Capital One Financial Corporation
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McLean, VA 22102

February 22, 2010

Mr. Robert E. Feldman, Executive Secretary
Attn: Comments
Federal Deposit Insurance Corporation
550 17th Street, NW
Washington, DC 20429
comments@FDIC.gov

Re: Advance Notice Of Proposed Rulemaking Regarding the 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:

Capital One Financial Corporation ("Capital One")[1] welcomes the opportunity provided by the Federal Deposit Insurance Corporation ("FDIC") to comment on the advance notice of proposed rulemaking regarding the treatment by the FDIC as conservator or receiver of financial assets transferred by an insured depository institution in connection with a securitization or participation after March 31, 2010 ("ANPR").

The FDIC, in its role as receiver or conservator for failed insured depository institutions, possesses broad powers to repudiate contracts of failed institutions. In 2000, in response to industry concerns that these powers could be used to disaffirm securitization transaction agreements and reclaim securitized assets, the FDIC issued the "Securitization Rule".[2] This rule provides a safe harbor to off-balance sheet securitizations by confirming legal isolation if all other standards for sale accounting under generally accepted accounting principles ("GAAP") are met by the transfer of financial assets.

With the release of Statements of Financial Accounting Standards No. 166 and 167, application of the safe harbor to most new securitization transactions is unclear. Capital One appreciates the FDIC's efforts to provide clarity regarding safe harbor treatment in connection with

[1] Capital One (www.capitalone.com) is a financial holding company whose subsidiaries, which include Capital One, N.A. and Capital One Bank (USA), N. A., had $115.8 billion in deposits and $212.0 billion in total managed assets outstanding as of December 31, 2009. Headquartered in McLean, Virginia, Capital One offers a broad spectrum of financial products and services to consumers, small businesses and commercial clients. Capital One, N.A. has approximately 1,000 branch locations primarily in New York, New Jersey, Texas, Louisiana, Maryland, Virginia, and the District of Columbia. A Fortune 500 company, Capital One trades on the New York Stock Exchange under the symbol "COF" and is included in the S&P 100 index.
[2] Codified at 12 CFR 360.6.

participations and securitizations issued after March 31, 2010.[3] However, we are concerned with two key aspects of the ANPR:

1) We believe the proposed reforms could be undertaken more effectively through a rule-making process that works in conjunction with other regulators in order to prevent growing uncertainty among key players in the financial markets; and
2) We believe the operational mechanics of the safe harbor, as proposed in the ANPR, do not fully address investor and rating agency concerns about both stay risk and repudiation risk.

We address the first concern in the sections below, while Appendix 1 sets forth our concerns with the currently-proposed safe harbor mechanics. Additionally, while we do not believe that many of the proposed safe harbor conditions, such as restrictions around capital structure and compensation, are relevant to a legal isolation safe harbor determination, in Appendix 2 we do outline our views on some of the questions posed in the ANPR.

The FDIC's Responsibilities as Deposit Insurer and Receiver

The FDIC has the responsibility for the protection of insured depositors and the resolution of failed banks. As such, we appreciate that the FDIC must ensure that loans and other financial assets originated by insured banks are done so in a safe and sound manner. The loosened underwriting of mortgages and certain other consumer loans originated over the past few years resulted in an increase in repurchase demands, losses on MBS and certain ABS, and declines in financial asset values, all of which precipitated the failure of several insured depository institutions and losses to the Deposit Insurance Fund.

Given the FDIC's mandate to protect insured depositors and its fiduciary responsibility to the Deposit Insurance Fund, we understand its caution about the application of the legal isolation safe harbor for securitized assets. While many of the points the FDIC has raised regarding effective regulation of securitizations are important, we believe they should be addressed through a wider, interagency reform effort. However, we do not believe that the application of safe harbor treatment should be altered simply because of a change to a securitization's consolidation status for the purposes of GAAP. Rather, safe harbor treatment should be based on confirmation that securitized assets are truly separate from and not owned by an issuing bank. *(See Appendix 1 for a more detailed discussion on safe harbor mechanics.)*

As such, we fully agree that the requirements laid out in paragraph (c) of the ANPR's preliminary regulatory text must be met for a transaction to be legally isolated from the issuer.

However, we believe many of the conditions proposed in paragraph (b) of the preliminary regulatory text are not relevant to the determination of legal isolation for a securitization transaction and its eligibility for the safe harbor. While we recognize the importance of many of these proposed requirements in the wake of the financial crisis, such as the need for better

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[3] Capital One also appreciates the FDIC's interim final rule issued in November 2009 to provide for safe harbor treatment in connection with participations and securitizations until March 31, 2010.

underwriting and greater transparency, we believe they are more effectively developed and implemented as part of an interagency effort.

Need for Legislative and Interagency Regulatory Coordination

We appreciate that certain securitized products may have encouraged some issuers to focus on fee generation at the expense of sound underwriting. We therefore welcome legislative and regulatory efforts to prevent such practices and to promote a stable, robust securitization market for the future.

One of our key concerns, however, is the threat of regulatory and legislative overload. In addition to the proposals laid out in the ANPR, the banking industry is currently facing, among other proposals, proposed overhauls from the Executive Branch, financial reform bills in the House and Senate, and changes to the Basel liquidity and capital regimes. As financial institutions are required to absorb and respond to these changes, we need to understand if and how they fit together. In order to ensure a sustained recovery from the financial crisis, we believe regulators and legislators should start migrating toward some common ground to avert the rapidly mounting confusion in the financial markets.

At the 2010 annual meeting of the World Economic Forum in Davos, Switzerland, the Institute of International Finance, a leading organization that speaks for international banks and other financial institutions, warned against the rapid proliferation of different proposals from a variety of nations and their respective regulatory and legislative bodies. As reported in the Wall Street Journal, "the Institute reiterated past warnings that regulators should be aware of the cumulative costs of all their separate initiatives—such as boosting bank-capital buffers, increasing the amount of cash and other liquid assets banks must hold, and special taxes—which could combine to constrain bank lending."[4]

Many of the reform proposals contained in the ANPR would be better considered on an interagency basis. The fact that the Deposit Insurance Fund bears the losses of failed banks certainly justifies the important role the FDIC must play in the regulatory reform process of insured banks. However, there are proposals in the ANPR that would appear to fall within the jurisdiction of other regulatory agencies such as the SEC (rules on securities offerings) and therefore there is risk of continued market uncertainty and confusion should the FDIC implement them independently. We believe that a joint effort among regulators could produce a more coordinated and robust regime than one driven in isolation.

In addition to the concerns that attaching unrelated requirements to the legal isolation safe harbor would complicate the regulatory landscape, we believe there would be significant competitive inequities between those institutions covered by the safe harbor and those that do not require its protection. We agree with Comptroller Dugan's assessment at the December 15 FDIC board meeting that unequal treatment of securitization sponsors "would run the risk of driving the market to foreign banks and less regulated financial institutions that are not subject to FDIC

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[4] Stephen Fidler, ***Wall Street Journal***, Coordination Needed: Financial-Industry Group Cites Risks of Mismatched Governmental Reforms, Jan 26, 2010

jurisdiction while at the same time hindering the ability of depository institutions to meaningfully participate to provide additional credit to the economy."

Therefore, we encourage the FDIC to engage not only other domestic regulators so that all U.S. financial institutions follow the same rules, but also international regulatory bodies that govern securitization activities abroad. If well-crafted reforms to securitization can be applied to financial institutions worldwide, the resurgent market will provide ample liquidity to those institutions that need it while at the same time preventing another credit crisis and protecting the Deposit Insurance Fund.

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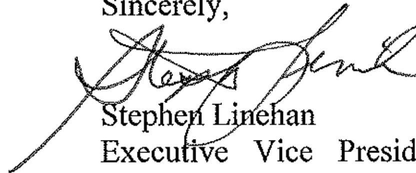
Capital One appreciates the opportunity to comment on this ANPR. If you have any questions about our comments, please contact me at (703) 720-1000.

Sincerely,



Stephen Linehan
Executive Vice President and Treasurer

Appendix 1

We are concerned about a fundamental premise underlying the safe harbor provisions in paragraph (d) of the preliminary regulatory text and, as a result, about the substantive adequacy of the approach taken there. These provisions seem to presume that the legal structure and attributes of a securitization transaction must necessarily be recharacterized based solely on an insured depository institution's ("IDI's") consolidation of the issuing entity for accounting purposes.

This position, in our view, is not supported by any legal precedent or by the accounting literature cited in the ANPR. If adopted by the FDIC, such a position could have grave consequences for the continuing viability of securitization and for trillions of dollars in liquidity on which consumers, homeowners, small businesses, and state and local governments have come to depend.

Our concern stems first from the Supplementary Information in the ANPR, which suggests that an institution's consolidation of a separate entity for accounting purposes results in the legal character of transactions between them being altered or in that entity's legal identity being disregarded. We are troubled most especially by the following statements:

> These accounting changes will require some IDIs to consolidate an issuing entity to which financial assets have been transferred for securitization on to their balance sheets for financial reporting purposes. [Footnote omitted.] Given the likely accounting treatment, securitizations could be considered to be an alternative form of secured borrowing. As a result, the safe harbor provision of the Securitization Rule may not apply to the transfer.
>
> As a result of the changes by FASB, most securitizations will not be treated as sales for accounting purposes. Given this likely accounting treatment, securitizations alternatively could be considered to be a form of secured financing . . . . If a securitization is not given sale accounting treatment under the changes to GAAP, but is treated as a secured financing, section 11(e)(13)(C) could prevent the security holders from recovering monies due to them by up to 90 days in a receivership. During that time, interest on the securitized debt theoretically could remain unpaid.

ANPR, 75 Fed. Reg. at 935.

We are not aware of any legal authority that would support the conclusory statements in the ANPR that that the legal structure and characteristics of a securitization transaction would be recharacterized as a secured financing based solely on the application of Statements of Financial Accounting Standards Nos. 166 and 167. To the contrary, a recent decision by the Delaware Chancery Court highlights that the opposite is true.

In *BASF Corp. v. POSM II Properties Partnership, L.P.*, the inclusion of a subsidiary in its parent's consolidated financial statements was argued to mean that a petrochemical facility being

run by the subsidiary was in fact being operated by the parent. The Delaware Chancery Court concluded differently:

> This line of reasoning is not, well, really reasoning. A holding corporation like LyondellBasell must present reports of their affairs on a consolidated basis. [Footnote omitted.] The fact that holdings corporations do so does not render all their subsidiaries inutile, deprived of all their separate legal dignity. If that were the case, one wonders why large public holding corporations would continue their common practice of running business lines and holding assets through multiple subsidiaries. [Footnote omitted.] After all, simply by making SEC filings, the holding corporation would eliminate its subsidiaries' separate legal existences!

BASF Corp. v. POSM II Properties Partnership, L.P., 2009 WL 522721, *8 (Del. Ch. 2009).

The same principle applies equally to IDIs and their consolidated subsidiaries. The mere fact that an institution consolidates a separate entity onto its balance sheet for accounting purposes does not, under any existing law, alter the character of their transactions or cause the subsidiary's assets and liabilities to become assets and liabilities of the institution.

The only authority cited in support of the position espoused in the ANPR is Paragraph 26A of Statement of Financial Accounting Standards No. 166, which as already noted does not dictate the legal treatment of this same transaction. Specifically, Paragraph 26A provides:

> As a result, in determining whether the transferor has surrendered control over transferred financial assets, the transferor must first consider whether the transferee would be consolidated by the transferor. Therefore, if all other provisions of this Statement are met with respect to a particular transfer, and the transferee would be consolidated by the transferor, then the transferred financial assets would not be treated as having been sold in the financial statements being presented. **However, if the transferee is a consolidated subsidiary of the transferor (its parent), the transferee shall recognize the transferred financial assets in its separate company financial statements, unless the nature of the transfer is a secured borrowing with a pledge of collateral (for example, a repurchase agreement that would not be accounted for as a sale under the provisions of paragraphs 47–49)**.

(Emphasis added.) The bolded text, which follows the language quoted in Footnote 1 of the ANPR, makes clear that financial assets can be sold for accounting purposes to a transferee that is consolidated onto the transferor's balance sheet and that the transferee not only can but must recognize the legal characteristics and consequences of the transaction involving such financial assets on its separate general ledger and other financial statements.

For these reasons, we believe that financial assets can be sold for both legal and accounting purposes even if the transferor and the transferee are consolidated onto a single balance sheet for financial reporting purposes. Therefore, in our view, the application of Statements of Financial Accounting Standards Nos. 166 and 167 alone cannot result in any securitization transaction,

irrespective of its legal characteristics and consequences, being considered "an alternative form of secured borrowing" as contemplated by the ANPR.

What could cause a securitization to be treated in this way, instead, is affirmative action by the FDIC to recharacterize its form and structure and then validation of that action by a court. More specifically, the FDIC could seek to disregard the separate existence of the issuing entity or a subsidiary involved in the securitization or to treat as a secured borrowing any transfer that was intended by the institution to be a sale or a contribution to capital.

Because consolidation for accounting purposes alone does not alter the legal character of a securitization and because a "security interest" approach runs into seemingly insurmountable hurdles, we believe that a different conceptual framework is needed. Specifically, in our view, the FDIC should refrain from seeking to reclaim, recover, or recharacterize as property of an institution or a receivership any financial assets that have been transferred by the institution in connection with a securitization if (i) the institution received adequate consideration for the transfer, (ii) the transfer is perfected under applicable law, (iii) the transferee is duly formed and validly existing under applicable law, and (iv) any consolidated financial statements that include both the institution and the transferee make clear that the transferee is separate from the institution and that the financial assets are not owned by the institution.

This kind of approach, we believe, would be consistent with the FDIC's longstanding recognition that a securitization is not a secured borrowing by an insured depository institution but instead involves the legal isolation of financial assets in a separate entity from which the institution or one of its subsidiaries may acquire a beneficial interest. Such an approach also would function appropriately on a practical level, with the resolution process being more efficiently advanced by repudiating any continuing obligations, administering and realizing on any beneficial interest held by the institution, and otherwise leaving the securitization to wind down.[5]

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[5] In one instance, the Supplementary Information seems to hearken back to these traditional policies and meld the "security interest" approach with the relief provided under the original Securitization Rule:

> The ability of the FDIC as conservator or receiver to reach financial assets transferred by an IDI to an issuing entity in connection with a securitization is limited by the statutory provision prohibiting the conservator or receiver from avoiding a legally enforceable or perfected security interest, except where such an interest is taken in contemplation of insolvency or with the intent to hinder, delay, or defraud the institution or the creditors of such institution. Accordingly, in the case of a securitization that satisfies the standards set forth in the ANPR, the conservator or receiver will not, in the exercise of its statutory repudiation power, attempt to reclaim or recover financial assets transferred by an IDI in connection with a securitization if the financial assets are subject to a legally enforceable and perfected security interest under applicable law.

ANPR, 75 Fed. Reg. at 935.

Appendix 2

As stated in the introduction to this letter, we believe that many of the conditions proposed in the ANPR extend well beyond those that should apply to the FDIC's determination to exercise its statutory repudiation power to reclaim financial assets transferred by an insured depository institution connection with a securitization. We respectfully request that these issues be considered in a more coordinated manner by all US financial regulators and appropriate international regulatory bodies.

We are supportive of the FDIC's suggestion that different rules should apply to different asset classes. Specifically, we believe that many of the requirements contained in the preliminary regulatory text should apply only to RMBS securitizations and not to all other asset classes. Each asset class features different legal and capital structures, has experienced different performance trends, and in general requires a different regulatory approach to promote a safe and robust securitization market. For example, while improved disclosures would encourage investor demand for any asset class, a mandatory delay in compensation for sponsors and third-party service providers may only be necessary for asset classes where participants had previously followed the "originate-to-sell" model of underwriting.

Credit card ABS transactions, which are usually structured as master securitization trusts that hold revolving receivables originated and serviced by the sponsor, present different regulatory issues than RMBS transactions that are structured as discrete, amortizing trusts holding receivables originated by third-parties and serviced by other third-parties. The incentive and ability of credit card ABS sponsors to require strict underwriting are considerably stronger than those of "originate-to-sell" RMBS participants where the defects and misalignment of incentives in the securitization process contributed to the erosion of underwriting standards. Consequently, credit card ABS performed substantially better than RMBS both during and since the financial crisis. These and other differentiators among different asset classes necessitate that new securitization regulations be tailored appropriately, otherwise the regulatory burden of compliance may force issuers to shy away from the securitization market.

Despite these concerns, in an effort to provide reasonable context to the above parties, we offer the below responses to specific questions raised in the ANPR.

General Questions:

2. Is the transition period to March 31, 2010 sufficient to implement the changes required by the conditions identified by Paragraph (b) and (c)? How does this transition period impact existing shelf registrations?

No. Given the extensive and far-reaching conditions outlined in paragraphs (b) and (c) of the sample preliminary text, we do not believe that a transition period ending on March 31, 2010 is long enough for issuers to implement new processes and disclosures. For example, the ANPR requires RMBS issuers to provide loan-level information on, but not limited to, type, structure, maturity and property location. As part of their role in the American Securitization Forum's (ASF) Project RESTART, a broad-based industry-developed initiative to help rebuild investor

confidence in mortgage-backed securities, issuers, originators and servicers have determined that disclosing loan-level information at issuance and monthly thereafter requires substantial operational work and time, with compliance likely taking between 12 and 18 months. Additionally, the provision of loan-level information is not relevant (or possible) for other types of asset-backed securities, such as credit card ABS.

We believe that the transition period should be extended well beyond March 31, 2010. Given the 45-day comment period associated with this ANPR and a similar comment period attached to any resulting NPR, we believe that regulatory deliberations will run significantly past March 31. If there is a gap between the end of the transition period and the publication of a final rule, the securitization market could freeze as it did in October and November before the issuance of the Interim Rule.

Extension of the transition period is also appropriate given the potential impact that regulatory reform legislation could have on any preconditions for the new safe harbor. As Comptroller Dugan indicated in his address to the FDIC Board:

"Key issues and questions raised by the ANPR are also addressed by the financial reform legislation in both Houses of Congress, which could become law in the not-too-distant-future. Those legislative proposals are not the same as an FDIC proposal, however, in that they are less specific, involve other agencies besides those represented on the FDIC board, and would apply across the board to all securitizations, not just those sponsored by insured depository institutions. If that legislation moves to enactment or much closer to enactment, I think we will very much need to take that broader process into account in order to avoid unnecessary overlap or conflicting requirements."[6]

However, it is difficult to determine what such an extension should look like since the ANPR does not set forth an actual proposal. The Board notes in the ANPR that the preliminary regulatory text "should be considered as one example of regulatory text, and not the only option to be considered". Therefore, since we do not know what the ultimate proposal around the safe harbor will be, we cannot currently propose a realistic implementation period.

Capital Structure:

3. Should certain capital structures be ineligible for the future safe harbor? For example, should securitizations that include leveraged tranches that introduce market risks (such as leveraged super senior tranches) be ineligible?

We do not believe that leverage should be a factor in the determination of safe harbor treatment as it is connected with neither legal isolation nor true sale.

4. For RMBS specifically, in order to limit both the complexity and the leverage of RMBS, and therefore the systemic risk introduced by them in the market, should the capital structure of the

6 Statement of John C. Dugan Comptroller of the Currency On the Federal Deposit Insurance Corporation's Advance Notice of Proposed Rulemaking on Securitizations December 15, 2009

securitization be limited to a specified number of tranches? If so, how many, and why? If no more than six tranches were permitted, what would be the potential consequence?

We do not believe that the capital structure of RMBS transactions should be limited to a specific number of tranches. Applying a cookie-cutter regime to RMBS would simply limit the ways in which issuers and originators can meet investor needs. Additionally, we do not believe there is any relationship between structural complexity and asset quality, provided that there is appropriate disclosure about the underlying assets.

5. Should there be similar limits to the number of tranches that can be used for other asset classes? What are the benefits and costs of taking this approach?

We would apply the same rationale given above for other amortizing structures, such as auto loan securitizations, and linked revolving trusts, such as early credit card master trust securitizations. For each of these structures, limiting tranching would limit issuers' ability to meet investor requirements. For delinked revolving trusts, which most large credit card issuers use today, restrictions around tranching simply do not make sense because the trust structure would have already been created when the master trust was launched.

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?

We would like to request some clarification regarding unfunded secured lending commitments from ABCP conduits. In particular, if a securitization issuer opens a funding line with an ABCP conduit issuer before termination of the Interim Rule but does not draw on the line until after termination of the Interim Rule, we would like greater clarity on how the assets securing the drawn amount are treated.

8. Should all securitizations be required to have payments of principal and interest on the obligations primarily dependent on the performance of the financial assets supporting the securitization? Should external credit support be prohibited in order to better realign incentives between underwriting and securitization performance? Are there types of external credit support that should be allowed? Which and why?

We believe that a major regulatory goal, which we fully support, should be to reduce overall risk in the financial system. While principal and interest payments should be largely dependent on underlying collateral, we believe that external credit support has an appropriate place in the system. With enhanced transparency and disclosure, we believe that credit support providers will be better able to model transaction risk and maintain robust, well-balanced risk portfolios. Requiring originators/issuers/sponsors to provide all credit support to a transaction will greatly increase the cost of a securitization, particularly those collateralized by nonprime obligations, thus limiting credit available to consumers.

Disclosures:

9. What are the principal benefits of greater transparency for securitizations? What data is most useful to improve transparency? What data is most valuable to enable investors to analyze the credit quality for the specific assets securitized? Does this differ for different asset classes that are being securitized? If so, how?

For some asset classes, especially RMBS, greater transparency for securitizations may attract investors back to the market, thereby increasing liquidity and preventing further reductions in credit available to consumers and small businesses. Additionally, as investors will be better able to distinguish between high- and low-quality loans, the presence and liquidity of better loan products will naturally increase. The ASF, through collaboration among issuers, originators, credit rating agencies, financial guarantors, primary mortgage insurance companies and investors, has already launched a set of enhanced disclosures and reporting for RMBS via ASF Project RESTART.

Other asset classes will require different types of disclosure than RMBS. For example, industry participants have agreed that loan level disclosure and reporting does not make sense for credit card ABS. Loan level information is not practical for an analysis of a revolving pool of assets in a master trust, which can contain tens of millions of accounts. Furthermore, issuers of credit card ABS believe that producing and auditing loan-level data would be so costly for a master trust issuer that such a requirement could potentially prevent future securitizations by that issuer. As such, it is critically important that any changes to disclosures be recommended following collaboration across the industry and across all asset types.

10. 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 Securities and Exchange Commission Regulation AB, 17 C.F.R. §§ 229.1100-1123, or any successor disclosure requirements?

No. We do not believe that investors that take part in private placements require the same level of disclosure that other investors do. Investors in private placements are typically qualified institutional buyers ("QIBs"), sophisticated investors who have access to the information they need. Requiring the expansion of any disclosures typically required only for public offerings to private placements to QIBs runs the risk of shutting certain issuers out of the capital markets. For example, some issuers, particularly smaller ones who are unable to develop the vast operational framework required for enhanced disclosure, have had to rely entirely on the private placement market since the implementation of Reg AB. Losing these issuers would further constrain market liquidity and the provision of credit to small businesses and consumers.

Additionally, many private placement issuers already provide disclosures that are similar to Reg AB in order to satisfy investor demand for improved disclosure. We believe the market should continue to work by rewarding better disclosure, but that it should not be mandated through regulation.

11. Should qualifying disclosures also include disclosure of the structure of the securitization and the credit and payment performance of the obligations, including the relevant capital or tranche structure? How much detail should be provided regarding the priority of payments, any specific subordination features, as well as any waterfall triggers or priority of payment reversal features?

These items are already disclosed via offering documents as required by Item 1113 and, in certain cases, Item 1114 of Regulation AB.

12. Should the disclosure at issuance also include the representations and warranties made with respect to the financial assets and the remedies for such breach of representations and warranties, including any relevant timeline for cure or repurchase of financial assets.

For asset classes such as auto loan ABS and credit card ABS, representations and warranties, as well as conditions for repurchase, are already disclosed at time of issuance in deal documents. An abridged form of these contractual provisions is usually provided in the related offering documents.

14. Should reports include detailed information on the ongoing performance of each tranche, including losses that were allocated to such tranche and remaining balance of financial assets supporting such tranche as well as the percentage coverage for each tranche in relation to the securitization as a whole? How frequently should such reports be provided?

We believe that monthly servicing reports already provide this information for most consumer ABS.

Compensation

27. Should similar or different provisions be applied to compensation for securitizations of other asset classes?

While the offering and rating processes for other asset classes of ABS are largely similar to those of RMBS, the servicing function for each asset class varies substantially. Residential mortgage servicing of a securitized loan is often performed by an entity unaffiliated with the sponsor of the securitization, and servicing follows the loan regardless of its owner. For credit card ABS, for example, such a framework would have to take into account that the sponsor of a securitization usually performs the servicing function. For card and auto ABS, the servicing fee takes into account all requirements associated with the servicing function. To the extent that the fee does not reflect what a market participant would require to service the portfolio, a servicing asset or liability is booked.

Origination and Retention Requirements

28. For all securitizations, should the sponsor retain at least an economic interest in a material portion of credit risk of the financial assets? If so, what is the appropriate risk retention percentage? Is five percent appropriate? Should the number be higher or lower? Should this vary by asset class or the size of securitization? If so how?

We believe the better way to encourage sound mortgage underwriting is to increase the regulation of mortgage origination. We would note that auto and credit card ABS, which are

collateralized by underlying assets that have been better regulated, have not had the same issues as RMBS.

Mere retention of a portion of credit risk by an originator or securitization sponsor will not necessarily result in improved asset quality. As we have seen over the past several years, many originators and sponsors who held substantial credit risk in securitized assets still suffered significant losses due to the poor underwriting quality of those assets.

Additionally, rigid risk retention requirements conflict with key policy goals, namely the reduction of risk on bank balance sheets and the extension of credit by banks to consumers and small businesses. Furthermore, under new accounting standards FAS 166/167, risk retention requirements would prevent issuers from receiving accounting sale treatment and thus regulatory capital benefits. As Comptroller Dugan noted in his statement to the FDIC Board, "Recent studies note that a policy of requiring a rigid minimum retention requirement risks closing down parts of securitization markets if poorly designed and implemented." These requirements may also have significant pro-cyclical impacts, making it more difficult to fund loans when financial institution balance sheets are stressed by broader economic contraction.

Increased Cost/Reduced Availability of Credit

Requiring originators to retain a significant percentage of credit risk in securitized assets may make funding those assets uneconomical, due to the cost of financing and holding capital against those retained positions. This could limit the ability of the financial system to extend credit to borrowers, particularly non-prime ones. Additionally, depending upon how they are structured, credit risk retention requirements could raise significant accounting and legal true sale issues, further reducing banks' ability to fund consumer and business assets via securitization.

In particular, forced risk retention for mortgages will essentially make it impossible for any future mortgage-backed securitization to receive off-balance sheet treatment. The proposed 5% "skin in the game" requirement would effectively disable the prime non-Agency market because the retained credit risk would exceed (or at least equal) the capital requirements for prime mortgages. This development, in conjunction with other restrictions around securitizations, would push issuing banks toward a portfolio/deposit approach, reducing the supply and increasing the cost of mortgages to the consumer.

Increased Risk

General anti-hedging restrictions may raise safety and soundness issues by interfering with the ability of financial institutions to implement desirable credit risk management practices. Moreover, such restrictions are likely to be ineffective in maintaining an alignment of economic incentives since the risk profiles of retained credit exposures in individual securitizations are likely to change over time.

Regulatory Flexibility

Finally, any retention requirements should take into account differences in securitization structures and asset classes. For example, a credit card issuer that securitizes a portion of its portfolio retains the remainder of that portfolio of assets (or similar assets) on its balance sheet. Additionally, a required percentage of trust assets is also owned by the issuer and has always

been accounted for as on-balance sheet (seller's interest). As such, the issuer's incentives are already substantially aligned with those of its investors.

Therefore, to the extent that regulations are adopted requiring originators and/or sponsors to retain credit risk in securitized assets, we believe that regulators should be able to specify permissible forms of retention. They should also retain the authority to determine the amount of risk retention and whether and to what extent retained credit exposures may be hedged.

29. Should additional requirements to incentivize quality origination practices be applied to RMBS? Is the requirement that the mortgage loans included in the RMBS be originated more than 12 months prior to any transfer for the securitization an effective way to align incentives to promote sound lending? What are the costs and benefits of this approach? What alternatives might provide a more effective approach? What are the implications of such a requirement on credit availability and institutions' liquidity?

We do not believe that requiring banks to maintain mortgage loans on balance sheet for 12 months prior to securitizing them is an effective way to encourage strict underwriting standards. Forcing banks to hold additional capital against these loans for one year will limit the amount of capital that can be put to use in other areas, namely lending to prospective homeowners, small businesses, and other consumers. Additionally, banks will increasingly favor prime borrowers since capital required against prime mortgages is lower than that required for non-prime loans. This requirement, in conjunction with the "skin in the game" requirement, would significantly constrain the amount of credit available to small businesses and consumers, particularly those considered subprime.

32. What are appropriate alternatives? What are the primary benefits and costs of potential approaches to these issues?

We believe alternative mechanisms can help establish an alignment of economic interests between originators and investors that is both more effective than credit risk retention requirements and less likely to cause a restriction in credit.

We would recommend transparent, comprehensive standards whereby investors would be able to execute appropriate quality assurance either on their own or with a third party due diligence provider. More stringent regulatory evaluation of the quality of asset origination and underwriting platforms, including internal policies and controls relating to risk management, fraud protection and detection mechanisms, would further enhance the alignment between issuers and investors.

Significantly, for RMBS the ASF convened a group of issuers, originators, credit rating agencies, financial guarantors, primary mortgage insurance companies and investors to develop more enhanced and transparent representations and warranties. As stated in the December 15, 2009 press release: ***"Without exception, our originator, issuer and investor members view representations and warranties as risk retention for RMBS transactions. We support a 100% repurchase of a loan where its characteristics do not materially conform to the stated characteristics set forth by the originator…Risk retention requirements based on a percentage***

of each loan in a securitization trust do not stand up to a full repurchase of the defective loans at which risk retention requirements are aimed."

The Model RMBS Representations and Warranties released on December 15, 2009 represent a year-long effort to create customary market representations and warranties in the same, transparent language across transactions. Such transparency will provide a standard against which investors and rating agencies can measure the representations and warranties contained in a particular transaction. The Model RMBS Representations and Warranties were also developed to more clearly allocate origination risks between issuers and investors and provide enhanced investor protections over what had been previously provided in "pre-crisis" transactions.[7]

However, card issuers, as indicated in our response to question 28, have always had incentives that are aligned with investors. Given that they only securitize a portion of their card portfolio, maintain seller's interest, as well as a first loss position, there is no need for additional "skin in the game."

Additional Questions

33. Do you have any other comments on the conditions imposed by paragraphs (b) and (c) of the sample preliminary text?

See introduction to this Appendix.

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?

See our discussion in Appendix 1.

35. Do the provisions of paragraph (e) of the sample regulatory text provide adequate clarification of the receiver's agreement to pay monies due under the securitization until monetary default or repudiation? If not, why not and what alternatives would you suggest?

We agree with the spirit of paragraph (e) of the sample regulatory text and believe its inclusion is vital to restoring confidence in a securitization's legal isolation. However, we believe an important step in restoring investor confidence in securitization's legal isolation is for the FDIC to clarify the meaning of "regularly scheduled payments" in the regulatory text. In order to alleviate potential rating agency and investor concerns arising from perceived stay risk, all contractually-required payments, including interest on securitized debt, necessarily should be paid during the duration of the FDIC stay. Accordingly, we believe the FDIC should clarify its reference to "regularly scheduled payments" so that all securitization participants may remain

[7] From the ASF press release: "For these Model Reps to truly be effective, the repurchase process in place for breaches needs to be reformulated. In light of these issues, members of ASF Project RESTART have begun developing a uniform set of procedures (the "Model Repurchase Provisions") to enforce the Model Reps by, among other things, clearly delineating the roles and responsibilities of transaction parties in the repurchase process and allowing greater access into the mortgage loan files so that breaches can be discovered. The ASF hopes to release a request for comment on proposed Model Repurchase Provisions in early 2010."

confident that all payments due under the securitization transaction documents, such as monthly principal and interest payments payable during the receivership, will be paid on their regularly scheduled basis by the FDIC.