30 Broad Street, *28th floor*, New York, NY 10004
Tel: 212.509.1844 *Fax:* 212.509.1895
www.cmbs.org

February 22, 2010

VIA ELECTRONIC FILING
Mr. Robert E. Feldman
Executive Secretary
Attention: Comments
Federal Deposit Insurance Corporation
550 17th Street, NW
Washington, DC 20429

Re: Treatment by the Federal Deposit Insurance Corporation as Conservator or Receiver of Financial Assets Transferred by an Insured Depository Institution in Connection with a Securitization or Participation After March 31, 2010, RIN # 3064-AD55

Dear Mr. Feldman:

The Commercial Mortgage Securities Association ("CMSA") appreciates this opportunity to respond to the request of the Federal Deposit Insurance Corporation for comments concerning the Advance Notice of Proposed Rulemaking regarding treatment of assets transferred by an insured depository institution in connection with a securitization or participation when such institutions enter FDIC conservatorship or receivership.[1] CMSA is the collective voice of the entire commercial real estate (CRE) finance market, including investors such as insurance companies, pension funds, and money managers; commercial and investment banks; rating agencies; accounting firms; servicers; and other service providers.

Because our membership consists of all constituencies across the entire market, CMSA has been able to develop comprehensive responses to policy questions to promote increased market efficiency and investor confidence. For example, our members have, and will continue, to work closely with policymakers in Congress, the Administration, and financial regulators, providing practical advice on measures designed to restore liquidity and facilitate lending in the

[1] Advance Notice of Proposed Rulemaking, Treatment by the Federal Deposit Insurance Corporation as Conservator or Receiver of Financial Assets Transferred by an Insured Depository Institution in Connection with a Securitization or Participation After March 31, 2010, 75 Fed. Reg. 934 (Jan. 7, 2010) ("ANPR").

commercial mortgage market, such as the Term Asset-Backed Securities Loan Facility ("TALF"). CMSA also is recognized as a leader in the development of standardized practices and in ensuring transparency in the commercial real estate finance industry.

Thus, we have a distinct perspective on the tremendous challenges facing the $3.5 trillion market for commercial real estate finance and the need to craft regulatory reforms so that they support, rather than undermine, the recovery of the commercial real estate sector and that of the nation's economy as a whole. One of the biggest challenges facing the commercial real estate sector is the lack of available credit. Originations by portfolio lenders and securitization programs have fallen dramatically, contributing to the decline in property values and exacerbating loan defaults and losses. Restarting commercial real estate via securitization is a critical step in restoring the flow of credit, and stemming the tide of mounting losses.

I. OVERVIEW

CMSA concurs that the FDIC's existing safe harbor rule must be updated to account for recent changes in accounting rules that will affect the ability of securitizations to meet the criteria for an accounting sale that are presently necessary to comply with the safe harbor's legal isolation requirement. However, we urge the FDIC to:

- First, be mindful of the fact that the FDIC's securitization reform proposals come in the midst of broader regulatory reform initiatives – which include securitization reform – that are being developed by Congress, as well as by the Securities and Exchange Commission in carrying out its investor protection function. By proceeding with separate securitization reform provisions, the FDIC would be creating an environment of piecemeal regulation that fails to get at the root of the problem of imprudent underwriting and securitization practices that concern us all, since any FDIC regulations would apply only to insured depository institutions. With piecemeal regulation comes the danger of competitive disadvantage for banks that sponsor securitizations, if they are compelled to comply with securitizations restrictions that other types of institutions can ignore. And the possibility of there being restrictions that overlap, or worse, conflict with those imposed by Congress is not a matter that can easily be dismissed.

  For these reasons, CMSA urges the FDIC to work in concert with Congress, the Administration, and other agencies that are developing securitization reforms to ensure that the FDIC's efforts to address its concerns as conservator or receiver of failed institutions do not lead to a regulatory framework of conflicting or overlapping requirements that unnecessarily impede resumption of securitizations and the restoration of functioning credit markets. In short, we believe that securitization reform should not be added to the present task of updating the FDIC's safe harbor rule, but are more appropriately addressed in the context of legislative solutions that will apply new securitization requirements to <u>all</u> securitizations, not just those sponsored by banks.

- Second, the FDIC should limit this initiative to making the necessary modifications to the safe harbor rule by focusing on legal isolation criteria rather than risk unintended consequences that could end up perpetuating the decline of the securitization market

and credit constraints. A very clear example of the potential for such consequences can be seen in the ANPR's suggestion of a minimum five percent credit risk retention by the sponsor-institution to ensure that sponsors maintain adequate "skin in the game" to induce sound underwriting of the loans that are securitized. But as policymakers are beginning to recognize, while risk retention obligations may appear to be an effective step toward reform when considered in isolation, they will create practical difficulties when they must operate in the context of numerous other regulatory changes that have recently gone into effect, particularly the changes in securitization accounting standards promulgated by the Financial Accounting Standards Board ("FASB") that have given rise to this very rulemaking. Indeed, rigid risk retention obligations, when coupled with the new accounting standards, could eliminate the utility of securitization and actually shut down parts of this market at a time when securitization is desperately needed to help restore the flow of credit.

While securitization reform is an important policy objective, at this time the soundest approach in this context is to de-link securitization reform from the safe harbor. Conditions such as minimum risk retention and loan seasoning are not required for the safe harbor to function effectively, and there are better ways to encourage prudent underwriting.

- Third, note that where securitization reforms such as minimum risk retention are ultimately adopted, it is critically important that they recognize and account for significant differences between various types of asset-backed securities, or they risk harming the markets they seek to reform.

  Such a considered approach was taken in the adoption of a risk retention requirement in the Wall Street Reform and Consumer Protection Act of 2009 (H.R. 4173) passed by the U.S. House of Representatives in December.[2] At the urging of CMSA and others, the bill would give regulators the flexibility to develop risk retention requirements that are adapted to the category of asset involved, rather than prescribing a rigid minimum risk retention regime for sponsors or originators of asset-backed securities. Such flexibility would be warranted in the context of CMBS. This is the case because the CMBS market has unique characteristics that minimize the types of abusive practices policymakers seek to address, and CMBS is structured in such a way that third-party investors may seek to acquire and hold the retained risk, and should be allowed to do so to free up sponsors' capital, which gets injected back into the credit system in the form of additional, much needed liquidity.

  In short, before proposing and implementing a risk retention requirement or other types of securitization reform, there must be consideration of whether, in light of the actions of Congress and other agencies, the adoption of certain reforms by the FDIC will be effective and will facilitate the health of the securitization markets overall. CMSA accordingly commends the FDIC for initiating this rulemaking process with an Advanced Notice of Proposed Rulemaking rather than a specific proposed rule, because we believe this approach will stimulate robust comment on these matters at the outset and help the FDIC proceed in a fashion that will minimize unintended negative consequences.

---

[2] Wall Street Reform and Consumer Protection Act of 2009, H.R. 4173, 111th Cong. § 1501 et seq. (2009).

- And finally, on the topic of timing, we note that the amount of deliberation that obviously will be necessary to formulate sound policy here, coupled with the amount of time that will be needed to implement the new safe harbor requirements, make it clear that the transition period bridging the old and new requirements must be extended beyond March 31, 2010. Therefore, CMSA requests that any modified safe harbor requirements become effective no sooner than 12 months after *Federal Register* publication of the final rules. CMSA offers this recommendation with the caveat that it applies only if the FDIC opts not to include significant securitization reform elements in a new rule such as risk retention, disclosure and documentation requirements. CMSA is unable to opine, at this early stage, on the amount of lead time that would be necessary if any of these sweeping changes are ultimately incorporated into the safe harbor rule.

The following discussion will offer some brief detail regarding the current troubled state of the commercial real estate market and the importance of securitization in aiding the market's recovery. General observations regarding the ANPR's approach will then be discussed, followed by more specific suggestions concerning particular aspects of the new safe harbor framework described in the ANPR.

II. CURRENT STATE OF THE COMMERCIAL REAL ESTATE MARKET AND THE IMPORTANCE OF SECURITIZATION

There are tremendous challenges facing the $7 trillion commercial real estate (CRE) market. These challenges have and will continue to impact U.S. businesses that provide jobs and services, as well as millions of Americans who live in multi-family housing. Unlike in previous downturns, the stress placed on the CRE sector today comes from a number of different but connected factors that when taken together will exacerbate the capital crisis and prolong a recovery:

1. Little or no liquidity or lending – the volume of new CRE loan originations and thus new securitizations in the commercial mortgage-backed securities (CMBS) market has plummeted from $240B in 2007 (half of all CRE lending in 2007) to $12B in 2008, and approximately $2B in 2009;

2. Significant loan maturities – there will be approximately $1 trillion in CRE loan maturities over the next several years, but the capital necessary to refinance these loans remains largely unavailable and many loans require additional equity to refinance given the decline in CRE asset values;

3. An economic downturn – that negatively impacts key indicators in CRE, such as employment and business performance, as well as commercial and multifamily occupancy rates, rental income, and property values; and

4. An "equity gap" – with 30-50% depreciation in CRE, an equity gap exists between loan amounts and the equity needed to extend or re-finance a loan, which impacts even performing loans.

Even in robust economic times, the primary banking sector did not have enough lending capacity to meet borrowers' financing demands. Hence the importance of private investors who provide much needed capital that fuels overall lending through the process of securitization.[3] Securitization also offers a more efficient and less expensive form of financing than other types of equity or debt financing, and facilitates the efficient allocation of risk by enabling entities that originate credit risk to transfer it to others throughout the financial system who are willing to assume it.

Given these factors, policymakers have correctly recognized that no economic recovery plan will succeed unless it helps re-start the securitized credit markets,[4] and securitization has been a key component in many of the government's initiatives to help restore liquidity to financial markets, such as TALF.

III. NECESSARY SECURITIZATION REFORMS SHOULD NOT BE TIED INTO THE SAFE HARBOR REGIME

It is against this backdrop – of extraordinary challenges for the CRE finance market and for the nation's financial markets as a whole – that new and unprecedented financial regulatory reform proposals have been made that would change the nature of the securitized credit markets which are at the heart of recovery efforts. The securitization reform proposals are plainly prompted by some of the problematic practices that were typical in the subprime and residential securitization markets.

CMSA does not oppose efforts to address such issues, as we have long been an advocate within the industry for enhanced transparency and sound practices. Nor is there any question that the FDIC must establish appropriate standards to address its prudential concerns as conservator or receiver of an insured financial institution. However, we are very concerned about the FDIC's incorporation of securitization reform into the safe harbor regime because this approach would apply only to securitizations sponsored by insured depository institutions, and not to other financial institutions that sponsor securitizations.

---

[3] See, e.g., U.S. Department of the Treasury, "Road to Stability: Consumer & Business Lending Initiative," (March 2009) (securitized loans "account for almost half of the credit going to Main Street"), www.financialstability.gov/roadtostability/lendinginitiative.html.

[4] E.g., Remarks by Treasury Secretary Timothy Geithner Introducing the Financial Stability Plan (Feb. 10, 2009) ("Because this vital source of lending has frozen up, no financial recovery plan will be successful unless it helps restart securitization markets for sound loans made to consumers and businesses – large and small."), http://www.ustreas.gov/press/releases/tg18.htm; International Monetary Fund, "Restarting Securitization Markets: Policy Proposals and Pitfalls," Chapter 2, Global Financial Stability Report: Navigating the Financial Challenges Ahead (Oct. 2009), at 33 ("Conclusions and Policy Recommendations" section) ("restarting private-label securitization markets, especially in the United States, is critical to limiting the fallout from the credit crisis and to the withdrawal of central bank and government interventions."), http://www.imf.org/external/pubs/ft/gfsr/2009/02/pdf/text.pdf.

Key issues and questions raised by the ANPR, including measures to better align risk and protect investors, are addressed by the financial reform legislation in both Houses of Congress, which could soon become law. Those legislative proposals would apply across the board to all securitizations, not just those sponsored by insured depository institutions. The FDIC should keep in mind the real prospects for Congressional action in this area. And the agency must take the legislation into account and avoid allowing its very legitimate safety and soundness concerns to lead to development of a regulatory framework of conflicting or overlapping requirements and unintended negative consequences that impede restoration of functioning credit markets.

A. The Danger of Piecemeal Securitization Restrictions

By imposing securitization restrictions in a piecemeal manner, regulators risk driving the market to foreign banks and less regulated financial institutions that are not subject to FDIC jurisdiction, while at the same time hindering the ability of depository institutions to meaningfully participate to provide additional credit to the economy. CMSA believes it would be preferable to have rules that would apply across the board, as envisioned by the legislative proposals, than adopt a rule that applies only to insured depository institutions.

It follows that the suggestion in the ANPR of an entirely different disclosure regime for bank securitizations[5] would be unsound policy. As a practical matter, requiring additional disclosure for transactions sponsored by banks would create inconsistent disclosure practices that may complicate efforts by investors to compare transactions sponsored by banks with those sponsored by other institutions, and may cause unnecessary confusion. Moreover, the different disclosures for bank securitizations would be difficult to track and could adversely affect the trading of bank securitizations on secondary markets. In effect, such rules would add a layer of complexity, rather than the transparency the FDIC seeks. While a robust disclosure regime is needed more uniformly across the market, an overlay of special FDIC-imposed additional requirements on insured depositary institutions is not necessary for a workable safe harbor rule.

We appreciate the ANPR's desire to provide enhanced disclosure requirements for securitizations. However, to ensure broad market efficiency and adequate liquidity, expanded disclosure requirements should be applied to all securitization issuers, and not just to insured depository institutions seeking to comply with the safe harbor rules. SEC Regulation AB is intended to achieve uniformity in disclosures among all types of issuers. We believe that overall disclosure requirements should remain in the province of the SEC to promote consistency and uniform transparency. Significantly, we note that the financial regulatory reform legislation recently passed by the U.S. House of Representatives directs the SEC to adopt new disclosure requirements for ABS,[6] and separately, the SEC has announced that it has initiated a review of its current ABS disclosure requirements.[7]

---

[5] See ANPR Sample Regulatory Text, Section 360.6 (b)(2), 75 Fed. Reg. at 940.

[6] See H.R. 4173, §§ 1503, 1504.

[7] Speech by SEC Chairman Mary Schapiro: "The Road to Investor Confidence," (Oct. 27, 2009) ("I have asked the staff to broadly review our regulation of ABS including disclosures, offering process, and reporting of asset-backed issuers. The staff is considering a number of

All of the foregoing concerns militate against linking securitization reform to the safe harbor. None of the reform proposals, such as minimum risk retention and enhanced disclosures, are required for a workable safe harbor rule. And while it is unquestionably desirable to promote policies such as prudent underwriting and safety and soundness of insured institutions, there are other, more surgical means of addressing these concerns. For example, minimum underwriting standards have been proposed in the residential context. Other means of imparting discipline in underwriting can be adopted for other contexts, again without having to conflate those issues with the question of whether the safe harbor applies.

B. The Particular Importance of Customized Regulatory Requirements for Securitization

As a general matter, policymakers must ensure that regulatory reforms are tailored to address the unique aspects of each securitization asset class, because failure to do so will risk the viability of markets that already are functioning in a way that does not pose a threat to overall economic stability. Reforms also must not be adopted in a vacuum, because ignoring the combined effects of various regulatory regimes may likewise lead to more harm than good. We will explain why such measures are critically important using our market as an example.

The CMBS market has innate characteristics that minimize the risky securitization practices that policymakers hope to address. These characteristics relate to the type and sophistication of the borrowers, the structure of securities, the underlying collateral, and the level of transparency in CMBS deals:

- Borrowers: Commercial borrowers are highly sophisticated businesses with cash flows based on business operations and/or tenants under leases. This characteristic stands in stark contrast to the residential market where, for example, loans were underwritten in the subprime category for borrowers who may not have been able to document their income, or who may not have understood the effects of factors like floating interest rates and balloon payments on their mortgage's affordability. Additionally, securitized commercial mortgages have different terms (generally 5-10 year "balloon" loans), and they are, in the vast majority of cases, non-recourse loans that allow the lender to seize the collateral in the event of default.

- Structure of CMBS: There are multiple levels of review and diligence concerning the collateral underlying CMBS, which help ensure that investors have a well informed, thorough understanding of the risks involved. Specifically, in-depth property-level disclosure and review are done by credit rating agencies as part of the process of rating CMBS bonds. Moreover, non-statistical analysis is performed on CMBS pools. This review is possible given that there are far fewer commercial loans in a pool (typically between 100 and 300) that support a bond, as opposed, for example, to residential pools, which are typically comprised of between 1,000 and 4,000. The more limited number of loans in the commercial

---

proposed changes, which are designed to enhance investor protection in this vital part of the market."), http://www.sec.gov/news/speech/2009/spch102709mls.htm.

context allows market participants (investors, rating agencies, etc.) to gather detailed information about income producing properties and the integrity of their cash flows, the credit quality of tenants, and the experience and integrity of the borrower and its sponsors, and thus conduct independent and extensive due diligence on the underlying collateral supporting their CMBS investments.

- First-loss Investor ("B-Piece Buyer") Re-Underwrites Risk: CMBS bond issuances include a first-loss, non-investment grade bond component. The third-party investors that purchase these lowest-rated securities (referred to as "B-piece" or "first-loss" investors) conduct their own extensive due diligence (usually including, for example, site visits to every property that collateralizes a loan in the loan pool) and essentially re-underwrite all of the loans in the proposed pool. Because of this, the B-piece buyers often negotiate the removal of any loans they consider to be unsatisfactory from a credit perspective, and specifically negotiate with bond sponsors or originators to purchase this non-investment-grade risk component of the bond offering. This third-party investor due diligence and negotiation occurs on every deal before the investment-grade bonds are issued.

- Greater Transparency: A wealth of transparency currently is provided to CMBS market participants via the CMSA Investor Reporting Package® (CMSA IRP®). The CMSA IRP provides access to loan, property and bond-level information at issuance and while securities are outstanding, including updated bond balances, amount of interest and principal received, and bond ratings, as well as loan-level and property-level information on an ongoing basis. The "CMSA IRP" has been so successful in the commercial space that it is now serving as a model for the residential mortgage-backed securities market. By way of contrast, in the residential realm, transparency and disclosure are limited not only by servicers, but by privacy laws that limit access to borrowers' identifying information.

As the FDIC is aware, a risk retention provision is included in the regulatory reform bill recently passed by the House.[8] In terms of reforms, "skin-in-the game" requirements may be a key component regardless of who ultimately retains it – the originator, the issuer, or the first-loss buyer – and regardless of the form it takes. It is important here to bear in mind that "skin-in-the game" measures can take a number of forms (such as the use of appropriate representations and warranties, covenants to re-purchase, B-Piece investors, and a seller's interest in an asset), in addition to the much-discussed concept of having an originator or sponsor retain a minimum percentage of credit risk in the securitization.

Continuing with the use of our market as an example, the structure of CMBS has always had a third-party in the first-loss position that specifically negotiates to purchase this risk. Most significantly, these third-party investors are able to, and do, protect their own interests in the long-term performance of the bonds rather than relying merely on the underwriting and representations of securitizers or originators. First-loss buyers conduct their own extensive credit analysis on the loans, examining detailed information concerning every property – before buying the highest risk bonds in a CMBS securitization. And notably, in many cases, the holder

[8] H.R. 4173, § 1502.

of the first-loss bonds is also related to the special servicer who is responsible on behalf of all bondholders as a collective group for managing and resolving defaulted loans through workouts or foreclosure.

It follows that the policy rationale for imposing a risk retention requirement on issuers or underwriters as "securitizers" that could preclude them from transferring the first-loss position to third parties is unnecessary in this context, because, although the risk is transferred, it is transferred to a party that is acting as a "securitizer" and that is fully cognizant, through its own diligence, of the scope and magnitude of the risk it is taking on. In effect, when it comes to risk, the first-loss buyer is aware of everything the issuer or underwriter is aware of.

Therefore, within the confines of a risk retention rule, CMBS securitizers should be permitted to transfer risk to B-piece buyers who – in the CMBS context at least – act as "securitizers." To require otherwise would limit the ability of CMBS lenders to originate new bond issuances, by needlessly tying up their capital and resources in the retained risk, which in turn, would crush the flow of credit at a time when our economy desperately needs it.

The House bill takes such factors into account by incorporating flexibility for regulators to tailor risk retention rules to fit the unique aspects of the various classes of asset-backed securities. So, for example, the legislation would not preclude regulators from permitting CMBS securitizers to transfer risk to B-piece buyers, or from adopting other retention structures that have the desired effect.[9] Significantly, Congress also directed that a study be made of the effects of risk retention requirements particularly as they interact with other regulatory standards like accounting rules, to give policymakers a more complete understanding of these matters.[10]

The danger of imposing a rigid, one-size-fits-all risk retention requirement on all originators of asset-backed securities should be readily apparent from the preceding discussion. If the consequences of the requirement are not completely thought out and understood, and if the rule does not allow for the differences between asset classes, the likely and unintended consequence will be the shutdown of some securitization markets. We note that Comptroller of the Currency John C. Dugan has expressed similar concerns in urging the FDIC to be mindful of the prospects for legislative action concerning securitization reform.[11]

C. The Importance of Considering the Combined Effects of Regulation

[9] See H.R. 4173, § 1502 (a) (which would add a new Section 29(c)(2)(A) to the Securities Act of 1933).

[10] See id. § 1502 (b).

[11] See John C. Dugan, Comptroller of the Currency, Statement on the Federal Deposit Insurance Corporation's Advance Notice of Proposed Rulemaking on Securitizations (Dec. 15, 2009), at 1-3 ("[R]ecent studies note that a policy of requiring a rigid minimum retention requirement risks closing down parts of securitization markets if poorly designed and implemented. Before proposing and implementing such a requirement for all securitizations, further analysis is needed to ensure an understanding of the potential effects of the different ways in which risk could be retained.").

The potential for harming the credit markets is heightened when reforms like minimum risk retention are coupled with the new consolidation requirements in Financial Accounting Standard ("FAS") 166/167. Not only do FAS 166/167 make sales treatment more difficult to achieve, as the FDIC recognizes, the combination of a required minimum retained risk by an originator and consolidated accounting will lead to capital and credit constriction, a consequence also pointed out by Comptroller Dugan.[12]

It would obviously be undesirable if reforms designed to strengthen a market end up stifling it instead. This is one of the reasons that the House bill directs that a study of the effects of securitization reform coupled with other regulations, including accounting standards, be done before final reforms such as risk retention are imposed.[13] CMSA suggests that the FDIC take a similar, deliberate approach if it decides to proceed with adopting restrictions on securitizations, and only adopt such restrictions after attaining a thorough understanding of their effect in combination with the new accounting rules.

IV. OBSERVATIONS CONCERNING SPECIFIC ASPECTS OF THE PROPOSED SAFE HARBOR CONDITIONS

Leaving aside the aspects of the ANPR that involve risk retention, disclosure, and other significant changes to the safe harbor conditions, we wish to preface our more specific suggestions by generally urging the FDIC not to regulate creativity out of the securitization process, as creativity, appropriately bounded, will help spur the types of evolution in the financial markets that can inure to the good of the nation's economy as a whole.

Our observations concerning the parts of the ANPR that relate more directly to the determination of whether assets will be treated as legally isolated are as follows:

First, CMSA observes that overall, the ANPR would create a safe harbor framework that may be completely ineffectual. This is so because certain conditions, such as ongoing periodic disclosures, would make application of the safe harbor uncertain over time. We believe that because the market will require certainty on the critical protections provided by the safe harbor, the safe harbor must be established reliably at transaction origination, rather than being dependent upon subjective factors[14] or future events.[15] The safe harbor protections lose much, if not all, of their benefit if they are dependent upon subjective standards or the ongoing actions or inactions of one or more transaction counterparties.

---

[12] Id. at 3 ("The suggested five percent retention would also make sales treatment more difficult to achieve under FAS 166/167, with capital and credit constriction implications.").

[13] See H.R. 4173 § 1502 (b)(2).

[14] For example, see ANPR Sample Regulatory Text, Section 360.6 (b)(2)(i)(A), 75 Fed. Reg. at 940 (requirement to provide to provide disclosure that is "presented in such detail and in such format as to facilitate investor evaluation and analysis of the obligations and financial assets securitized").

[15] E.g., ANPR Sample Regulatory Text, Section 360.6 (b)(2)(i)(C) and (D), 75 Fed. Reg. at 940 (requirement to comply with ongoing disclosure obligations).

Second, the ANPR suggests that re-securitizations would not be eligible for the safe harbor unless all underlying securitizations satisfy all conditions in the ANPR.[16] We disagree with this approach, as this would effectively exclude legacy ABS, and perhaps future non-bank ABS, from the scope of qualifying collateral. The purported benefits of limiting banks' re-securitization options to achieve increased liquidity and ratings insulation for securities of this nature are not readily apparent.

Third, the ANPR asks whether all securitizations should be required to have payments of principal and interest on the obligations primarily dependent on the performance of the financial assets supporting the securitization.[17] CMSA does not believe such a requirement would be sound policy. External credit enhancement should be an available tool for banks to use when sponsoring securitization transactions. Guarantees and insurance have been, and will likely continue to be, an important component of mortgage finance in the United States, including the roles played by the government sponsored enterprises and the Government National Mortgage Association. These techniques should not be forbidden in the non-agency market. This proposal may limit the liquidity of certain types of loan products and increase funding costs for banks. Different approaches might be considered for asset-backed commercial paper, and other unique circumstances. It would also appear to limit the ability of banks to provide seller's loss coverage and other seller-provided external credit support to transactions, which would be consistent with the alignment of the incentives the FDIC's suggested condition seeks to achieve.

Fourth, we note that in a January 2010 article, Moody's Investors Service, Inc. raised a number of concerns that ultimately call into question whether the safe harbor envisioned in the ANPR would provide the benefit of delinking the rating of the securitization obligations from the rating of the asset originator or sponsor.[18] More specifically, the Moody's article observes that while the sample regulation in the ANPR effectively addresses the risk that the FDIC would exercise its stay powers to delay payments to ABS investors, the ANPR is unclear as to whether securitizations meeting the safe harbor requirements would be afforded safe harbor from repudiation, a protection afforded by the existing safe harbor rules.[19] Moody's highlights this gap because upon repudiation, the FDIC would only have to pay ABS investors damages limited to the market value of the underlying assets, which may be less than the par value of the ABS, thereby introducing market value risk to the ABS. Moody's advises that a concern related to the FDIC's retention of repudiation power is the possibility that repudiation could lead to intra-payment period interest shortfalls. By statute, repudiation damages include accrued interest prior

---

[16] See ANPR Sample Regulatory Text, Section 360.6 (b)(1)(i)(A), 75 Fed. Reg. at 939.

[17] See id. at 937.

[18] "Moody's: FDIC's Advanced Notice on Proposed Safe Harbor Unclear on Protection Against Repudiation Risk," (Jan. 6, 2010) (hereafter, "Moody's Safe Harbor Sector Comment").

[19] See id. comparing ANPR Sample Regulatory Text, Section 360.6 (d)(4), 75 Fed. Reg. at 942, to the introductory text at 75 Fed. Reg. at 935 (the introductory text of the sample regulation states that the safe harbor would preclude repudiation (p. 7), but section (d)(4) of the sample regulation indicates that the FDIC would retain the power to repudiate).

to the date the FDIC is appointed as conservator or receiver. But if the FDIC exercised its repudiation powers some time after it was appointed, the repudiation payment would not include interest accrued between the FDIC's appointment and the repudiation. The ANPR seems to try to mitigate this shortfall by having the FDIC consent to making "regularly scheduled payments." However, there could still be an interest shortfall if the FDIC repudiated in the middle of a payment period. In such a case, ABS investors would not receive accrued interest from the last payment date until the date of repudiation.

Moody's finally notes that the FDIC's consent to "regularly scheduled payments" in the ANPR is not explicitly defined. The lack of clarity is problematic because it is plausible to interpret the term as including only payments that would be payable to investors had the sponsor not gone into receivership, and that increased or different payment priorities caused by events of default related to receivership would be beyond the scope of regularly scheduled payments. It is unclear whether the term "regularly scheduled payments" includes changes to payment priorities (i.e., an acceleration of principal payments) due to performance-based amortization triggers breached prior to receivership. If the FDIC does not consent to these "performance" or "amortization" payments being made, a transaction could revert back to the pre-amortization period waterfall for a period of up to 90 days, which would reduce anticipated payments to bondholders.

Moody's advises that its ABS ratings typically address credit losses on the underlying assets in a scenario where the assets are held to maturity pursuant to the promise made by the issuer. Adding exposure to market value risk would dramatically alter the credit analysis since, in addition to credit losses, the asset pool would be subject to being valued under potentially harsh or illiquid market conditions following the sponsor's failure. If the FDIC's repudiation power is not waived or otherwise mitigated in the final version of the rule, the credit quality of bank-sponsored ABS issued after the rule's effective date will be more highly linked to the credit quality of its bank sponsor than is the case now, eliminating an important benefit that is provided by the safe harbor. Moody's stated, in sum that "[b]ank sponsors rated below "Aa" would be unlikely to achieve "Aaa" ratings for their ABS if this risk isn't mitigated."[20]

Lastly, there are two conditions the ANPR suggests be imposed only on residential securitizations and not commercial ones, but that are cause for sufficient concern that CMSA wishes to make clear such conditions would be problematic, and under no circumstances should such conditions be extended to CMBS:

- The ANPR asks whether all external credit support should be banned for RMBS.[21] We disagree with such an approach. Investors view external credit enhancement as important to address their specifications with respect to a transaction. External enhancement also serves the beneficial purpose of bringing an additional party into the transaction to review collateral and express views on the structure and risks associated with the underlying assets. Overall, external support may serve to reduce risk to the banking system. While we are not arguing with the premise that

[20] Moody's Safe Harbor Sector Comment at 1.

[21] Id. at 937.

maintaining “skin in the game” is a worthwhile objective, restricting all third party support may result in investors demanding higher rewards, and these costs are likely to be passed on to consumers; and,

- The ANPR asks whether mortgages to be securitized should be retained on the institution’s balance sheet for twelve months prior to transfer.[22] This approach would be counter-productive because it would diminish an institution’s capacity to make new loans, since the institution would have to hold capital against these prior to securitization. This requirement could also cause lenders to prefer prime quality borrowers, to the detriment of credit availability for non-prime borrowers.

V. CONCLUSION

CMSA believes the FDIC has taken a productive step by initiating this rulemaking process with an Advanced Notice of Proposed Rulemaking rather than a proposed rule. Such an approach will stimulate robust comment on these matters at the outset and help the FDIC proceed in a fashion that will minimize unintended negative consequences. In the immediate term, we urge that the transition period bridging the old and new safe harbor requirements be extended beyond March 31, 2010, considering the amount of time that will be needed to formulate sound policy here and the amount of time that will be needed to implement the new safe harbor requirements. A modified new safe harbor requirement should become effective no sooner than 12 months after *Federal Register* publication of the final rules.

Longer term, we urge the FDIC to take CMSA’s comments into account and avoid the prospect of piecemeal or conflicting regulation, and negative unintended consequences for the securitization market, by following the Congress’s lead on securitization reform.

Sincerely,

Dottie Cunningham
Chief Executive Officer

[22] Id. at 938.