate consistent with those charters, we urge you and your fellow agencies to create rules that are not inconsistent with each other. In particular, we urge the agencies to look to Congress for guidance on the rules that should be followed, even those cases in which Congress addresses a question in the context of a statute that does not govern the specific agency actions.

For example, we applaud the effort by the Corporation to coordinate its disclosure rules with those of the SEC. We believe that is a positive effort toward uniform national standards. However, because Reg AB is massive and its disclosure provisions cover more than is necessary for the implementation of the Proposed Rule, we urge the FDIC to strictly limit its requirement to comply with the disclosure provisions of Reg AB to only those provisions in Reg AB that the FDIC expressly states are necessary for its purposes as opposed to incorporation all of the disclosure requirements of Reg AB in their entirety. In addition, we believe that there remain a number of inconsistencies between the two sets of rules, and we urge the Corporation to address those inconsistencies. For example, the Proposed Rule requires sponsors to hold the risk, while the SEC proposal permits sponsors or their affiliates to hold the risk. Disclosures are different. Most obviously, the SEC pertains only to shelf registrations, while the FDIC is not so limited. In addition, the proposal of the SEC is still a proposal (its comment period does not close until August 2, 2010), and the Commission may modify it substantially before final promulgation. While the final SEC rule may be more or less stringent, it may also ultimately involve issues that are not inherently compatible with the purposes of the Proposed Rule. The Corporation would be best advised to await a final rule from the SEC.

As important, Congress is still working on the regulatory reform bill. The base text for the conference exempts entities from retaining risk in a category of loans that meet certain specified underwriting criteria. Securitizations composed of loans that meet these stringent requirements are exempt from risk retention mandates. It is reasonable to conclude also that Congress has decided that such an approach does not present undue risk to the Deposit Insurance Fund of the FDIC. The Proposed Rule does not contain these provisions.

Congress has spent much time considering how to deal with the concept of risk retention in securitization. Language providing the ability of the agencies to jointly develop rules implementing the general rule of mandated risk retention was included in the House bill on regulatory reform (H.R. 4173). The Senate adopted a similar rule, but on the day following the release of the FDIC Notice of Proposed Rulemaking, it included a mandate that the agencies must adopt exemptions for a statutorily prescribed category of residential mortgages (Sec. 941 of S. 3217). The requirement was just that, mandatory, not precatory as in the House bill. In addition, the agencies were authorized to adopt modifications and exempt other categories of loans from the risk retention requirements. While these rules are amendments to the Securities Exchange Act, not the FDI Act, the Congressional intention with respect to risk retention in securitization is clear and the requirements of the Proposed Rule are inconsistent with those provisions.

We urge the FDIC to reconsider its rigid formulation and adopt instead a formulation that is consistent with the Congressional language. There are good reasons for this besides the obvious one that our government should speak with one voice.

II. The Proposed Rule introduces unfair competition into the market

With respect to insured depository institutions, it is irrelevant that compliance with the restrictions of the Proposed Rule is voluntary; if an institution fails, in receivership the Proposed Rule will determine whether there will be an expedited decision by the FDIC and continuation of interest payments. Since no one can predict which institution will fail, credit rating agencies must assume the worst, and absent compliance with the Proposed Rule, the credit rating agencies will rate the issue as though the institution itself will fail. The restrictions, therefore, are effectively mandatory.

Yet for issues offered by non-insured depository institutions, the credit rating of the issue itself will be judged by the rating agencies, not the credit of the issuing entity. None of the restrictions mandated under the Proposed Rule will be imposed upon those entities, and their absence will not determine what happens if the entity fails. The issue will be judged by normal bankruptcy standards, and therefore, the issue will not be judged on the credit rating of the issuer.

This will put insured depository institutions at a competitive disadvantage to specialty finance companies, foreign depository institutions and other companies not regulated by federal regulators and not subject to the FDIC Proposed Rule.

While the Proposed Rule clarifies the position that the FDIC will take, it is not the only position it could take that would meet the same goals -- recovery of the securitization market and protection of DIF. The commentary argues that absent rigid standards outlined in the Proposed Rule, the securitization market will not recover. Yet Congress, in adopting the language it has adopted in the regulatory reform bill, has judged that not to be the case.

Risk retention as a buffer for losses is an indirect one at best. Those who argue for it believe that requiring such retention will result in better underwriting. It is better underwriting,

however, that leads to lower default rates and smaller losses. Mandating risk retention is one step removed and creates unintended consequences. Since the new legislation will provide nearly limitless authority for the government to require standards for firms to meet in order to demonstrate that they have considered the requirement in the statute that consumers have the ability to repay loans (or in refinancings, received a net tangible benefit), the pressure to use risk retention to achieve the same result indirectly has been dramatically reduced. Underwriting standards can be as strict as the government wants going forward.

With respect to protection for DIF, we would again stress that protection for DIF is a continual goal of Congressional action. Congress does not take actions intentionally that it believes will increase the risk of failures and losses to DIF. Its decisions with respect to risk retention cannot be said to increase the risk of loss to DIF. The Corporation could adopt the same position as Congress has on risk retention without endangering the DIF.

III. The Proposed Rule in conjunction with recently adopted accounting changes may stifle securitizations

There is one additional policy matter that we raised in our earlier comments, and while the Corporation commented that such an issue had been raised it did not respond to the issue in the commentary. The Proposed Rule does not reflect any obvious consideration of the question raised by any mandated risk retention in light of the changes in FAS 166 and 167.

The FDIC and the other agencies have already determined that those accounting changes will lead to more consolidation of assets on bank balance sheets. *Final Rule Amending the Risk-Based Capital Rules to Reflect the Issuance of FAS 166 and FAS 167*. In that rule, the agencies conclude that consolidation will be required in those cases in which a bank retains a residual interest and servicing rights in a securitization. While the rule does not attempt to distinguish different levels of retention, 5% seems as though it would meet any standard for a level at which consolidation might well be required.

Similarly, while the rule links retention of residual interest and servicing rights, there may remain questions about those cases in which servicing rights are not retained -- will there be required consolidation simply from the retention of 5% of the credit risk? If so, should the FDIC rule take that into account?

In addition, the Proposed Rule requires 5% of proceeds of the issue must be retained for one year separate and distinct from the 5% general risk retention. That 5% reserve, when combined with the other restrictions in the rule, increases the chance that an accounting firm would require consolidation under the Proposed Rule. At a minimum it would be a negative consideration.

Clear guidance of the accounting treatment under FAS 166 and 167 will not be settled for some time, but the Proposed Rule makes it more likely that any particular issue will have to be consolidated on the balance sheet of the insured depository institution.

Directly mandating underwriting standards relating to fully indexed and documented income address risk avoidance directly and effectively, and do not raise the same consolidation questions as mandating risk retention.

IV. The safe harbor must have certainty at time the transaction is completed

Investment in securitizations is aided by opinions from legal counsel that the terms of the issuance satisfy mandated rules and laws. Traditionally, those opinions have given comfort to investors that they may rely on the assets in the securitization even if the insured depository institution should fail.

Counsel will be reluctant to give unconditional opinions if there are acts and events that might occur after the transaction closing that are unpredictable and significant. Absent unconditional opinions, investors will be hesitant to invest, thereby adversely limiting the amount of securitization that might occur and the amount of funds that would be available for housing credit.

It is crucial, therefore, that the Proposed Rule avoid ambiguous conditions and mandates for performance after the transaction is completed.

In a number of provisions, the Proposed Rule mandates that certain actions after closing be done, such as making disclosures available to investors. Confirming that disclosures will be made to investors after closing will not be possible at the time the transaction is completed, but it would be possible to confirm that representations and warranties had been made that such disclosures had been made available or would be in the future. In another provision, the Proposed Rule requires that mortgages be originated in compliance with all legal requirements. That may not be able to be confirmed at closing, but a representation and warrant that they have been so originated can be confirmed. A servicer is required to maintain sufficient records or its actions to permit appropriate review, but what is sufficient or what is appropriate is not defined. There are other examples in the draft similar to these.

We urge another review of these kinds of mandated acts to ensure that they are couched in a way that they can be ascertained and confirmed at the time the transaction is closed.

V. Assets as well as securitizations should be grandfathered

It is important that the FDIC grandfather certain securitizations that when made met all of the statutorily required conditions even though they would not now meet the conditions of the Proposed Rule. Many of the underlying assets would not have carried with them the records and information needed to satisfy the conditions in the Proposed Rule.

Similarly, it is important that assets not in pools that have been originated prior to the Proposed Rule be likewise grandfathered so that securitizations can be composed of these assets and the safe harbor be applied. Sponsors would have the same difficulty in discovering the data needed to provide the compliance necessary under the rule. At a minimum, the FDIC should

provide a conditional grandfather, conditioned upon a representation by the sponsor that a diligent search has been made for the data and no data has been found.

Rating agencies would be able to rate those issues with that kind of representation.

VI. The FDIC should adopt a transition period coincident with the transition period adopted by Congress for the risk retention provisions of the regulatory restructuring bill

We urge that a reasonable transition period after the adoption of the Proposed Rule be adopted for whatever rule the Corporation promulgates, and that such rule be coincident with any transition period chosen by Congress to be applied in the case of the risk retention provisions in the regulatory restructuring bill. At the present time, the Senate bill being used as base text for the regulatory restructuring conference committee has an effective date of one year after publication of the final regulations for RMBS, and two years after publication of final regulations for all other assets covered. We believe these would be appropriate transition rules.

VII. The FDIC should Clarify That Sales to Affiliates Are Permissible Up to a Threshold Amount

Section (c)(1) of the Proposed Rule provides that "the obligations shall not be sold to an affiliate or insider." As drafted, this provision would prevent a trust for which an affiliate holds any interest, no matter how small, from obtaining the safe harbor under the Proposed Rule. We do not believe is the FDIC's intent. Many securitization issuers utilize a structure in which affiliates retain some or all of the credit-enhancing subordinated tranches. We therefore suggest that this portion of paragraph (c)(1) be rewritten to say "no more than [50%] of the obligations shall be sold to an affiliate or insider of the sponsor." Alternatively, the FDIC could re-insert the word "predominately" in Section (c)(1) if it deems a bright-line approach to be inadvisable.

In order to obtain a AAA rating on its most senior securitization issuances, many issuers have periodically issued certain subordinated series or tranches to an affiliate. While the most senior tranche is held exclusively by third parties and represents a clear majority of the outstanding investor interest in issuers' securitization trusts, the percentage of outstanding securities owned by affiliates of those issuers has increased in the past 12-18 months due to the absence of a public market for these subordinated securities. In addition, some issuers typically hold a significant seller's interest in our securitization vehicles to facilitate their ability to enter the market quickly and to cover possible fluctuations in outstanding balances. The size of this seller's interest also increases when tranches of securities sold to third parties are repaid. We do not believe the existence of the seller's interest, which is a core feature of credit card master trusts, should affect the availability of the safe harbor. We note, further, that in each case these retained interests represent significant "skin in the game" for issuers. This retention of risk is consistent with the Proposed Rule, new Regulation AB and the proposed legislation on regulatory reform, all of which emphasize retention of risk as a fundamental aspect of securitizations.

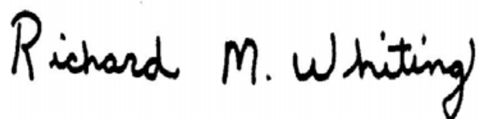
VIII. <u>Confirm that Undrawn Commitments are Grandfathered</u>

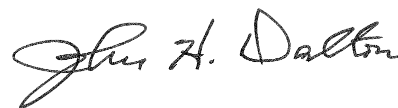
Through securitization trusts, issuers often enter into transactions with asset-backed commercial paper conduits in which the commitment amount may be fully or partially undrawn at closing. This structure allows issuers to issue additional interests to the conduit during the term of the commitment, up to a specified maximum amount. A number of issuers utilize this structure to provide cost-effective contingent liquidity. It allows the bank to use this liquidity on as little as one to three days' notice to the conduit sponsor (agent). These undrawn conduit commitments do not represent an unfunded securitization structure, but rather a fully or partially unfunded tranche of a larger issuance trust, with many issuances to third parties outstanding. This securitization structure is viewed favorably by federal banking agencies as a source of liquidity.

We respectfully request clarification with respect to the Final Rule's provisions regarding transitional Safe Harbor as related to the fact that the Safe Harbor applies to securitizations "for which *beneficial interests* were issued on or before September 30, 2010." In the case of an undrawn conduit, a "beneficial interest" is not technically issued until the draw is made, which in some transactions could occur after September 30, 2010. Consequently, we are requesting that the FDIC clarify that the Safe Harbor applies to undrawn commitments that are entered into prior to September 30, 2010 that otherwise satisfy the requirements necessary to qualify for the Safe Harbor. If these undrawn conduits are not grandfathered under the Safe Harbor, issuers would lose their ability to draw on these facilities and, consequently, the contingent liquidity they provide to their businesses. We believe our position on this issue is consistent with the FDIC's commentary to the NPR that states "the FDIC does not view the inclusion of existing credit lines that are not fully drawn in a securitization as causing such securitization to be an "unfunded securitization."

We appreciate the opportunity to respond to the request for comments on the Proposed Rule.

Respectfully submitted,





Rich Whiting
Executive Director & General Counsel
The Financial Services Roundtable

John H. Dalton
President
Housing Policy Council
The Financial Services Roundtable