Via Electronic Mail: Comments@FDIC.gov

February 22, 2010

Robert Feldman, Executive Secretary
Federal Deposit Insurance Corporation
550 17th Street, NW
Washington, D.C. 20429
Attention: Comments

Re: Treatment of 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 (RIN3064-AD55)

Ladies and Gentlemen:

Discover Financial Services ("Discover") appreciates the opportunity to submit this letter in response to the request for comment by the Federal Deposit Insurance Corporation (the "FDIC") regarding its Advance Notice of Proposed Rulemaking entitled "Treatment of 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" (the "ANPR"). Discover commends the FDIC for its ongoing support of the securitization market and acknowledgment of the vital role that securitizations play in allowing financial institutions to provide cost-effective credit to consumers. As recognized in the ANPR, the legal isolation safe harbor is a critical component of a functioning securitization market, and Discover supports the FDIC's efforts to develop an effective safe harbor in response to recent accounting changes that have impacted issuers' ability to satisfy the requirements of the FDIC's existing rule.

Discover has been active in the credit card securitization market since 1989, securitizing over $93.5 billion in credit card receivables through more than 100 transactions. Credit card securitization has been an important, efficient and cost-effective means for Discover to fund its lending activities, allowing Discover to provide credit to its cardholders at a lower cost than would otherwise have been possible. As of November 30, 2009, Discover had $22.3 billion in securitization funding outstanding. For the past 20 years, Discover's securitization trusts have paid all maturing securities in full and on time and have never had an early amortization event, event of default or other adverse event that would cause early or late repayment.

We appreciate that events of the past two years have led to a reexamination of securitization principles and practices, driven largely by issues in the mortgage-backed securities markets and related repackagings of those securities. But we are concerned that issues surrounding these other types of securitizations, which are very different than credit card securitizations in their economics, participants, disclosure practices, risk retention and other aspects, is leading to restrictions on our ability to continue to use a funding source on which we and others in our industry have responsibly relied for decades. We understand that our ability to continue to fund our receivables through securitization depends on the performance of our assets over time and our ability to repay our investors as they expect, and we have been incredibly protective of our asset quality, our brand loyalty, our securitization program and our investors over the years.

The FDIC has been a long-time supporter of and advocate for securitization, and we believe that the reasons for that support—at least in the context of credit card securitizations—are still fundamentally sound. The current FDIC Rule adopted in 2000 (12 CFR 360.6 (the "Securitization Rule")) has been a critical component in maintaining the efficient functioning of the securitization market over the past decade. The Securitization Rule established a clear and reliable path to qualifying a transaction under the legal isolation safe harbor, which provided certainty to issuers and investors as well as the rating agencies. This certainty around legal isolation and regulatory protection is necessary to enable issuers to attain the highest rating for these securities from the rating agencies, which is fundamental to the positive economics of the securitization market that allow issuers to rely on capital markets liquidity, rather than deposits, to provide cost-effective credit to consumers. Consequently, in order to achieve its stated goal of promoting a robust securitization market going forward, it is incumbent upon the FDIC to structure a new safe harbor with clear and achievable conditions that provides certainty for both issuers and investors. In our view, such a safe harbor is fully consistent with the overarching responsibility of the FDIC to protect the deposit insurance fund and promote the soundness of the financial system as a whole.

Discover is a member of the American Securitization Forum (the "ASF") and has participated directly in the ASF's FDIC Working Group, which has submitted a separate comment letter on the ANPR. Many of the comments contained in the ASF response letter touch directly on areas of concern to Discover, and we would like to express our strong support for the comments and suggestions in the ASF comment letter. This letter provides Discover's additional comments on matters raised in the ANPR that are of particular importance to Discover.

Extend Transition Period under Interim Final Rule

Discover commends the FDIC for adopting the interim final rule that extended the Securitization Rule's legal isolation safe harbor through March 31, 2010 (the "Transition Period"). However, given the critical role that a functioning securitization market has played in allowing financial institutions to provide credit to consumers, Discover believes that the Transition Period should be extended to allow for a more robust analysis of the impacts that revisions to the safe harbor rule may have both on the functionality of the securitization market and ability of issuers to satisfy the conditions contained therein. Extending the Transition Period would also minimize disruption to potential issuances in the securitization market.

Safe Harbor Must Provide Certainty as to Legal Isolation

The Securitization Rule's legal isolation safe harbor has been a critical component of maintaining the efficient functioning of the securitization market by providing certainty to issuers, investors and the rating agencies that the FDIC will not seek to reclaim assets that have been transferred in a securitization that meets the conditions of the safe harbor. In order to maintain an effective securitization market going forward, the FDIC must structure a revised safe harbor that is as clearly defined and provides the same degree of certainty as its predecessor.

In order to provide this certainty, the safe harbor must rely solely on conditions that can be satisfied at the closing of the transaction. If conditions are present that could permit the FDIC to void the safe harbor after the issuance of securities, the rating agencies will be unwilling to assign the highest level ratings to the transactions, which would negatively impact the economics of securitizations in a way that would likely make them prohibitive to issuers.

Substantive Reform of Securitization Activities Should Not Undermine Safe Harbor

The ANPR proposes to impose additional disclosure and other requirements on securitizations. We do not believe that utilizing the legal isolation safe harbor rule to impose these types of substantive requirements on issuers of securitizations is the appropriate way to effect substantive regulation of the securitization market. The FDIC has consistently emphasized the importance of a functioning securitization market, but without an achievable and certain path to legal isolation, issuers will be unable and/or unwilling to utilize securitizations. Consequently, substantive regulation of the securitization market must be achieved in a way that does not adversely impact issuers' ability to achieve legal isolation for the underlying assets. We do not believe that the linkage of safe harbor modification and substantive reform will be consistent with this. In fact, imposing regulatory reforms through the safe harbor may have the effect of destroying the utility of the safe harbor rather than addressing policy goals.

Specifically, we note that Congress and the SEC are currently considering regulatory reform proposals that could impact the structure of securitization transactions, including the disclosure and reporting requirements related thereto. We do not believe the FDIC should impose substantive requirements through the safe harbor that may be inconsistent with the final legislative and/or regulatory standards imposed by these other bodies.

Responses to specific questions raised by the ANPR

Question 2: Do you have any other comments on the transitional safe harbor currently in place until March 31, 2010?

Discover requests that the FDIC clarify that the transitional safe harbor would encompass the full committed amount of beneficial interests that could be issued during the term of a securitization facility so long as the transaction documentation establishing the total commitment amount has been executed prior to expiration of the interim final rule. Discover has consistently managed a portion of its liquidity needs by using asset-backed conduit facilities in which all or a portion of the principal commitment amount of the facilities may be undrawn at closing. We have the

option to draw down the remaining committed principal amount on the facility at any time during its term and we pay an unused commitment fee on that undrawn portion. We, like other issuers, consider this type of partially or completely undrawn conduit financing to be a source of flexible and cost-effective contingent liquidity. If the undrawn portion of these conduits does not qualify under the safe harbor in the interim final rule and we are unable to comply with the conditions of a new safe harbor, or one has not yet been finalized by the expiration of the interim final rule, we may have to choose between accepting the additional cost of fully drawing our facilities prior to the expiration of the safe harbor or losing access to this portion of our contingent liquidity. We believe many other issuers utilize these facilities and will have the same issue related to contingent liquidity.

Question 5: Should there be limits to the number of tranches that can be used for asset classes other than residential mortgage backed securities ("RMBS")? What are the benefits and costs of taking this approach?

Discover believes there should be no limit to the number of tranches that can be used in a securitization of credit card receivables. We, like most credit card issuers, currently use a structure that has four classes of notes—Class A, Class B, Class C, and Class D—but within each class we have the flexibility to issue any number of tranches to reflect market terms at the time of issuance of the tranche. Our underlying assets and our waterfall are the same for all tranches in each class. Credit card securitization structures use subordinate classes to provide efficient credit support to the more senior securities that comprise the most significant portion of our securitization funding. These subordinate classes attract investors who are knowingly seeking increased yield in exchange for more junior cash flow. When we issue multiple tranches within a class, these tranches all receive pari passu distributions of cash flows, and are distinguishable from each other only by their interest rate, maturity date and other market terms. These structures, in which the waterfall typically does not change from year to year, allow investors to make multiple investments in the same asset pool without familiarizing themselves with new documentation and priorities of payment for each investment. In our view, limiting the number of tranches in a credit card securitization would, in addition to making the structure less efficient, also make the documentation for these transactions less uniform and the securities harder to compare against each other.

Question 7: Should securitizations that are unfunded or synthetic securitizations that are not based on assets transferred to the issuing entity or owned by the sponsor be eligible for expedited consent?

Discover requests that the FDIC clarify what is meant by "unfunded securitizations." As stated in our response to Question 2 above, Discover often utilizes conduit financings that include a partially or completely undrawn principal commitment amount. This conduit structure has been attractive to both issuers and investors and does not raise any additional risks to the investors. Consequently, Discover believes there should be no restriction on this form of securitization and that it should qualify for the safe harbor.

<u>Question 10</u>: Should disclosures required for private placements or issuances that are not otherwise required to be registered include the types of information and level of specificity required under SEC Regulation AB or any successor disclosure requirements?

Discover believes that private placements and other non-registered issuances should not be subject to the disclosure standards of Regulation AB. With the exception of two transactions placed in Europe in 1996 and 1998 and our short-term funding certificate program which ran from 2000 to 2005—and in all of which our disclosure mirrored the scope of that in our registered public offerings—we use private placement exclusively in connection with our conduit facilities and transactions with our affiliates. Our conduit investors are highly sophisticated investors that actively negotiate their terms, perform diligence in reliance on information we provide directly to them on a confidential basis, and are represented by their own experienced counsel throughout the transaction. Were we to have to prepare offering documents for our conduit and affiliate transactions, we would incur significant costs that would provide little or no value to any party. We strongly request the FDIC not to add disclosure requirements for private offerings.

<u>Question 13</u>: What type of periodic reports should be provided to investors? Should the reports include detailed information at the asset level? At the pool level? At the tranche level? What asset level is most relevant to investors?

SEC regulations currently require credit card securitization issuers to provide robust and detailed reporting regarding the performance metrics of the collateral within master trusts at the pool and series (tranche) level. Requiring loan level reporting for millions of cardholder accounts would be unduly burdensome on credit card issuers, and this loan level reporting would not be relevant for an asset pool where the balance activity changes daily.

Further, as stated above, Discover believes that it would be inappropriate for the FDIC to use the legal isolation safe harbor to impose additional disclosure and/or reporting requirements for securitization transactions. The safe harbor should promote certainty and contain only those conditions that are readily determinable at the time securities are issued. The terminology and form of disclosure and reporting requirements typically vary by industry and often involve a degree of interpretation, which is inconsistent with the certainty that must be present to ensure an effective safe harbor rule.

Additionally, the SEC has the statutory authority to establish rules and regulations for required disclosures and is currently considering additional disclosure and reporting requirements for securitization transactions. To the extent the FDIC believes additional disclosure and reporting requirements should be implemented, we believe the FDIC should coordinate in the SEC's effort to craft those additional requirements rather than using the safe harbor rule to establish a separate set of disclosure and reporting requirements that would be costly and time consuming for issuers and potentially inconsistent with SEC regulations.

Question 33: Do you have any other comments imposed by paragraphs (b) and (c) of the sample regulatory text?

Section (b)(1(i)(B) says "the securitization may not be unfunded." As stated in our response to Question 2 above, Discover requests that the FDIC clarify that references to "unfunded securitizations" are not intended to include transactions that include a principal amount that is partially or completely undrawn.

Section (c)(1) of the text states that "the transaction shall not be sold predominantly to an affiliate or insider." Discover requests that the FDIC confirm that "predominantly" would not include a structure where a minority of the beneficial interest in the trust is held by an affiliate of the issuer. With respect to Discover's structure, in order to obtain a AAA rating on its most senior securitization issuances, Discover Bank has 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 Discover's securitization trust, the percentage of outstanding securities owned by affiliates of Discover Bank has increased in the past 12-18 months due to the absence of a public market for these subordinated securities. In addition, we typically hold a significant seller's interest in our securitization vehicles to facilitate our 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" that we maintain with respect to our structures.

Section (c)(6) of the text states "the transfer and duties of the sponsor as transferor must be evidenced in a separate agreement from its duties, if any, as servicer, custodian, paying agent, credit support provider or in any other capacity other than transferor." Discover's securitization facility utilizes a Pooling and Servicing Agreement ("PSA") that establishes our master trust and clearly defines and governs Discover Bank's obligations as both transferor and servicer for the facility. The PSA has been one of the key governing documents for our securitization program since October 1993, and we believe that many other issuers in the credit card securitization market utilize this same approach. The PSA is described in the disclosure documentation for Discover's securitization facility and is freely available to investors. Discover does not believe that requiring these duties to be evidenced by separate agreements would provide any additional transparency or protection for investors. Further, satisfying this requirement would require significant time, effort and expense along with the possible additional burden of attaining required certificate and noteholder approval for the necessary amendments to the program documents.

Question 34: Is the scope of the safe harbor provisions in paragraph (d) of the sample regulatory text adequate? If not, what changes would you suggest?

As stated above, Discover believes it is critical that the safe harbor rule provide clear and achievable conditions to establishing legal isolation so that issuers and investors will have certainty that the conditions necessary to satisfy the safe harbor have been achieved at the time a

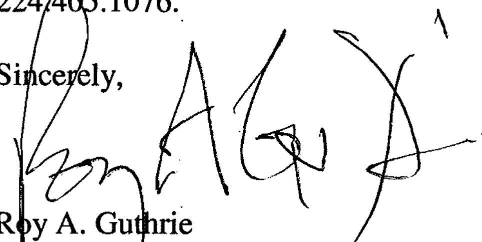
transaction is closed. Many of the requirements in paragraphs (b) and (c) of the sample regulatory text lack clarity and the provisions themselves are not explicit and sufficient in scope to provide the necessary confidence for issuers, investors and rating agencies. The requirements set forth in the sample text are such that even after initial compliance, ongoing compliance is difficult to ascertain.

Additionally, rather than a clear statement of the FDIC's intent to waive its repudiation powers to reclaim assets transferred in a qualifying securitization, the text provides for a much less explicit requirement to pay damages, which limits the effectiveness of the safe harbor. Further, waiving the provisions of the 2006 Amendment to the FDI Act which provides for an "Automatic Stay" of the exercise of rights of a contract to obtain control over property for 45 or 90 days without consent of the conservator or receiver needs to be explicitly defined. Without this waiver, timely payment will be in question given the provisions for remedies in the sample regulatory text.

* * * * * * * * * * *

Discover very much appreciates your consideration of our responses and comments to the questions posed by the ANPR and the views of other industry participants. Should you have any questions concerning our views and recommendations, please do not hesitate to contact me at 224/405.1076.

Sincerely,



Roy A. Guthrie
Executive Vice President and
Chief Financial Officer